GAS NATURAL SDG, S.A. AND ITS SUBSIDIARIES

Audit Report,
Consolidated Annual Accounts and
Directors' Report
as at 31 December 2017

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

Independent auditor´s report on the consolidated annual accounts

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

Report on the consolidated annual accounts

Opinion

We have audited the consolidated annual accounts of Gas Natural SDG, S.A. (the Parent company) and its subsidiaries (the Group), which comprise the balance sheet as at December 31, 2017, and the income statement, statement of other comprehensive income, statement of changes in equity, cash flow statement and related notes, all consolidated, for the year then ended.

In our opinion, the accompanying consolidated annual accounts present fairly, in all material respects, the equity and financial position of the Group as at December 31, 2017, as well as its financial performance and cash flows, all consolidated, for the year then ended, in accordance with International Financial Reporting Standards as adopted by the European Union (IFRS-EU) and other provisions of the financial reporting framework applicable in Spain.

Basis for opinion

We conducted our audit in accordance with legislation governing the audit practice in Spain. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated annual accounts* section of our report.

We are independent of the Group in accordance with the ethical requirements, including those relating to independence, that are relevant to our audit of the consolidated annual accounts in Spain, in accordance with legislation governing the audit practice. In this regard, we have not rendered services other than those relating to the audit of the accounts, and situations or circumstances have not arisen that, in accordance with the provisions of the aforementioned legislation, have affected our necessary independence such that it has been compromised.

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 consolidated annual accounts of the current period. These matters were addressed in the context of our audit of the consolidated annual accounts as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

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Key audit matter	How our audit addressed the key audit matter
Evaluation of Electrificadora del Caribe, S.A. ESP As stated in Note 8 of the accompanying consolidated annual accounts, the Group owns 85.4% of the share capital of Electrificadora del Caribe, S.A. ESP (Electricaribe), engaged in the distribution of electricity in Colombia, which, in the last years, has suffered severe cash problems due to a high number of unpaid invoices of clients and major fraud with electricity consumption. On 14 November 2016, the Superintendency of Residential Public Services of Colombia ordered taking possession of the assets and business of Electricaribe, with its board members being relieved of their duties and an agent appointed to replace the board in its duties. On 11 January 2017 the Superintendency agreed to extend its intervention until 14 March 2017, when it announced its decision to liquidate Electricaribe. On 22 March 2017, the Group submitted the relevant documents to start arbitration proceedings with the Tribunal of the United Nations Commission on International Trade Law (UNICTRAL) to recover the company with a viable regulatory framework or, failing this, to obtain compensation in line with the company's fair value, as stated in Note 8 of the accompanying notes to the consolidated annual accounts. In accordance with IFRS 10 "Consolidated financial statements", the Group concluded that, at 31 December 2016, it no longer controlled this subsidiary and, consequently, it proceeded to deconsolidate it and derecognise its assets and liabilities, and in accordance with IAS 39 "Financial instruments: recognition and measurement", it recognised an investment under the caption "Non current Financial assets" of the consolidated balance sheet as a Financial asset available for sale for €475 million. At 31 December 2017, Gas Natural SDG, S.A.'s Management has reviewed the valuation of the interest and has concluded that there has been no variation to the parameters which the main assumptions refer to. Therefore, the valuation has only changed due to the exchange rate effect and it amounts to €416 million.	We have evaluated the seizure of Electricaribe's assets and business by the Superintendency of Residential Public Services of Colombia from 15 November 2016 and the implications and scope of the agent's functions to analyse the effects of the control of the current majority shareholder on Electricaribe in 2017 and we consider that the conclusions reached by the Group's Management on the loss of control of the company since last year are reasonable in the circumstances. With the collaboration of our experts in valuations, we have also assessed the methodology and main assumptions used to determine the fair value of the investment in Electricaribe. With our team of legal experts on the matter, we have assessed the analysis made by the Group's legal services on the implications of the seizure and the situation of the arbitration proceedings brought by the Group regarding the estimated amount that is reasonably likely to be recognised by the bodies and courts which may decide on a price or compensation in line with the the fair value stated in Note 8, considering the situation of juridical uncertainty commented in this note. Regarding the Group's insurance policy for political risks, we have reviewed the documents exchanged between the Group and the insurance company. We have also assessed whether the information disclosed in the consolidated annual accounts regarding this situation is adequate. On the basis of the work carried out, we can conclude that Management's approach and information is reasonable and is supported by the evidence obtained.

Key audit matter	How our audit addressed the key audit matter
All of these facts have led to an analysis of the situation, the main judgements and estimates made by the Group's Management on the situation and the valuation of the investment in Electricaribe. We therefore consider that its evaluation is a key audit matter.	
Assessment of the recoverability of the carrying amount of certain assets of the Group The accompanying consolidated annual accounts present a goodwill and intangible assets with an indefinite useful life totalling €4,760 and €2,637 million, respectively. These assets, together with the corresponding net operating assets, are allocated to the corresponding cash-generating units (CGUs), as indicated in Notes 5 and 3.4.5 of the accompanying consolidated annual accounts. In addition, as stated in Note 7 of the accompanying consolidated annual accounts, the Group has an investment in Union Fenosa Gas, accounted for by the equity method, whose carrying amount at year end is €925 million. The recoverability of the carrying amount of those assets by CGU, has been determined on the basis of the present value of the cash flows they are expected to generate in the future. These cash flows are calculated on the basis of the business plans approved by Management. The key assumptions are detailed in Note 3.4.5 of the accompanying consolidated annual accounts. Elsewhere, Management carried out a sensitivity analysis, varying the most significant on key assumptions that, based on historical experience, are reasonably likely to suffer changes. As a result of the above analyses, the Group's Management has concluded that no impairment/reversal should be recorded for CGUs where impairment tests have been performed by Management in 2017.	Our analysis begins with the consideration of the adequacy of the allocation made of the assets to the CGUs and the process to identify those that require impairment analysis according to the requirements of accounting regulations. We also checked that the cash flow projections prepared by the Group in the past have been consistently borne out by reality; this included monitoring delivery of the various business plans. In addition, we evaluated the calculation process, concluding that the process used to prepare the calculations is subject to the opportune level of supervision and cross-checking by Management. Elsewhere, with the assistance of our valuation experts, we checked the appropriateness of the valuation models used, the assumptions and estimates used in the calculations, specifically including short- and long-term forecasts for energy prices, tariffs and future regulated income, electricity output volumes, the cost of natural gas supplies, the volume of gas to be procured from suppliers, operation and maintenance costs, required capital expenditure levels, long-term growth expectations and discount rates. We similarly confirmed the mathematical accuracy of the calculations and models prepared and the sensitivity analyses performed by Management and checked the estimated magnitude of change in the key inputs required for the assets to become impaired, factoring in the probability of such change. Lastly, we evaluated the sufficiency of the information disclosed in the consolidated annual accounts with respect to the testing of these assets for impairment.

Key audit matter	How our audit addressed the key audit matter
This is a key audit matter because it implies the use of significant estimates regarding the key assumptions made (which depend on market conditions) in the calculations performed by Management to assess the recoverability of the carrying amount of those assets; were these estimates to differ, the revised estimates could have a significant impact on the Group's consolidated annual accounts.	Based on the procedures performed, we can conclude that the approach taken and information disclosed by Management is reasonable and consistent with the evidence obtained.
Recognition of the sale of Gas Natural, S.A. ESP (Colombia) As stated in Note 9 of the accompanying consolidated annual accounts, on 17 November 2017, the Group announced its agreement to sell the 59.1% interest in Gas Natural, S.A. ESP, a listed company in Colombia. This agreement will be carried out in two stages. Firstly, Gas Natural Fenosa has transferred 17.2% of Gas Natural, S.A. ESP's share capital in several operations carried out on the Colombian stock exchange on 20, 21 and 22 December 2017. The interest in this company has therefore been reduced to approximately 41.9%, which has resulted in a loss of control. At a second stage, to be completed in 2018, the rest of the company's share capital will be transferred by means of a public offer by the purchaser, after certain conditions precedent have been met, including, mainly, the condition that the purchaser obtain certain administrative authorisations in Colombia. The consolidated annual accounts include the profit of the first stage of the transactions totalling €106 million and the effect of the revaluation of the retained interest in accordance with accounting standards, which totals €244 million.	In our audit of the disposal of Gas Natural, S.A.ESP., we have applied the following audit procedures: • Procuring, reading and analysing the purchase-sale contract. • Analysing the sale of 17.2% of the first stage of the operation and its recognition. • Assessing whether the conclusion of the first stage of the operation has led to a loss of control by the Group in Gas Natural, S.A. ESP. based on the percentage of voting rights and number of representatives in the boards of directors. • Analysing the valuation at fair value of the retained interest and whether it is reasonably presented as "Non-current assets held for sale", considering the likelihood that the operation will be completed in 2018. • In addition, we have assessed the presentation of income and expenses of the sold business and related capital gains, as "After-tax profit/(loss) for the year from discontinued operations" of the consolidated income statement in accordance with applicable accounting standards. • Evaluating the disclosures in the consolidated annual accounts for the disposal of Gas Natural, S.A. ESP

Key audit matter	How our audit addressed the key audit matter
The interest retained at year end is presented in "Non-current assets held for sale" by €327 million of the consolidated balance sheet at 31 December 2017, as stated in Note 9 of the accompanying notes to the consolidated annual accounts, as Management considers that the disposal is highly probable. The gas distribution activity in Colombia is a major line of business and therefore the income and expenses for 2017 and 2016 are reported in "After-tax profit/(loss) for the year from discontinued operations" of the consolidated income statement totalling €430 million and €87 million, respectively, and the comparative figures are re-presented in the 2016 consolidated income statement in accordance with Notes 3.4.8 and 9. This transaction is a key audit area as it involves applying critical judgements in assessing the control on the investment and considering the level of the amounts stated. We have therefore considered that this is a key audit issue.	Based on the procedures performed, we consider that Management's accounting treatment of the operation and the disclosures included in the consolidated annual accounts are reasonable.
Recognition of revenue and settlements in regulated businesses As stated in Note 4 of the accompanying consolidated annual accounts, a significant portion of the Group's business activities are subject to comply with sectorial legislation applicable in the various countries where the Group is present. The regulatory framework of the Group's main activities is described in Note 2 of the accompanying consolidated annual accounts. Interpreting the regulatory framework of each country and applying IFRS – EU involves making judgements to estimate income, including certain aggregates of other companies to estimate the global supply charges of the system which should materialise in the corresponding final supply charges. In addition, in past years, the regulatory framework has grown increasingly more complex in several countries, where critical judgements and significant estimates are required to determine these matters (Notes 3.4.19 and 3.4.21.g) in the consolidated notes) This is therefore a key aspect of the audit.	In our audit response for the analysis of the regulatory recognition of income, we firstly gained an understanding of the framework for the activities of the different jurisdictions where the Group has a presence. We have also analysed the regulatory changes made during the year, the regulatory changes approved and their impact on the consolidated annual accounts. We have also verified during the audit process that regulated revenue has been recognized in accordance with the legislation in force in each country by carrying out test of details. Finally, we consider that the information disclosed in the consolidated annual accounts is sufficient with respect to the regulatory framework and its accounting implications. Based on the procedures carried out, the impacts regarding the different regulatory frameworks which the Group is exposed to are adequately reflected in the accompanying consolidated annual accounts.

Key audit matter	How our audit addressed the key audit matter
Evaluation of derivative financial instruments	
As indicated in Notes 3.4.7.3 and 35 of the accompanying consolidated annual accounts, the Group is contractually committed to the purchase of natural gas under long-term arrangements. As is customary practice in the gas sector, those contracts have terms of between 20 and 25 years, involve minimum purchase commitments (take-or-pay clauses under which the buyer undertakes to pay for the minimum volume of gas contracted regardless of whether or not it takes receipt of it) and price review mechanisms indexed to international natural gas prices and natural gas prices in destination markets. These contracts are entered into and maintained with the purpose of covering the Group's expected need to physically receive or deliver natural gas in keeping with regular purchase and sales estimates. As a result, the Group classifies these contracts as 'own use' contracts, thus removing them from the scope of IAS 39 "Financial instruments – recognition and measurement". At 31 December 2017, the Company had entered into commitments for the purchase €71,108 million of natural gas (Note 35). Evaluation of the long-term natural gas supply contracts and specifically concluding whether they can be classified as 'own use' contracts, requires the use of judgement by the Group's Management with respect to supply and demand estimates over the short, medium and long term, the impact of price renegotiation processes, the trend in market prices for natural gas and compliance with the clauses embedded in the contracts. As a result, this is a key audit matter. In addition, as detailed in Note 17, the Group has arranged a number of financial derivative instruments, recognised in the amount of €118 million on the asset side of the balance sheet and €139 million on the liability side. The designation of these instruments as accounting hedges and their measurement requires the use of judgement, documentation and estimates on the part of Management.	Our audit response to this matter included the performance of the following procedures: ▪ Procuring, reading and analysing the natural gas supply contracts entered into by the Group. ▪ Checking that the commitments to buy and sell natural gas in the short and long term are balanced with the aim of confirming that the contracts qualify as 'own use' contracts. ▪ Evaluating the amounts acquired during the year and checking that they met the minimum volumes contracted for. ▪ Analysing the price revision and arbitration proceedings to which the Group is party in order to analyse the magnitude of possible impacts on the consolidated annual accounts by reading the contracts and the available information in the course of meetings with the Group's Management. ▪ Together with our experts in financial derivatives, we analysed the designation of the instruments as accounting hedges and the measurement of the main derivatives. ▪ Lastly, we evaluated the sufficiency of the information disclosed in the consolidated annual accounts with respect to the gas purchase agreements and the derivative financial instruments. Based on the procedures so performed, we can conclude that the measurement and disclosure of the Group's contractual commitments and financial derivative instruments in the accompanying consolidated annual accounts are reasonable.

Other information: Consolidated management report

The other information comprises exclusively the consolidated management report for the year 2017, the formulation of which is the responsibility of the directors of the Parent Company and is not an integral part of the consolidated annual accounts.

Our audit opinion on the consolidated annual accounts does not cover the consolidated management report. Our responsibility for the information contained in the consolidated management report is defined in the regulations governing the audit activity, which establishes two different levels of the same:

a) A specific level that is applicable to the status of non-financial information, as well as to certain information included in the Annual Corporate Governance Report, as defined in art. 35.2. b) of Law 22/2015, on Audit of Accounts, which consists of verifying only that the aforementioned information has been provided in the consolidated management report and, if not, informing about it.

b) A general level applicable to the rest of the information included in the consolidated management report, which consists of evaluating and reporting on the concordance of the aforementioned information with the consolidated annual accounts, based on the knowledge of the entity obtained in the execution of the audit of the aforementioned annual accounts and without including information other than that obtained as evidence during the same, as well as evaluating and reporting whether the content and presentation of this part of the consolidated management report are in accordance with the regulations that result from application. If, based on the work performed, we conclude that there are material misstatements, we are obliged to report them.

Based on the work performed, as described previously, we have verified that the specific information mentioned in section a) above is provided in the consolidated management report and that the rest of the information contained in the consolidated management report agrees with the information of the consolidated annual accounts for the year 2017 and its content and presentation are in accordance with the applicable regulations.

Responsibility of the directors and the audit committee for the consolidated annual accounts

The Parent company´s directors are responsible for the preparation of the accompanying consolidated annual accounts, such that they fairly present the consolidated equity, financial position and financial performance of the Group, in accordance with International Financial Reporting Standards as adopted by the European Union and other provisions of the financial reporting framework applicable to the Group in Spain, and for such internal control as the directors determine is necessary to enable the preparation of consolidated annual accounts that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated annual accounts, the Parent company´s directors are responsible for assessing the Group´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 Group or to cease operations, or have no realistic alternative but to do so.

The Parent company´s audit committee is responsible for overseeing the process of preparation and presentation of the consolidated annual accounts.

Auditor's responsibilities for the audit of the consolidated annual accounts

Our objectives are to obtain reasonable assurance about whether the consolidated annual accounts 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 legislation governing the audit practice 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 consolidated annual accounts.

As part of an audit in accordance with legislation governing the audit practice in Spain, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated annual accounts, 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 Group´s internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Parent company´s directors.

- Conclude on the appropriateness of the Parent company´s 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 Group´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 consolidated annual accounts 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 Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the consolidated annual accounts, including the disclosures, and whether the consolidated annual accounts represent the underlying transactions and events in a manner that achieves fair presentation.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated annual accounts. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Parent company´s audit committee 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 Parent company´s audit committee with a statement that we have complied with relevant ethical requirements, including those relating to independence, and we communicate with the audit committee those matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Parent company´s audit committee, we determine those matters that were of most significance in the audit of the consolidated annual accounts 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

Report to the Parent company´s audit committee

The opinion expressed in this report is consistent with the content of our additional report to the Parent company's audit committee dated 14 February 2018.

Appointment period

The General Ordinary Shareholders' Meeting held on April 20, 2017 appointed us as auditors of the Group for a period of one year, for the year ended December 31, 2017.

Previously, we were appointed by resolution of the General Shareholders' Meeting of June 12, 1990 for the period of 9 years (1990 - 1998), we have been re-elected annually by the General Shareholders' Meeting since then, and we have been performing the work of audit of accounts in an uninterrupted form since the year ended on December 31, 1990.

Services provided

Services provided to the Group for services other than the audit of the accounts, are disclosed in Note 35 to the consolidated annual accounts.

PricewaterhouseCoopers Auditores, S.L. (S0242)

Juan Manuel Anguita Amate (20367)

14 February 2018

Gas Natural Fenosa
2017 Annual Report

CONSOLIDATED ANNUAL ACCOUNTS

Consolidated Balance Sheet
Consolidated Income Statement
Consolidated Statement of Comprehensive Income
Statement of Changes in Consolidated Equity
Consolidated Cash Flow Statement
Notes to the Consolidated Annual Accounts

Gas Natural Fenosa
Consolidated Balance Sheet **(million euro)**

	31.12.2017	31.12.16
ASSETS		
Intangible assets *(Note 5)*	9,921	10,920
Goodwill	4,760	5,036
Other intangible assets	5,161	5,884
Property, plant and equipment *(Note 6)*	22,654	23,627
Investments recorded using the equity method *(Note 7)*	1,500	1,575
Non-current financial assets *(Note 8)*	1,315	1,907
Deferred tax assets *(Note 21)*	849	872
NON-CURRENT ASSETS	**36,239**	**38,901**
Non-current assets held for sale *(Note 9)*	1,682	-
Inventories *(Note 10)*	720	758
Trade and other receivables *(Note 11)*	4,994	4,999
Trade receivables	4,347	4,348
Other receivables	469	489
Current tax assets	178	162
Other current financial assets *(Note 8)*	462	389
Cash and cash equivalents *(Note 12)*	3,225	2,067
CURRENT ASSETS	**11,083**	**8,213**
TOTAL ASSETS	**47,322**	**47,114**
EQUITY AND LIABILITIES		
Capital	1,001	1,001
Share premium	3,808	3,808
Treasury shares	(9)	(21)
Reserves	9,904	9,549
Profit for the period attributed to the parent company	1,360	1,347
Interim dividend	(330)	(330)
Measurement adjustments	(1,000)	(129)
Asset and liability revaluation reserve	(101)	54
Currency translation differences	(899)	(183)
Equity attributed to the parent company	**14,734**	**15,225**
Non-controlling interests	**3,571**	**3,780**
EQUITY *(Note 13)*	**18,305**	**19,005**
Deferred income *(Note 14)*	842	842
Non-current provisions *(Note 15)*	1,129	1,248
Non-current financial liabilities *(Note 16)*	15,916	15,003
Borrowings	15,914	14,997
Other financial liabilities	2	6
Deferred tax liability *(Note 21)*	2,312	2,509
Other non-current liabilities *(Note 18)*	1,210	1,331
NON-CURRENT LIABILITIES	**21,409**	**20,933**
Liabilities related to non-current assets held for sale *(Note 9)*	621	-
Current provisions *(Note 15)*	183	158
Current financial liabilities *(Note 16)*	2,543	2,599
Borrowings	2,477	2,437
Other financial liabilities	66	162
Trade and other payables *(Note 19)*	3,920	4,072
Trade payables	2,885	3,274
Other payables	888	692
Current tax liabilities	147	106
Other current liabilities *(Note 20)*	341	347
CURRENT LIABILITIES	**7,6084**	**7,176**
TOTAL EQUITY AND LIABILITIES	**47,322**	**47,114**

The accompanying Notes 1 to 38 and Appendices are an integral part of the consolidated statements of financial position at 31 December 2017 and 2016.

Gas Natural Fenosa
Consolidated Income Statement **(million euro)**

	2017	**2016(1)**
Sales *(Note 22)*	23,306	21,908
Procurements *(Note 23)*	(16,679)	(14,611)
Other operating income (*Note 24)*	238	240
Personnel costs *(Note 25)*	(1,031)	(974)
Other operating expenses (*Note 26)*	(1,984)	(1,991)
Gain/(loss) on disposals of fixed assets *(Note 27*)	23	51
Release of fixed assets grants to income and others *(Notes 14 and 9)*	42	41
GROSS OPERATING RESULTS	**3,915**	**4,664**
Depreciation, amortisation and impairment expenses (*Notes 5,6 and 9*)	(1,648)	(1,707)
Impairment of credit losses (*Note 11*)	(155)	(315)
Other results (*Note 28)*	-	122
OPERATING PROFIT	**2,112**	**2,764**
Financial income	111	124
Financial expenses	(808)	(937)
Variations in fair value of financial instruments	(2)	(2)
NET FINANCIAL INCOME *(Note 29)*	**(699)**	**(815)**
Profit/(loss) of entities recorded by equity method *(Note 7)*	14	(98)
PROFIT BEFORE TAXES	**1,427**	**1,851**
Corporate income tax *(Note 21)*	(190)	(333)
PROFIT FOR THE YEAR FROM CONTINUING OPERATIONS	**1,237**	**1,518**
Profit for the year from discontinued operations, net of taxes *(Note 9*)	460	193
CONSOLIDATED PROFIT FOR THE YEAR	**1,697**	**1,711**
Attributable to:		
the parent company	1,360	1,347
From continuing operations	932	1,215
From discontinued operations	428	132
Non-controlling interests *(Note 13)*	337	364
Basic and diluted earnings per share in euros from continuing operations attributable to the equity holders of the parent company *(Note 13)*	0.93	1.22
Basic and diluted earnings per share in euros attributable to the equity holders of the parent company *(Note 13)*	1.36	1.35

(1) The consolidated income statement for 2016 has been restated reclassifying to discontinued operations under IFRS 5 (Notes 3.3 and 9).

The accompanying Notes 1 to 38 and Appendices are an integral part of the income consolidated statements statements of financial position for the years ended 31 December 2017 and 2016.

Gas Natural Fenosa
Consolidated Statement of Comprehensive Income (million euro)

	2017	2016
CONSOLIDATED PROFIT FOR THE YEAR	**1,697**	**1,711**
OTHER COMPREHENSIVE INCOME RECOGNISED DIRECTLY IN EQUITY	**(1,052)**	**445**
Items that will not be transferred to profit/(loss):		
Actuarial gains and losses and other adjustments (Note 15)	5	(51)
Tax effect (Note 21)	-	13
Items that will subsequently be transferred to profit/(loss):		
Valuation of available-for-sale financial assets *(Note 8)*	(54)	4
Tax effect valuation of available-for-sale financial assets (Note 21)	-	(1)
Cash flow hedges	(109)	111
Tax effect cash flow hedges (Note 21)	13	(31)
Currency translation differences	(831)	378
Equity-consolidated companies (Note 7)	(76)	22
Cash flow hedges	(4)	2
Tax effect cash flow hedges (Note 21)	-	-
Currency translation differences	(72)	20
RELEASES TO INCOME STATEMENT	**15**	**115**
Valuation of available-for-sale financial assets	-	-
Cash flow hedges	(1)	106
Tax effect cash flow hedges (Note 21)	1	(28)
Currency translation differences	13	32
Equity-consolidated companies (Note 7)	2	5
Cash flow hedges	3	9
Tax effect cash flow hedges (Note 21)	(1)	(2)
Currency translation differences	-	(2)
OTHER COMPREHENSIVE INCOME FOR THE YEAR	**(1,037)**	**560**
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	**660**	**2,271**
Attributable to:		
the parent company	498	1,801
From continuing operations	84	1,650
From discontinued operations	414	151
Non-controlling interests	162	470

The accompanying Notes 1 to 38 and Appendices are an integral part of the consolidated statements of of comprehensive income at 31 December 2017 and 2016.

Gas Natural Fenosa
Statement of Changes in Consolidated Equity (million euro)

	Share Capital	Share premium	Treasury shares	Reserves and retained earnings	Profit for the year	Measurement adjustments	Subtotal	Non-controlling interests	Total Equity
Balance at 01/01/2016	**1,001**	**3,808**	-	**8,669**	**1,502**	**(613)**	**14,367**	**4,151**	**18,518**
Total comprehensive income for the year	-	-	-	(30)	1,347	484	**1,801**	470	**2,271**
Transactions with shareholders or owners	**-**	**-**	**(21)**	**580**	**(1,502)**	**-**	**(943)**	**(783)**	**(1,726)**
Dividend distribution (Note 13)	-	-	-	579	(1,502)	-	**(923)**	(214)	**(1,137)**
Transactions with own shares or equity interests (Note 13)	-	-	(21)	-	-	-	**(21)**	-	**(21)**
Other variations (Note 13)	-	-	-	1	-	-	**1**	(569)	**(568)**
Other net equity variations	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(58)**	**(58)**
Other variations (Note 13)	-	-	-	-	-	-	**-**	(58)	**(58)**
Balance at 31/12/2016	**1,001**	**3,808**	**(21)**	**9,219**	**1,347**	**(129)**	**15,225**	**3,780**	**19,005**
Total comprehensive income for the year	-	-	-	9	1,360	(871)	**498**	162	**660**
Transactions with shareholders or owners	**-**	**-**	**12**	**346**	**(1,347)**	**-**	**(989)**	**(313)**	**(1,302)**
Dividend distribution (Note 13)	-	-	-	346	(1,347)	-	**(1,001)**	(233)	**(1,234)**
Dependent transmission (Nota 13)	-	-	-	-	-	-	**-**	(73)	**(73)**
Transactions with own shares or equity interests (Note 13)	-	-	12	-	-	-	**12**	(8)	**4**
Other variations (Note 13)	-	-	-	-	-	-	**-**	1	**1**
Other net equity variations	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**(58)**	**(58)**
Other variations (Note 13)	-	-	-	-	-	-	**-**	(58)	**(58)**
Balance at 31/12/2017	**1,001**	**3,808**	**(9)**	**9,574**	**1,360**	**(1,000)**	**14,734**	**3,571**	**18,305**

The accompanying Notes 1 to 38 and Appendices are an integral part of the consolidated statements of changes in equity at 31 December 2017 and 2016.

Gas Natural Fenosa
Consolidated Cash Flow Statement **(million euro)**

	2017	2016
Profit before tax	**1,427**	**1,851**
Adjustments to income (Note 30)	**2,543**	**2,727**
Depreciation, amortisation and impairment expenses (Notes 5 and 6)	1,695	1,759
Other adjustments to net profit (Note 30)	848	968
Changes in working capital (Note 30)	**(155)**	**5**
Other cash flow generated from operations (Note 30):	**(1,047)**	**(1,208)**
Interest paid	(686)	(793)
Interest collected	26	31
Dividends collected	48	79
Income tax paid	(435)	(525)
CASH FLOW GENERATED FROM OPERATING ACTIVITIES	**2,768**	**3,375**
Cash flows into investing activities:	**(1,880)**	**(2,556)**
Group companies, associates and business units (Note 30)	(14)	(331)
Property, plant and equipment and intangible assets	(1,774)	(2,147)
Other financial assets	(92)	(78)
Proceeds from divestitures:	**220**	**653**
Group companies, associates and business units (Note 30)	136	405
Property, plant and equipment and intangible assets	39	222
Other financial assets	45	26
Other cash flows from investing activities:	**54**	**49**
Other proceeds from investing activities (Note 14)	54	49
CASH FLOWS FROM INVESTING ACTIVITIES (1)	**(1,606)**	**(1,854)**
Receipts/(payments) for equity instruments:	**5**	**(27)**
Issue (Note 30)	-	-
Acquisition (Note 30)	5	(27)
Receipts and payments on financial liability instruments:	**1,635**	**(243)**
Issue (Note 30)	9,317	7,826
Repayment and amortisation (Note 30)	(7,682)	(8,069)
Dividends paid (and remuneration on other equity instruments (Note 13))	**(1,284)**	**(1,526)**
Other cash flows from financing activities	**(124)**	**(61)**
CASH FLOW GENERATED FROM FINANCING ACTIVITIES	**232**	**(1,857)**
Other changes in cash and cash equivalents (Note 30)	**(116)**	**(42)**
Effect of fluctuations in exchange rates	**(120)**	**55**
VARIATION IN CASH AND CASH EQUIVALENTS	**1,158**	**(323)**
Cash and cash equivalents at beginning of the year (Note 12)	2,067	2,390
Cash and cash equivalents at year end (Note 12)	3,225	2,067

(1) Includes cash flows from continuing and discontinued operations (Note 9).

The accompanying Notes 1 to 38 and Appendices are an integral part of the consolidated statements of of cash flow at 31 December 2017 and 2016.

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Notes to the consolidated annual accounts of Gas Natural Fenosa for 2017

Note 1. General information

Gas Natural SDG, S.A. is a public limited company that was incorporated in 1843. Its registered office is located at Avenida de San Luis 77, Madrid.

Gas Natural SDG, S.A. and its subsidiary companies ("Gas Natural Fenosa") form a group that is mainly engaged in the supply, liquefaction, re-gasification, transport, storage, distribution and commercialisation of natural gas, as well as the generation, transport, distribution and commercialisation of electricity.

Gas Natural Fenosa operates mainly in Spain and also outside Spain, especially in Latin America, in the rest of Europe and Africa.

Note 4 includes financial information by operating segment and geographic area.

Appendix I lists the investee companies of Gas Natural Fenosa.

The shares of Gas Natural SDG, S.A. are listed on the four official Spanish stock exchanges, are traded simultaneously on all four ("mercado continuo"), and form part of the Ibex35.

Note 2. Regulatory framework

2.1. Regulation of the natural gas industry in Spain

<u>Main characteristics of the natural gas industry in Spain</u>

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

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

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

- It is an industry in which regulated and unregulated activities coexist. The regulated activities consist of transport, regasification, storage and distribution of natural gas. The non-regulated activities comprise generation, supply and marketing of natural gas.

- The natural gas sector is almost entirely dependent on foreign supplies of natural gas, which represent almost 99.9% of the natural gas supply in Spain.

- Under EU legislation (Directives 2003/55/CE of June 26, and 98/30/CE of June 22), the supply of natural gas in Spain is totally de-regulated, and all Spanish consumers can freely choose their natural gas provider as from 1 January 2003. The deregulation procedure for the industry has been reinforced substantially by the disappearance as from 1 July 2008 of the bundled tariff of distribution companies and the subsequent right of consumers to participate in the deregulated market (although as indicated further below a tariff of last resort has been maintained for consumers of lower consumption).

Regulation of natural gas activities in Spain

The natural gas activities are divided into: 1) regulated activities: transport, storage, regasification and natural gas distribution; and 2) non-regulated activities: production, supply and commercialisation of natural gas.

2.1.1. Regulated activities

Regulated activities are characterised by:

- *Need for prior government authorisation:* The undertaking of regulated activities requires prior regulated administrative authorisation. In order to obtain this authorisation, the applicant must basically demonstrate its legal, technical and economic capacity to exercise this activity.

- *Remuneration established by legislation:* The general directives that set the remuneration for these activities are governed by Law 18/24 and Royal Decree 949/2001, while the specific remuneration to be received is updated annually by ministerial order.

  Thus, the economic framework of these activities tries to incentivise grid development and allow the companies that undertake them to ensure the recovery of the investments made and the operating costs incurred.

  The regulatory framework for the natural gas industry in Spain has a procedure for settlement compensation amongst companies in the sector for net invoicing of gas acquisition and other costs, so that each company receives the appropriate remuneration for their regulated activities.

- *Subjection to specific obligations of third party access to the network and unbundling:* The carrying out of the regulated activities is subject to specific obligations to ensure the development of competition in marketing. The two main obligations in this sense consist of permitting access by third parties to the transport and distribution pipelines (including re-gasification and storage) and the obligation to keep the regulated and non-regulated activities separate.

  Royal Decree 948/2015, October 30, regulates access by third parties to the network, which is managed by a single telematic platform, as well as the rights and obligations of each person involved in the system, changing the procurement regime capacity established in 2001 by Royal Decree 949/2001. The owners of the transport and distribution pipelines have the right to receive tolls and levies in consideration for this access, which are revised annually under ministerial order.

  The legislation establishes the duty of functional separation, which means not only accounting separation, in order to avoid cross-subsidization and increase the transparency of the calculation of rates, tolls and levies, and legal separation, through separate companies, but also the requirement of independent operation of the regulated subsidiary company in relation to the other companies in the group.

2.1.1.1. Transport

The transport activity includes re-gasification, storage and transport of gas in the strict sense through the basic high pressure gas pipeline network:

- *Re-gasification:* Natural gas is imported to Spain through a pipeline network (in gas form) and by gas tankers (in liquid form, hereon, liquefied natural gas). The re-gasification is the activity that involves the conversion of liquid natural gas, stored in cryogenic tanks generally at re-gasification plants, into a gaseous state, and then pumped into the national gas pipeline network.

- *Transport*: once the natural gas is imported or produced and, if necessary, regasified, it is injected in gas form into the high pressure gas pipeline transport network. The transport network crosses most regions in Spain and transports the natural gas to the major consumers, such as electricity plants and industrial customers and local distributors.

  The transport network is owned mainly by Enagás, S.A., although certain Gas Natural Fenosa companies own a small proportion of it.

- *Storage*: facilities consist basically of underground tanks, which are necessary to ensure a constant supply of natural gas unaffected by seasonal changes and other demand peaks. These facilities also serve to fulfil the obligation established by Royal Decree 1766/2007 (28 December) to maintain minimum security reserves. Prevailing legislation allows unregulated underground storage facilities with third-party access, negotiated and previously authorised by the Spanish Government, although there are currently no such facilities.

  The Resolution of the Secretariat of State for Energy (SEE) laying down the procedure for the assignment of basic underground storage capacity and injection and extraction rights was published on 1 April 2017.

2.1.1.2. Distribution

Natural gas is transported from the high pressure transport pipeline network to the final consumer through the medium and lower pressure transport pipeline network.

The distribution business is based on a system of administrative authorisations that carry no exclusive use rights. A zone distributor has preference to obtain authorisations for adjoining zones.

A distributor's activity is restricted to the expansion and management of distribution networks; it cannot market power because specifically authorised supply companies are entrusted with last-resort supplies, as mentioned in point 2.1.2.2.

Law 18/2014 (17 October) established certain principles and regulations designed mainly to guarantee the gas system's economic and financial sustainability:

- The principle of the gas system's economic and financial sustainability is established, whereby any regulation relating to the sector that entails an increase in costs for the gas system or a reduction in revenue must also bring an equivalent reduction in other cost items or an equivalent increase in revenue to ensure a balance in the system.

- The principle of economic and financial sustainability means that the revenue generated from the use of the facilities must meet all system costs. Gas system revenue will be employed solely to remunerate the regulated activities performed to supply gas.

- Annual mismatches between system costs and revenue are limited and may not exceed 10% of revenue payable for the period; the sum of the annual mismatch and recognised outstanding yearly payments may not exceed 15%. If this sum is exceeded, tolls will be automatically revised to cover the portion that exceeds said limits. The portion of the mismatch which, without exceeding the limits, is not offset by the rise in tolls and charges, will be financed by the parties subject to the settlement system, in proportion to the remuneration applicable to them; they will be entitled to collect mismatch contributions over the following five years and an interest rate will be applied on market terms.

- The remuneration methodologies regulated in the natural gas sector will take into consideration the costs necessary for the activity to be performed by an efficient, well-managed company under the principle whereby the activity must be performed at the lowest possible cost to the system.

- Six-year regulatory periods have been established for the remuneration of regulated activities, allowing for possible adjustments every three years to the system's remuneration parameters (including unit reference values for customers and sales, operating and maintenance costs, etc.) in the event of significant changes to revenue and cost items. Neither the financial yield nor the efficiency ratio may be altered due to productivity improvements during the regulatory period. The first regulatory period will end on 31 December 2020.

- The remuneration system for transmission, regasification and storage facilities is based on consistent principles: use of the asset's net value as a basis for calculating investment remuneration, inclusion of variable remuneration based on gas transported, regasified or stored by asset type, and elimination of all automatic review procedures for values and parameters based on price indices.

- With respect to new secondary transmission facilities, remuneration is included in the remuneration methodology for distribution facilities, linking remuneration to growth in customers and to new demand generated.

- Having regard to distribution facilities, remuneration is maintained for each distribution company and all its facilities based on the number of customers connected and the volume of gas supplied. Automatic reviews are eliminated, and the parametric remuneration formula is stablished to distinguish, in the remuneration category for supplies at pressures equal to or below 4 bars, between consumers with an annual consumption of less than 50 MWh and consumers with a higher consumption, so as to guarantee the adequacy of system revenue at all consumption levels, taking into account toll revenue in each case.

- In order to incentivise network expansion to non-gasified zones and bring remuneration into line with actual costs incurred by companies, different unit values are used depending on whether or not customers are in recently-gasified municipalities.

- As regards the gas system's accumulated deficit at 31 December 2014, it is being recognised. This deficit will be financed by facility owners over a 15-year period; annual payments will be included as a system cost and an interest rate will be recognised on similar terms to market rates.

- The departure relating to remuneration for natural gas under the Algeria contract, supplied through the Maghreb pipeline, and assigned to the tariff market, as a result of the Award issued by the Paris International Court of Arbitration on 9 August 2010, has been recognised in as a system cost. The amount of Euros 164 million will be paid as from 2015 over five years, applying market conditions.

Order ETU/1977/2016 of 23 December 2016 established the remuneration for regulated gas sector activities for 2017. Additionally, this Order updated the tolls and levies for third-party access to gas facilities.

Order ETU/1283/2017 of 22 December 2017 established the remuneration for regulated gas sector activities for 2018.

2.1.2. Unregulated activities

2.1.2.1. Supplies

Taking into account the small volume of natural gas production in Spain, this section will centre on the international supply of natural gas.

Natural gas is supplied in Spain mainly by gas operators such as Gas Natural Fenosa under long-term contracts with gas producers. Although such supplies are not regulated, they are subject to two types of limit, basically to assure supply diversification and competition in the market: 1) no country can supply more than 60% of the gas imported into Spain; and 2) no business person or group can contribute as a whole natural gas for consumption in Spain that is greater than 70% of national consumption, excluding self-consumption.

2.1.2.2. Marketing

Pursuant to 12/2007 Law and its enabling regulations, natural gas is supplied exclusively by supply companies, the former tariff supply operations previously performed by distribution companies having been eliminated. The Law recognises that consumers connected at less than 4 bars who do not exceed a certain consumption threshold (50 MWh/year) are entitled to be supplied at a maximum price referred to as the social tariff or last-resort tariff (TUR).

The TUR calculation includes raw material costs, access tolls, supply costs and supply security costs.

The Ministry of Industry, Energy and Tourism issued Order ITC/1506/2010 (8 June), whereby the last-resort tariff for natural gas will be established in a ruling from the Directorate General for Energy Policy and Mines. The fixed and variable terms of the tariffs will be reviewed when there is a modification of the tolls and levies for access to the system or in the waste coefficients in force. The variable term will be reviewed quarterly, as from the 1st day of the months of January, April, July and October of each year, provided that the cost of raw materials varies upward to downward by 2%.

As regards energy efficiency, Royal Decree-Law 18/2014, stipulates the following:

- The national energy efficiency obligations system is created, whereby gas and electricity supply companies, oil product wholesalers and liquefied petroleum gas wholesalers will be allocated an annual energy-saving quota (saving obligations). Aggregate saving obligations will be equal to the target allocated to Spain in Directive 2012/27/EU.

- The National Energy Efficiency Fund allow the implementation of economic and financial support mechanisms, technical assistance, training and information, or other measures to enhance energy efficiency in different sectors, which are necessary to achieve the Energy Efficiency Directive's objectives.

- The financial equivalence of the saving obligations will be determined based on the average cost of the support mechanisms, incentives and measures required to mobilise the investments necessary to fulfil the annual saving target, through actions by the National Fund, based on the findings of the technical analysis by the Institute for Energy Diversification and Saving.

- The Government is also authorised to establish and develop a final energy savings accreditation system, by issuing Energy Saving Certificates (ESC). Once launched, this will allow companies to progressively fulfil their saving obligations by directly promoting energy efficiency enhancement actions that fulfil the necessary guarantees.

An annual ministerial order stipulates each liable party's obligations to make contributions to the National Energy Efficiency Fund. Order IET/359/2016 of 17 March established obligations in 2016 and Order IET/258/2017 of 24 March established the obligations for 2017.

Law 8/2015 was published on 22 May 2015, amending Law 34/1998 on the Hydrocarbons Sector and regulating certain tax and non-tax measures relating to hydrocarbons exploration, investigation and exploitation. This law creates an organised wholesale market and designates the organised gas market operator; the aim is to integrate, into the organised gas market, activities carried on throughout the Iberian Peninsula, in both Spain and Portugal.

On 31 October 2015, Royal Decree 984/2015, October 30, was published, regulating the organised gas market and third-party access to natural gas system facilities; on 9 December 2015, the Ruling of 4 December 2015 from the Secretary of State for Energy was published, approving market rules, the standard-form contract and the organised gas market rulings. The organised gas market became operational in December 2015, managed by MIBGAS.

In relation to the organised gas market, a resolution of the Council of Ministers dated 10 November 2017 established the obligation for the dominant operators in the natural gas industry, Gas Natural Fenosa and Endesa, to act as mandatory market makers in the organised gas market.(MIBGAS). This obligation means that these operators must continuously present purchase and sale offers in the organised gas market, in order to increase market liquidity. The conditions and requirements for complying with this obligation are set out in the Resolution of the Secretary of State for Energy published on 13 December 2017.

The Resolution of 6 June 2016 of the Secretary of State for Energy was published on 11 June 2015, and approved various provisions concerning the organised gas market, including the figure of market makers, the acquisition of cushion gas for Yela and the acquisition of heel gas and base gas.

The SEE Resolution of 2 August 2016 was published on 5 August 2016, and approved the rules for the management of guarantees in the gas system. This Resolution lays down a standardised model for the provision of guarantees and determines the amount and duration of guarantees for mismatches in the virtual handover point and of guarantees required for contracting capacity, defines the valid instruments for concluding guarantees and, finally, establishes the protocol for communication with the Guarantee Manager and the action protocol in the event of non-compliance.

In addition, The SEE Resolution of 2 August 2016 was published on 5 August 2016, approving the framework contract for access to the facilities of the Spanish gas system. The purpose of the framework contract is for users (supply companies or direct customers in the market) to contract services for accessing the gas system facilities, excluding the contracting of handover point access services, to or from a gas pipeline connection with Europe.

The tariff of last resort (TUR) has fluctuated as follows in 2017:

- On 31 December 2016, the DGPEM Ruling of 29 December 2016 was published, entailing an average 3.5% rise in the TUR applicable as from 01 January 2017.
- On 30 March 2017, the DGPEM Ruling of 24 March 2017 was published, entailing an average 1.8% rise in the TUR applicable as from 01 April 2017.
- On 29 June 2017, the DGPEM Ruling of 28 June 2017 was published, entailing an average 1.0% cut in the TUR applicable as from 01 July 2018.
- On 29 September 2017, the DGPEM Ruling of 25 September 2017 was published, entailing an average 1.3% cut in the TUR applicable as from 01 October 2018.
- On 28 December 2017, the DGPEM Ruling of 26 December 2017 was published, entailing an average 6.2% rise in the TUR applicable as from 01 January 2018.

Concerning supply security, Regulation (EU) 2017/1938 on measures to guarantee the security of the gas supply came into force on 1 November. It lays down reporting requirements for Spanish and European natural gas companies with respect to relevant gas contracts, for supply security reasons. This Regulation also strengthens regional cooperation and lays down a solidarity mechanism which is applicable in the event of a supply crisis in a Member State.

Under a Resolution dated 27 November 2017 a new winter action plan for the operation of the gas system was approved. The purpose of the plan is to guarantee supply in the event of an increase in demand derived from unexpected seasonal supply fluctuations and sudden cold spells. In general terms, it will be applicable from 1 November each year until 31 March of the following year.

In relation to the previous winter plan, the required reserves have been increased and their location has been limited to tanks in regasification plants. On a transitional basis, during the 2017-2018 winter period the stocks equivalent to the previous obligations may be located in underground storage facilities.

On a European level, two regulations have been issued which progress towards the achievement of the internal energy market. On 17 March, Commission Regulation (EU) 2017/459 of 16 March 2017 was published which lays down a network code that defines capacity allocation mechanisms in gas transport networks for existing and incremental capacity through auction arrangements. This regulation applies to interconnection points and may also be applied to points of entry and exit to and from third countries, subject to the decision of the corresponding authority.

Commission Regulation (EU) 2017/460 of 16 March 2017 was also published, establishing a network code which lays down the harmonisation rules for gas transport tariff structures as well as reserve prices for standard capacity products.

The supply of piped liquefied petroleum gas (LPG) is regulated by Law 34/1998 on the oil and gas industry. The MINETAD establishes the selling rates for piped LPG for end consumers and the assignment prices of LPG at which it is purchased by piped LPG distributors, laying down the specific rates or a system for automatically calculating and updating them. These prices are published under monthly resolutions.

2.2. Regulation of the natural gas industry in Latin America

In Brazil, Colombia, Mexico, Argentina and Peru the rates and remuneration of natural gas distribution companies are determined by the regulatory authorities. There are stable regulatory and tariff frameworks that lay down the procedures and formalities necessary for the regular review of rates and distribution margins. This tariff review is carried out every five years (except in Peru, where it is every four years) through the filing of the respective reports with the regulators. In Chile, the tariffs and remuneration of natural gas distribution companies are supervised by the regulatory authorities, and therefore are in line with the maximum regulatory profitability allowed. There are stable regulatory frameworks that define the procedures for supervising tariffs and distribution margins on an annual basis.

In Mexico, all the geographical distribution areas developed by Gas Natural Fenosa (Monterrey, Nuevo Laredo, Toluca, Saltillo, Metrogás (DF) and Bajío) have tariffs approved for the 2016-2020 five-year period. In addition, tariffs have been granted until 2020-21 for the new areas of Nordoeste, Sinaloa and Valle de México, which are under development, as well as new distribution permits for the Tabasco, Campeche and Mérida areas. The regulatory framework in Mexico is under review for its adaptation to the energy reform launched at the end of 2013, which will entail the liberalisation of natural gas supply and marketing activities. For gas distribution, the remuneration methodology is expected to be simplified and made more flexible.

In Brazil, on 30 December 2013, the regulator for Río de Janeiro state approved the new rates for companies of the group CEG and CEG Río, applicable from 1 January 2014 to the end of 2017. In aggregate terms, unit revenue from this activity was maintained. During the second half of 2017, the tariff review process was instigated for the next five years (2018-2022), which is expected to be completed in 2018 with the application of the new rates. In Brazil, the Sao Paulo state regulator is expected to approve new rates during 2018.

The tariff review process in Colombia is still under way. The distributors presented their applications for new rates in October 2015 in accordance with resolution CREG-202-2013, but on 15 July 2016 resolution CREG-93-2016 was published which revoked certain provisions of CREG-202 and shelved the cases filed by the distribution companies for the calculation of the new distribution rates. In Colombia, Resolution CREG 66-2017 was published on 21 June 2017, containing a new proposal for changing the method for remunerating gas distribution within the tariff review process that commenced with the publication of Resolution CREG 202-2013, which approved the gas distribution remuneration methodology. In June 2017, Circular 004-2017 was also published which authorised companies to submit their tariff proposals, in accordance with CREG 66-2017, which following the approval of the CREG, would remain in force until the new rates calculated using the definitive methodology were approved. Finally, in December 2017 the rates of Gas Nacer and Gas Cundiboyacense were approved, under resolutions CREG 176 and 177-2017, respectively.

In Argentina, a resolution establishing new natural gas and propane distribution prices was published on 30 March 2017, urging the regulator, Enargas, to release the tariff lists resulting from the comprehensive tariff review. In addition, on 30 March 2017 Enargas resolution No. I/4354-17 was published, which approved the distribution tariff lists arising from the comprehensive tariff review of Gas Natural BAN, S.A. effective from 1 April 2017, and a rise in the average tariff of 123% compared with the tariff in effect prior to that date. This increase will be applied in stages over the first year of the five-year period (30% in April 2017, 40% in December 2017 and the remaining 30% in April 2018) together with a financial factor that complements it for the purposes of maintaining equivalence between this staged increase and the direct increase in the tariff. On 30 November Enargas approved Resolution No. 122, which lays down the tariff lists that will be applicable as from 1 December 2017. Under this resolution the rates applied since April 2017 have been updated for inflation for the period and the second agreed level, which entails an increase of approximately 61% with respect to the tariff applied since April 2017.

In Chile, rates are freely established by the distributor, which is also the supply company in a way that the annual profitability is lower than a certain rate of profitability established in the recent Sector Law. Profitability is the quotient between the activity margin (sales revenue less activity costs) and the value of the assets. In the event that the profitability obtained exceeds the established rate, the Law would require the Regulator to establish mandatory rates for low-consumption customers.

In Peru the activity commenced during the last quarter of 2017. The applicable rates are defined in the concession contract and will be valid for eight years from the start of the activity, with subsequent quadrennial revisions.

2.3. Regulation of the natural gas industry in Italy

In Italy, the distribution business is regulated while the supply business is fully liberalised. The supply of natural gas can only be made by companies that are not engaged in other activities in the natural gas sector, except import, export, production and wholesaling. There is also an obligatory legal separation of the operator from the distribution system, and limitations on the maximum percentages of supplies and marketing, in order to foster competition and the entry of new operators. By means of Delibera number 573 of December 2013, the Italian Regulator published the distribution rates for the period 2014-2019. There are no fundamental changes in the methodology.

At end-2016 the Regulator instigated a process of discussion with agents for the modification of investments to be made in the future by distributors. This process is still under way.

2.4. Regulation of the Electricity sector in Spain

Main characteristics of the electricity sector in Spain

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

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

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

Generally, the electricity sector has the following main features:

- It is a sector in which regulated and non-regulated activities coexist. The regulated activities consist of transport and electricity distribution. The non-regulated activities comprise generation and sale of electricity.

  Following the directives of EU legislation (Directives 2009/72/CE), all Spanish consumers can freely choose their electricity provider. A regulated tariff system applies to consumers with contracted capacity less than or equal to than 10 kW. This regulated tariff is referred to as the Small Consumer Voluntary Price (PVPC). The last-resort tariff (TUR) also exists as the regulated price which is calculated based on the PVPC and is applicable to consumers classed as vulnerable and to consumers that do not meet requirements to apply the PVPC but are temporarily without a supply company in the free market. The last-resort tariff (TUR) for vulnerable consumers is funded by the social bond which has been assumed, since 23 December 2016 following the publication of Royal Decree-Law 7/2016.

- The electricity consumed in Spain is mostly generated domestically, since the international connections with France, Portugal, Andorra and Morocco have a very small capacity.

- Since July 1, 2007 the Iberian Electricity Market (MIBEL) has begun to operate effectively between Spain and Portugal, which has involved the integration of the electricity systems of both countries (although this integration is still not perfect).

- During the period 2000-2013, the electricity system was not self-sufficient in terms of price, an annual deficit having been generated and financed by the conventional electricity companies, including Gas Natural Fenosa.

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

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

- With respect to the principle of the system's economic and financial sustainability:

    - The principle of the electricity system's economic and financial sustainability is established, which must be in line with the measures taken by the Administration and other relevant parties, whereby any regulation relating to the sector that entails an increase in costs for the electricity system or a reduction in revenue must also bring an equivalent reduction in other cost items or an equivalent increase in revenue to ensure a balance in the system.
    - Mismatches due to a revenue deficit are limited to the extent that they may not exceed 2% of revenues estimated for the reference period and cumulative liabilities due to mismatches may not exceed 5% of those revenues. Should these limits not be observed, the relevant tolls or charges will be reviewed. The portion of the mismatch that is not offset by a rise in tolls and charges shall be financed by the parties subject to the settlement system in proportion to their debt claims arising from the activities performed. The amounts contributed in this way will be reimbursed in the settlements for the following five years, plus applicable interest. Any surplus revenues generated will be used to offset prior-year mismatches; while there are outstanding prior-year liabilities, charges may not be reduced.
    - The principles to be taken into consideration in the remuneration methods for regulated activities are established: transport, distribution, renewables, cogeneration and waste.
    - The remuneration calculation parameters will have a six-year term and will be reviewed prior to the start of the regulatory period taking into account the economic cycle, demand for electricity and an adequate return from these activities.
    - A distinction is made between transport and distribution network access tolls and the charges that are necessary to cover other costs of the relevant system activities, which will be determined using methodology to be established by the Government; in general, tolls and charges will be reviewed annually or in the event of circumstances that have a material impact on regulated costs or on the calculation parameters employed.
    - Small consumer voluntary prices (PVPC) are regulated and will be the same throughout Spain. These prices are defined in line with the prices previously referred to as last-resort tariffs, as the maximum prices that the reference supply companies may charge consumers that avail themselves of the prices. The last-resort tariff (TUR) has become the regulated price applicable to consumers classed as vulnerable and to consumers that do not meet requirements to apply the voluntary price for small consumers but are temporarily without a supply company in the free market.
    - The obligation to keep separate accounting records is extended, applying not only to the separation of electricity activities from non-electricity activities, but also to the separation of production with regulated remuneration activity from non-regulated. This obligation extends to all producers receiving regulated remuneration.

- Electricity generation:

    - The temporary closure of generation facilities is contemplated and will be subject to prior administrative authorisation.

- The daily market system of offers is regulated, with the particularity that all production units must offer their energy in the market, including those operating under the former special regime.
- Electricity demand and contracting, rights and obligations of electricity generators, and specific remuneration regime records are all regulated.
- Self-consumption is regulated, defined as the consumption of electrical energy derived from production facilities associated with a consumer.
- Tolls and charges for the self-consumed energy will be paid in the same terms as that consumed from the network. Consumers applying any self-consumption method will be required to contribute to the system costs and services for the self-consumed energy, paying access tolls, associated charges and costs for the provision of support services.

– Economic and technical management of the system:

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

– Electricity transmission:

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

– Electricity distribution:

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

– Regime for inspections, infringements and penalties:

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

The regulation of electricity activities in Spain

Electricity activities are divided into: 1) regulated activities: electricity transport and distribution; and 2) non-regulated activities: electricity generation and marketing.

2.4.1. Regulated activities

The regulated activities are characterised by the fact that access to them is subject to government authorisation, and remuneration for them is established by law, and undertaking these activities is subject to a series of specific obligations.

- *Need for prior government authorisation:* The undertaking of regulated activities requires prior regulated administrative authorisation. In order to obtain this authorisation, the applicant must basically demonstrate its legal, technical and economic capacity to exercise this activity. The abovementioned authorisation grants a legal monopoly in a given territory, which does not imply an exclusive right of use because of the third-party network access obligation.

- *Remuneration established by legislation:* Royal Decree 1047/2013, December 27, and Royal Decree 1048/2013, December 27, brought in remuneration methods applicable to the transmission and distribution activities, so as to ensure adequate remuneration and network development. The remuneration to be received is updated annually by ministerial order. The financial yield on assets during the first regulatory period, to 31 December 2019, is linked to the yield on government bonds plus a spread of 200 basis points.

  The regulatory framework for the electricity industry in Spain has a procedure for settlement compensation amongst companies in the sector for net invoicing of electricity acquisition and other costs, so that each company receives the appropriate remuneration for their regulated activities.

- *Subjection to specific obligations of third party access to the network and unbundling:* The carrying out of the regulated activities is subject to specific obligations to ensure the development of competition in marketing. The two main obligations in this respect consist of permitting access by third parties to transport and distribution and the obligation to keep regulated and unregulated activities separate.

  Royal Decree 1955/2000 regulates access by third parties to the grid, determining which persons will have access rights, how the application is made, the deadlines for the same, the grounds for rejection of access, as well as the rights and obligations of each person involved in the system.

The legislation establishes the duty of functional separation, which means not only accounting separation, in order to avoid cross-subsidization and increase the transparency of the calculation of rates, tolls and levies, and legal separation, through separate companies, but also the requirement of independent operation of the regulated subsidiary company in relation to the other companies in the group.

2.4.1.1. Transport

Electricity transport links the plants with the distribution networks and specific final customers. The network is owned mainly by REE, although other companies, including Gas Natural Fenosa's subsidiary Unión Fenosa Distribución, S.A., own a small interest on secondary transport network.

The current remuneration framework is determined by Electricity Sector Law 24/2013 and Royal Decree 1047/2013 (27 December), providing the new methodology for calculating electricity transport remuneration, and Order IET/2659/2015 of 11th December which approved standard installations and unitary values of reference for investment, operation and maintenance by fixed asset, which will be used when calculating the remuneration to be paid to the owners of electricity transmission facilities.

Transmission remuneration is laid down annually by the Ministry, which recognises compensation for investment, operation and maintenance, calculated on the basis of the regulatory unitary values of investment, operation and maintenance plus an availability incentive.

2.4.1.2. Distribution

The distribution of electricity includes all activities that bring electricity from the high tension grid to the final consumer.

The current remuneration framework is determined by Electricity Sector Law 24/2013 and Royal Decree 1048/2013 (27 December), providing the methodology for calculating electricity transmission remuneration, and Order IET/2660/2015 of 11th December which approved standard installations and unitary values of reference for investment, operation and maintenance by fixed asset and the unitary remuneration figures for other regulated tasks which will be used when calculating the remuneration to be paid to electricity distribution companies, establishing the definitions for natural growth and relevant power increase and compensation for use and reservation of facilities.

The remuneration is calculated annually by the Ministry and recognises compensation for investment and operation and maintenance of the distribution facilities, as well as other regulated services calculated on the basis of the unitary values approve by regulation, including incentives to reduce network losses, detect fraud and improve service quality.

Ministerial Orders IET/980/2016 and IET/981/2016 were published on 17 June 2016, which lay down the remuneration for electricity distribution companies and for owners of the transmission facilities for 2016. In 29 December 2016 was published on BOE the Order ETU/1976/2016 that set the 2017 access tolls. Accordingly to this Order, the access tolls have remained unchanged.

2.4.2. Unregulated activities

2.4.2.1. Electricity generation

The new Electricity Sector Law 24/2013 of 26 December stipulates that electricity production must be carried on under a free competition regime in the organised market, including both conventional generation and facilities using renewable energies, high-efficiency cogeneration and waste, which must market electricity on the same terms as the conventional plants. However, these facilities (renewable, high-efficiency cogeneration and waste) may have a specific remuneration scheme when an obligation exists to comply with energy targets under European legislation or their introduction entails a reduction in cost or on dependence on foreign sources. These facilities maintain dispatching priority only on equal economic terms with other technologies.

The specific remuneration scheme must be established for new facilities by means of a competitive tender process.

The remuneration of the generation activity is based on electricity market prices of electric production. The electricity generated in the system is sold to the wholesale electricity generation market, regulated by Royal Decree 2019/1997, either in the organised spot market or electricity pool or though bilateral, financial and physical agreements, and forward contracts.

The specific remuneration regime is additional to the revenues from energy sales valued at market price to assure a reasonable yield on the investment over its regulatory useful life.

Order ITC/3127/2011 of 17 November 2011 regulates remuneration in respect of capacity payments, including the incentive for investment in long-term capacity and the medium-term availability service, modifying remuneration for the capacity investment incentive stipulated in Order ITC/2794/2007 of September 27 and regulating the medium-term availability service applicable to marginal technologies in the daily market, i.e. fuel oil plants, combined cycle plants and coal plants, also applicable to pure-pumping, mixed-pumping and reservoir hydraulic plants.

Order ETU/1133/2017 published on November 23 reduces the period of application of the availability service from one year to six months and temporarily excludes pure pumping, mixed pumping and reservoir hydraulic facilities from the scope of application of the availability service, justifying said exclusion due to the scarcity of hydraulic reserves and uncertainty about rainfall levels.

The reduction in the application period is justified by the planned reform of the current capacity mechanisms to adapt them to the European "Clean Energy for all Europeans" legislative package.

In 2013, Law 15/2012, of December 27 on fiscal measures for energy sustainability was published, the principal aspects referring to electricity generation are:

- The establishment of a tax on the value of the production of electrical energy, of a direct type and real nature, imposed on the performance of production activities and incorporation of electricity into the Spanish electricity system. The tax will be applied on the production by all the generation installations at a rate of 7%.

- Two new taxes are regulated: the tax on production of nuclear fuel spent and radioactive residue that are the result of the nuclear generation of electricity and the tax on the storage of nuclear fuel generated and radioactive residue in central installations, with the aim of compensating society for the charges that it must bear as a result of this generation.

- Additionally, the Law revises the tax treatment applicable to the various energy generating products employed in the production of electricity. For electricity generation from fossil fuels, certain exemptions are abolished while the energy products employed for generation and combined cogeneration of heat and electricity are taxed. In particular, a positive rate is established for the use of natural gas in electricity generation and electricity and heat cogeneration, previously regulated at a zero rate, and the tax rate on coal is increased. At the same time, specific tax rates are created for fuels and gas-oils employed in the production of electricity or in the cogeneration of electricity and usable heat.

- A new royalty is applied to public domain assets for the use or exploitation of continental waters for hydroelectric power generation, amounting to 22% of the economic value of hydro-electricity generated; related enabling regulations are included in Royal Decree 198/2015, which develops Article 112.ii) of the revised Water Act and regulates the royalty for the use of continental waters to produce electricity in interregional hydrographic basins. Royal Decree-law 10/2017 published on 10 June 2017 increased the tax rate from 22% to 25.5%.

Revenues from these taxes cover the regulated costs in the electricity system.

European Parliament and Council Directive 2010/75/EU of 2010 on industrial emissions (integrated pollution prevention and control) provides that Member States may draw up a transitional national plan, applicable during the period 1 January 2016 to 30 June 2020, addressing combustion plants that obtained their first permit before 27 November 2002 or whose owners filed an application for a permit before said date, provided that the facility was in operation at the latest on 27 November 2003, indicating the facilities to be included therein.

On 19 October 2013, Royal Decree 815/2013 of October 18 was published, approving the Enabling Regulations on industrial emissions and developing Law 16/2002 of 1 July on integrated pollution prevention and control. The publication of this Royal Decree completed the transposition of the Industrial Emissions Directive into Spanish law. Legislative Royal Decree 1/2016, which approved the revised Law on integrated prevention and control and brought together all the amendments made to Law 16/2002 since 2005 in a single law, was published on 31 December 2016.

The specific remuneration scheme for generation using renewable energies, co-generation and waste was established by Royal Decree 413/2014 of 6 June, the main aspects being:

- Facilities will be classed as standard types (based on technology, capacity, age, etc.), each facility obtaining specific remuneration in accordance with the parameters applicable to each standard type facility.

- Over their regulatory useful lives, the facilities will receive compensation for energy sales on the market calculated at market prices and a specific compensation comprising two terms: a term per unit of installed power which covers, where appropriate, the investment costs for each standard facility that cannot be recovered through sales of energy on the market, called investment remuneration; and a term for operations which covers, as appropriate, the difference between the operating costs and operating income of the standard facility concerned, called operation remuneration.

- The specific remuneration will be sufficient for each standard type facility to obtain an adequate return. This return, before tax, will be similar to the average yield in the secondary market on 10-year government bonds, applying an adequate spread (300 basis points for existing facilities).

- Market prices will generally be applied to future facilities. In exceptional cases, where there is an obligation to fulfil objectives or other exceptional circumstances, a competitive mechanism will be established.

The renewable regulation, in addition to the six-year review of the remuneration parameters, establishes three-year regulatory half-periods for reviewing the specific remuneration of renewable cogeneration and waste facilities based on market prices. In this review, values are calculated with respect to deviations from market prices in relation to those considered at the beginning of the regulatory half-period. Additionally, estimates of future revenues from the sale of energy in the market and the parameters directly related to it for the next regulatory half-period are reviewed, which also effects the specific remuneration for standard facilities.

On 20 June 2014, Order IET/1045/2014, June 16, was published, approving remuneration parameters for facilities, rates applicable to certain facilities generating electricity from renewable sources, cogeneration and waste. In addition, various provisions have approved other standard facilities and their remuneration parameters.

Order ETU/130/2017 of 17 February updates the remuneration parameters of standard facilities for the purposes of their application to the regulatory half-period 2017-2019. This review relates to the update envisaged for the end of each regulatory half-period (every three years) in order to update the future market revenue forecasts and hence the resulting specific remuneration. Adjustments for variances in market price from the previous regulatory half-period are also made.

The remuneration for the operation of standard facilities with half-yearly reviews was updated in the previous regulations for the first half of 2017, while Order ETU/1046/2017 of 27 October updated the remuneration relating to the second half of 2017.

On 21 January 2016 the Resolution of 18 January 2016 of the DGPEM was published, concerning the auction for the assignment of the specific remuneration system for new biomass-based electricity production facilities in the mainland electricity system and for wind technology facilities, under the provisions of Royal Decree 947/2015. 700 MW for both wind and biomass plants was awarded, with the peculiarity that in both cases, the discount was 100% and therefore none of the awardees will receive any compensation for the investment costs.

An auction for the allocation of the specific remuneration scheme was held on 17 May and resolved upon under a Resolution of 19 May 2017, which resulted in the award of 3,000 MW of renewable facilities at no cost for electricity consumers in the benchmark average price scenario. Of the 3000 MW awarded, 2,979 MW pertain to wind installations.

Under a Resolution of 27 July 2017 the procedure for the mainland auction held on 26 July was resolved through the award of 5,037 MW at the maximum discount and, therefore, without any cost for electricity consumers. 3,909 MW were awarded to photovoltaic installations and 1,128 MW to wind installations.

The power awarded in these three auctions amounts to 8,737 MW and must be in operation by 2020.

On 10 November 2017 the European Commission authorised the Spanish system of financial support for electricity production from renewable sources, high-efficiency cogeneration and waste. Accordingly, it is concluded that it complies with EU rules on governing aid.

The SEE Resolution of 16 February 2016 was published on 22 February 2016, laying down the procedure for calculating the actual costs for making the definitive annual settlement of the electricity system for 2012 under Royal Decree 134/2010. Following this Resolution, the final settlement for 2012 can be performed.

Subsequently, the SEE Resolution of 2 August 2016 was published on 12 August 2016, laying down the procedure for calculating the actual costs for the performance of the definitive annual settlement for 2013 under Royal Decree 134/2010. Following this Resolution, the final settlement for 2013 can be performed.

Finally, the SEE Resolution of 19 September 2016 was published on 20 September 2016, laying down the procedure for calculating the actual costs for the performance of the definitive annual settlement for 2014 under Royal Decree 134/2010. Following this Resolution, the final settlement for 2014 can be performed. The amounts due were collected in the first fortnight of December 2016.

The instrument of ratification of the Paris Agreement concluded on 12 December 2015 was published on 2 February 2017. The Paris Agreement comes under the United Nations Framework Convention on Climate Change that establishes measures for the reduction of greenhouse gas (GHG) emissions through the mitigation, adaptation and resilience of global warming effects. Its application will commence in 2020, when the Kyoto Protocol expires.

Order ETU/555/2017 laying down the remuneration parameters for standard facilities applicable to facilities for the treatment and reduction of animal waste approved by Order IET/1045/2014, and which have been updated for the 2017- 2019 half-period, was published on 15 June 2017.

2.4.2.2. Commercialisation of electricity

The commercialisation is based on the principles of deregulated contracting and the customer's choice of provider. Commercialisation, as a deregulated activity, is remunerated at a price freely agreed by the parties.

As mentioned above, as from 1 July 2009 consumers purchasing more than 10 Kw must be supplied by a free market retailer, while those consuming power equal to or lower than 10 Kw have the option to continue buying electricity under the regulated price (last-resort tariff). As from the new Law 24/2013, this regulated tariff is referred to as the Small Consumer Voluntary Price (PVPC), the last-resort tariff (TUR) being the regulated price applicable to consumers classed as vulnerable and to consumers that do not meet requirements to apply the PVPC but are temporarily without a supply company in the free market.

The criteria for setting the last-resort tariff, now PVPC, have been regulated through successive legal provisions. Under the relevant legislation it must incorporate all supply costs, including energy production costs, access tolls and marketing costs.

On 29 March 2014, Royal Decree 216/2014, March 28, was published, providing the methodology for calculating small consumer voluntary prices (PVPC) and the related legal regime for contracting. It determines the structure of small consumer voluntary prices, which will apply to low-voltage consumers with a contracted capacity of up to 10 kW. The Royal Decree also stipulates the procedure for calculating the cost of power generation, which will include the small consumer voluntary price.

The cost of power generation will be calculated based on the daily market hourly price during the billing period. Billing will be performed by the reference supply company based on actual readings and taking into consideration consumption profiles, except for supplies using metering equipment capable of telemetering and telemanagement, effectively integrated into the relevant systems, in which billing will be effected using hourly consumption values.

Alternatively, a consumer may contract a fixed power price for one year with the reference supply company.

Royal Decree-Law 7/2016 amended the wording of Article 45.4 of Law 24/2013 and implemented a new social bond funding scheme under which this public services obligation is only to be funded by parties engaging in electricity marketing, specifically the parent companies of corporate groups engaging in the sale of electrical energy or the companies carrying out this activity that do not form part of any group. The percentage distribution is calculated in proportion to the customers' quotas and will be calculated annually by the CNMC.

On a transitional basis, until the enabling regulations for the new financing system are approved, the percentage share to be financed by each company has been calculated and Gas Natural Fenosa has been allocated 15.84% of the total (8.19% for Gas Natural S.U.R., SDG S.A., 7.44% for Gas Natural Servicios SDG, S.A. and 0.21% for Gas Natural Comercializadora, S.A.).

On 3 October 2017 and 27 December 2017 Order ETU/929/2017 and Order ETU/1288/2017 were published which ordered the reimbursement, by charge to the electricity system surplus, of the amounts paid by Gas Natural SDG as social bond financing in 2014, 2015 and 2016, plus legal interest calculated as from date on which payment was made until the date of its reimbursement.

On 7 October 2017 Royal Decree 897/2017 was published which regulates vulnerable consumers, the social bond and other protection measures for domestic electricity consumers, in compliance with the provisions of Royal Decree Law 7/2016. Order ETU/943/2017 under which said Royal Decree was developed was published on 9 October. The most relevant aspects are:

- Three types of vulnerable consumer are defined according to the kind of income or other circumstances unrelated to income levels: vulnerable consumer, severe vulnerable consumer and severe vulnerable consumer at risk of social exclusion.
- The social bond provides a discount of 25% on the PVPC for vulnerable consumers and 40% for severe vulnerable consumers, up to a consumption limit.
- Supplies to severe vulnerable consumers will not be interrupted in the event that the social services of a public authority finance at least 50% of their bill.
- The criteria and procedures for qualifying for the social bond are revised in terms of income, number of minors in the home and other conditions. The supply company concerned is responsible for processing the application and verifying the requirements.
- The social bond is granted for a period of two years, except for large families in which it lasts until such status expires.
- The procedure for suspending supply in habitual residences is reviewed.

In addition to ruling that the financing mechanism for the social bond is inapplicable, the Supreme Court judgements recognised the right of companies to be reimbursed for the amounts paid in this respect.

2.5. Regulation of the international electricity sector

2.5.1. Generation

Gas Natural Fenosa, through its subsidiary Global Power Generation (GPG), is present as a generator in Mexico, Panama, Costa Rica, the Dominican Republic, Kenya, Puerto Rico and recently in Chile, Brazil and Australia.

In Costa Rica, Kenya and Puerto Rico, the Group's generation operations are subject to the regime for Power Purchase Agreement (PPA) with the sector's domestic companies, Costa Rica Electricity Institute (ICE), Kenya Power and Lighting Company (KPLC) and Puerto Rico Electric Power Authority (PREPA), respectively; all three public corporations vertically integrated and exclusively responsible for transport, distribution and commercialisation.

Generation under the PPA regime also exists in Mexico, with energy being sold to the Federal Commission for Electricity (CFE) and to end-customers under bilateral contracts. Surplus energy is sold on the market created under the energy reform carried out in 2015 and 2016. Additionally, the Bii Hioxo wind farm became operational during 2014, selling the power generated under bilateral contracts to final customers.

In Panama and the Dominican Republic, electricity generated is sold under bilateral contracts with the distributors at market rates.

In Chile, GPG won a tender in August 2016 for generation under a long-term contract scheme (PPA) with distributors (20 years). To meet this commitment, GPG expects to carry out two projects (wind and solar) which will enter service in 2021 with a total installed capacity of approximately 330 MW.

In Australia, GPG was awarded a wind generation project in 2016 through a 20-year contract, with regulated tariffs for energy injected into the system with an installed capacity of 91 MW.

Finally, GPG is also present in Brazil through the acquisition of two renewable solar generation projects with a total capacity of 68 MW involving long-term contracts for the sale of reserve energy to the Chamber for Commercialising Electrical Energy (CCEE), which have already been signed, based on a successful bid in the energy auction held in 2015. These projects have entered into operation during the year 2017.

In all these countries, electricity sector regulations are well-established and stable; legislation is developed and administered by independent regulators.

2.5.2. Distribution

In the countries in which Gas Natural Fenosa is present as a distributor, Argentina, Chile, Colombia, Moldova and Panama, the distribution activity is regulated. The distributors have the function of transporting electricity from the transport network to the customer hook up points and also the function of supplying electricity at regulated rates, to regulated customers, who, based on their consumption volumes, cannot chose their supplier. As for the unregulated customers that choose to purchase electricity from another supplier, they must pay the regulated distribution toll for the use of the networks.

The tariffs are revised periodically to reflect the variations in energy purchase prices and the transport tariffs, as well as the variation in economic indicators.

There are regulatory and tariff frameworks in these countries that lay down the procedures and paperwork necessary for the periodical revision of tariffs and distribution margins. The tariff revision is carried out between four and five years by filing tariff revision applications with the respective regulators.

In Moldova, distribution and supply tariffs will be in force until March 2018. On 15 July 2016 the Regulator approved a Resolution containing the procedure for the recovery of deviations from energy prices that are not passed on to end customers as they should be, in a period of four years. The Resolution was published on 15 July 2016. On 25 October 2016 the last outstanding agreement was concluded with energy generation companies (with the state corporation Energocom), successfully bringing an end to the negotiations with the Moldovan government to recover the debt derived from the failure to reflect real energy purchase prices in electricity rates.

In Moldova, the ANRE ruling was issued on 24 March 2017 with the electricity rates to be applied from that date, which included the tariff supplement relating to the first year in which the tariff variances were recovered although they also included other downward adjustments. Subsequently, the ANRE resolutions introducing changes in the prevailing methodologies for calculating electricity distribution and supply tariffs were published on 5 May 2017.

The distribution and sub-transmission activity in Chile is regulated under a known and stable framework. Tariffs are updated regularly to reflect fluctuations in cost indices and purchase prices, and are revised every four years.

Law 20.936 was published on 20 July 2016, which amended some provisions concerning transmission activities under the Law on Electricity Services and set up an Independent Coordination Body for the National Electricity System. The same law approved a two-year extension for current sub-transmission rates into 2016 and 2017, and therefore the new sub-transmission rates will not enter force until January 2018.

Decree 11T-2016 was published in the Official Gazette on 24 August 2017, which lays down the tariff formulae applicable to electricity distribution end-customers for the period 2016-2020, as well as the amounts applicable to each distribution company. The tariffs will be applied retroactively from 4 November 2016 and will remain in effect until November 2020.

The new Quality Standard for the electricity distribution service was issued in December, which approved more demanding quality indicators and obliged distributors to renew all end-customer measuring devices to bring them into line with new technologies.

Concerning sub-transmission, the new rates should have come into force on 1 January 2018 but the Supreme Decree approving them has not yet been delivered. Once it is, they will be applied retroactively from 1 January 2018 and will remain in force for two years.

In Panama, work on the tariff review commenced in 2017 and the new tariff list will come into effect in July 2018.

Note 3. Basis of presentation and accounting policies

3.1. Basis of presentation

The Consolidated annual accounts of Gas Natural Fenosa for 2016 were adopted by the General Meeting of Shareholders of 20 April 2017.

The consolidated annual accounts for 2017, which were drawn up and signed by the Gas Natural SDG, S.A. Board of Directors on 6 February 2018, will be submitted, along with those of the investee companies, to the approval of the respective General Meetings. It is expected that they will be adopted without modification.

The Consolidated annual accounts of Gas Natural Fenosa for 2017 have been prepared on the basis of the accounting records of Gas Natural SDG, S.A. and the other companies in the Group, in accordance with the provisions of International Financial Reporting Standards adopted by the European Union (hereinafter "IFRS-EU"), as per (EC) Regulation 1606/2002 of the European Parliament and Council.

In the preparation of these consolidated annual accounts the historical cost method has been used, although modified by the criteria for the recognition at fair value of available-for-sale financial assets, derivative financial instruments, business combinations and defined benefit pension plans.

These Consolidated annual accounts fairly present the consolidated equity and consolidated financial situation of Gas Natural Fenosa at 31 December 2017, and the consolidated results of its operations, the Changes in the Consolidated Statement of Comprehensive Income, the Changes in Consolidated Equity and the Consolidated Cash Flows of Gas Natural Fenosa for the year then ended.

The aggregates set out in these Consolidated annual accounts are stated in million euro, unless indicated otherwise.

3.2 New IFRS-EU and IFRIC interpretations

As a result of their approval, publication and coming into force on 1 January 2017 the following standards, interpretations and amendments have been applied:

- IAS 12 (Amendment), "Recognition of deferred tax assets for unrealised losses"; addresses the deferred tax accounting treatment when the tax asset base is bigger than its fair value.

- IAS 7 (Amendment), "Disclosure initiative"; that entities shall provide disclosures that enable users to understand changes in financial liabilities as changes with cash flow movement as expenditure and reimbursement of loans or changes without cash flow movements as acquisitions, disposals and unrealized exchanges differences.

The application of these standards, interpretations and amendments did not have a significant impact on the consolidated annual accounts.

The standards, amendments and interpretations that will come into force for years commencing after 1 January 2018 and later years are described below.

Standards adopted by the European Union		Entry into force for years commencing
IFRS 9, “Financial instruments”	New standard which replaces the classification, measurement, recognition and derecognition requirements for financial assets and liabilities, hedge accounting and impairment contained in IAS 39.	01 January 2018
IFRS 15, “Revenue from contracts with customers”	New revenue recognition standard which replaces IAS 18, IFRIC 15, IFRIC 18 and SIC 31).	01 January 2018
IFRS 4 (Amendment), “Application of IFRS 9 Financial Instruments with IFRS 4 Insurance contracts”	Allows entities within the scope of IFRS 4 the option to apply IFRS 9 or a temporary exemption.	01 January 2018
IFRS 16, “Leases”	New standard that replaces IAS 17.	01 January 2019

None of these standards or amendments has been applied early.

Standards issued by the IASB and yet to be adopted by the European Union		Entry into force for years commencing
IAS 40 (Amendment), “Transfers of investment property”	Clarifies that a reclassification of an investment from or to investment property is only permitted due to a change of use.	01 January 2018
Annual improvements to IFRS, Cycle 2014-2016	Minor changes to various standards.	01 January 2018
IFRS 2 (Amendment), “Classification and measurement of share-based payments”	Clarifies specific issues relating to the accounting of transactions with share-based payments.	01 January 2018
IFRIC 22, “Transactions and advance payments in foreign currency”	Lays down the transaction date for determining the exchange rate in transactions involving foreign currency advances.	01 January 2018
IFRIC 23, “Uncertainty over income tax treatments”	Clarifies the recognition and valuation of IAS 12 in cases of uncertainty as to whether the tax authorities accept a certain tax treatment used by the entity.	01 January 2019
IFRS 9 (Amendment), “Prepayment features with negative compensation”	Enables entities to measure at amortised cost some prepayable financial assets.	01 January 2019
IFRS 10 (Amendment) and IAS 28 (Amendment) "Sale or contribution of assets between an investor and its associates or joint ventures"	These amendments clarify the accounting treatment of sales and asset contributions between an investor and its associates and joint ventures	Postponed without a specific date
IAS 28 (Amendment), "Long-term interests in associates and joint ventures”	Clarifies the application of IFRS 9 to long-term interests in associates or joint ventures when the equity method is not used.	01 January 2019
Annual improvements to IFRS, Cycle 2015-2017	Minor changes to various standards.	01 January 2019
IFRS 17, “Insurance contracts”	New standard that replaces IFRS 4.	01 January 2021

With regard to standards, amendments and interpretations that will come into force for years commencing after 1 January 2018 and based on the analyses carried out to date, Gas Natural Fenosa estimates that only IFRS 9, IFRS 15 and IFRS 16 will have impact on the consolidated annual accounts.

IFRS 9 - “Financial instruments"

IFRS 9 establishes the criteria for the classification, measurement and derecognition of financial assets and liabilities, introduces new rules for hedge accounting and provides a new model for the impairment of financial assets.

Gas Natural has chosen not to adopt the new standard in advance, opting not to restate the comparative information analysis for 2017. Therefore the adjustment to the carrying amount of financial assets and liabilities will be recognised in reserves, at 1 January 2018.

The main expected impacts derived from the initial application of IFRS 9 are as follows:

a) Classification of financial assets: With respect to investments in equity instruments currently classified as available-for-sale financial assets (Note 8), changes in fair value of which are recognised in equity and are taken to income when they are transferred or impairment is recognized, Gas Natural Fenosa expects to utilise these investments, except in the case of Medgaz that remains to be negotiated, the option permitted by the Standard concerning the irrevocable classification in the new category of investments in equity instruments at fair value through other comprehensive income. Increases and decreases in the fair value of these assets will be recorded under “Other accumulated comprehensive income”, impairment losses will not be recognised in results and gains or losses will not be reclassified to the consolidated income state at the time of sale. In addition, in relation to financial assets other than equity instruments, Gas Natural Fenosa holds such assets mainly in order to obtain contractual cash flows and therefore they will continue to be measured at amortised cost as from 1 January 2018.

b) Exchange of debt instruments: Gas Natural Fenosa has carried out refinancing operations in which, in accordance with IAS 39, there have been no substantial variations in the debt instrument and therefore the carrying amount of the liability has been adjusted based on the relevant costs and incurred commissions, which are amortised over the remaining useful life of the adjusted liability. Under IFRS 9, in operations involving changes to financial liabilities it is necessary to determine the current value of the cash flows of the new financial liability calculated using the effective internal rate of return of the former financial liability, recording the difference between the new and original carrying amounts in the consolidated income statement. The approximate impact estimated at 1 January 2018 is a decrease of Euros 48 million in financial liabilities with the corresponding increase in deferred tax liabilities of approximately Euros 12 million.

c) Impairment of financial assets: This involves the application of a new financial asset impairment model based on expected loan losses, unlike the current model under IAS 39 based on the losses incurred. Gas Natural Fenosa will apply the general expected loss model for financial assets with the exception of Trade and other receivables, for which the estimated simplified expected loss model will be used. In this context, Gas Natural Fenosa has taken into account available information on past events (such as customer payment behaviour), current conditions and forward-looking factors (for example, macroeconomic factors as GDP evolution, unemployment, inflation, interest rates…) that could impact the credit risk of the debtors of Gas Natural Fenosa. On the basis of the evaluations carried out to date by Gas Natural Fenosa, the estimated approximate impact as at 1 January 2018 is an increase in the impairment provision for financial assets of approximately Euros 102 million with a corresponding increase in deferred tax assets of approximately Euros 26 million.

d) Hedge accounting: The new hedging rules will align the accounting treatment of hedging instruments more closely with the Group's risk management practices. Gas Natural Fenosa does not expect substantial changes in its hedging model, confirming that its current hedging relationships will qualify as hedges that will continue with the adoption of IFRS 9. The entity intends to apply the new hedging standards from 1 January 2018. In line with the its current hedge accounting policy, Gas Natural Fenosa does not intend to exclude the term component of foreign exchange insurance contracts in the designation of hedging relationships.

e) Other adjustments: These include the estimated impacts due to the adoption of IFRS 9 for the companies recorded using the equity method mainly for the application of the new model of impairment of financial assets based on the expected credit lost and the tax effects of adjustments previously detailed in sections b) and c), recognised as deferred tax assets or liabilities.

In summary, the expected impact of the adoption of IFRS 9 on the consolidated balance sheet at 1 January 2018 is as follows:

	Amount (Million euro)	Adjustments
Investments recorded using the equity method	(23)	e)
Non-current financial assets	(1)	c)
Deferred tax assets	26	c)
NON-CURRENT ASSETS	**2**	
Trade and other receivables	(101)	c)
CURRENT ASSETS	**(101)**	
Non-current financial liabilities	(48)	b)
Deferred tax liabilities	12	b)
NON-CURRENT LIABILITIES	**(36)**	
Equity attributed to the parent company	(50)	
Non-controlling interests	(13)	c)
EQUITY	**(63)**	

The new standard also introduces expanded disclosure requirements and changes in presentation. These are expected to change the nature and scope of the information disclosed by the Group concerning its financial instruments in the period in which the new standard is adopted.

IFRS 15 - "Revenue from contracts with customers"

IFRS 15 concerns the recognition of revenue derived from contracts based on compliance with performance obligations with customers.

Gas Natural has chosen not to adopt the new standard early and has decided not to restate the comparative information for 2017. It will therefore recognise the accumulated effect of the application of the new criteria as an adjustment to reserves at 1 January 2018.

On the other hand, the entity intends to apply the practical solutions that consist in do not consider significant the financing component when the payment period is less than one year and do not adopt the standard in a retrospective way in the contracts that has been completed before 1 January 2018 and recognize the obtaining contracts cost as an expense when its depreciation period is like a year or less.

The expected impacts derived from the initial application of IFRS 15 are as follows:

a) The internal revenue recognition policies for the different types of contracts with customers have been analysed, identifying the performance obligations, transaction price and allocation thereof, in order to identify possible differences with respect to the revenue recognition model under the new standard. No significant differences between them, or performance obligations that lead to the recognition of liabilities due to contracts with customers, have been detected.

b) In accordance with currently applicable criteria, all expenses directly related to obtaining contracts with customers are recorded in the consolidated profit and loss account when they are incurred. In contrast, IFRS 15 requires the recognition of an asset for incremental costs incurred in obtaining such contracts and which are expected to be recovered. They are amortised systematically in the profit and loss account as the income related to the asset concerned is recognised. On the basis of the evaluations conducted to date, Gas Natural Fenosa expects an increase in the volume of assets recognised from intangible assets for the commissions paid in previous years for to the obtainment of contracts of energy supply with customers and still effective at 1 January 2018 totalling approximately Euros 61 million, with the corresponding increase in deferred tax liabilities of approximately Euros 15 million.

In summary, the expected impact of the adoption of IFRS 15 on the consolidated balance sheet at 1 January 2018 is as follows:

	Amount (million euro)	Adjustments
Intangible assets	61	b)
NON-CURRENT ASSETS	**61**	
Deferred tax liabilities	15	b)
NON-CURRENT LIABILITIES	**15**	
Equity attributed to the parent company	46	b)
EQUITY	**46**	

The new standard also introduces expanded disclosure requirements and changes in presentation. These are expected to change the nature and scope of the information disclosed by the Group concerning its financial instruments in the period in which the new standard is adopted.

Estimated impact of IFRS 9 and IFRS 15 on the consolidated balance sheet at 1 January 2018

The estimated effects on the consolidated balance sheet at 1 January 2018 derived from the adoption of IFRS 9 and IFRS 15, explained above, are as follows:

Consolidated balance sheet (million euro)

	1.1.2018	IFRS 9	IFRS 15	Total adjustments	1.1.2018 IFRS 9 and IFRS 15
ASSETS					
NON-CURRENT ASSETS	**36,239**	2	61	**63**	**36,302**
CURRENT ASSETS	**11,083**	(101)	-	**(101)**	**10,982**
TOTAL ASSETS	**47,322**	(99)	61	**(38)**	**47,284**
EQUITY AND LIABILITIES					
Equity attributed to the parent company	14,734	(50)	46	**(4)**	14,730
Non-controlling interests	3,571	(13)	-	**(13)**	3,558
EQUITY	**18,305**	(63)	46	**(17)**	**18,288**
NON-CURRENT LIABILITIES	**21,409**	(36)	15	**(21)**	**21,388**
CURRENT LIABILITIES	**7,608**	-	-	**-**	**7,608**
TOTAL EQUITY AND LIABILITIES	**47,322**	(99)	61	**(38)**	**47,284**

IFRS 16 - "Leases"

IFRS 16 will enter force in 2019 and will replace IAS 17 and the current associated interpretations.

Gas Natural Fenosa has started analysing the impacts of IFRS 16 "Leases", which provides that right-of-use assets and liabilities derived from operating leases must be recognised in the consolidated balance sheet (except for short-term leases and those relating to low-value assets). In addition, there will be a change in the policy for recognising the lease expense, which will be recorded as a depreciation expense for the relevant asset and a financial expense due to the revaluation of the lease liability.

The analysis is still under way at the date of these consolidated annual accounts. Gas Natural Fenosa is gathering the data needed concerning its operating lease contracts to be able to assess the relevant impacts. However, considering the negligible volume of commitments for lease contracts held by the Group (Note 36), Gas Natural Fenosa does not expect IFRS 16 to have a material impact on the consolidated annual accounts.

3.3 Comparability

As a result of the divestments of the gas distribution and supply business in Italy, gas distribution and supply in Colombia, electricity distribution in Moldova and electricity generation in Kenya, described in Note 9 "Non-current assets and disposal groups of assets held for sale and discontinued operations", the income statement for 2016 has been restated for purposes of comparison with the information relating to 2017, in compliance with IFRS 5.

A breakdown of the effects of the restatement on the consolidated income statement for 2016 is as follows:

2016 consolidated income statement

	2016	Application IFRS 5 (Note 9)	2016
Revenue	23,184	(1,276)	21,908
Procurements	(15,420)	809	(14,611)
Other operating income	265	(25)	240
Personnel costs	(1,013)	39	(974)
Other operating expenses	(2,140)	149	(1,991)
Profit/(loss) on disposals of fixed assets	51	-	51
Release of fixed assets grants to income and other	43	(2)	41
GROSS OPERATING RESULTS (EBITDA)	**4,970**	**(306)**	**4,664**
Depreciation, amortisation and impairment expenses (*Notes 5,6 and 9*)	(1,759)	52	(1,707)
Impairment of credit losses (*Note 11*)	(327)	12	(315)
Other results	122	-	122
OPERATING PROFIT	**3,006**	**(242)**	**2,764**
Financial income	131	(7)	124
Financial expenses	(954)	17	(937)
Variations in fair value of financial instruments	(2)	-	(2)
Exchange differences	-		-
NET FINANCIAL INCOME/(EXPENSE)	**(825)**	**10**	**(815)**
Profit/(loss) of companies measured under the equity method	(98)	-	(98)
PROFIT BEFORE TAXES	**2,083**	**(232)**	**1,851**
Corporate income tax	(416)	83	(333)
PROFIT FOR THE YEAR FROM CONTINUING OPERATIONS	**1,667**	**(149)**	**1,518**
Profit for the year from discontinued operations, net of taxes	44	149	193
CONSOLIDATED PROFIT FOR THE YEAR	**1,711**	**-**	**1,711**
Attributable to:			
the parent company	1,347	-	1,347
From continuing operations	1,325	(110)	1,215
From discontinued operations	22	110	132
Non-controlling interests	364		364
Basic and diluted earnings per share in euros from continuing operations attributable to the equity holders of the parent company	1.33	(0.11)	1.22
Basic and diluted earnings per share in euros attributable to the equity holders of the parent company	1.35		1.35

On the other hand, the presentation structure of the consolidated profit and loss account has been modified, presenting in an independent line the deterioration due to credit losses that was previously presented under the heading of other operating expenses. As a result, the comparative information corresponding to the consolidated profit and loss account for 2016 has been modified.

3.4. Accounting policies

The main accounting policies used in the preparation of these consolidated annual accounts have been as follows:

3.4.1 Consolidation

a) Subsidiaries

Subsidiaries are companies controlled by Gas Natural Fenosa. Gas Natural Fenosa controls an entity when, as a result of its involvement, it is exposed or entitled to variable returns and has the capacity to influence those returns through the power exercised in the entity.

Subsidiaries are fully consolidated as from the date on which control is transferred to Gas Natural Fenosa and are excluded from consolidation on the date on which this control ceases.

In order to account for the acquisition of subsidiaries the acquisition method is used. The cost of acquisition is the fair value of the assets delivered of the equity instruments issued and the liabilities incurred and borne on the date of the exchange, the fair value of any additional consideration that depends on future events (provided that they are likely to occur and can be reliably measured).

The intangible assets acquired through a business combination must be recognised separately from goodwill if they met the criteria for asset recognition, whether they are separable or they arise from legal or contractual rights and when their fair value can be reliably measured.

The identifiable assets acquired and the liabilities or contingent liabilities incurred or borne as a result of the transactions are initially stated at their fair value at the date of acquisition, irrespective of the percentage of the non-controlling interest.

For each business combination, Gas Natural Fenosa may opt to recognise any non-controlling interest in the target company at fair value or at the proportional part of the target's net identifiable assets pertaining to the non-controlling interest.

Acquisition costs are expensed in the year when they are incurred.

The surplus cost of the acquisition in relation to the fair value of the shareholding of Gas Natural Fenosa 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 of the subsidiary acquired, the difference is recognised directly in the consolidated income statement.

The measurement period for business combinations begins on the acquisition date and ends when Gas Natural Fenosa concludes that it cannot obtain further information on the events and circumstances that existed at the acquisition date. This period may not in any case exceed one year as from the acquisition date. During the measurement period, the business combination is deemed to be provisional and adjustments to the provisional amount will be recognised, if applicable, as if the business combination had been fully recognised on the acquisition date.

In a business combination achieved in stages, Gas Natural Fenosa values its prior interest in the target's equity at the fair value on the control date, recognising resulting gains or losses in the consolidated income statement.

Inter-company transactions, balances and unrealized gains on transactions between Gas Natural Fenosa companies are eliminated in the consolidation process. Unrealized losses are also eliminated unless the transaction provides evidence of an impairment of the asset transferred.

The shareholding of the minority shareholders in the equity and profit or loss of the subsidiary companies is broken down under “Non-controlling interests” in the consolidated balance sheet and “Profit attributable to non-controlling interests” in the consolidated income statement.

In relation to the acquisitions or sale of shareholdings without loss of control, the difference between the price paid or received and their net carrying value, or as the case may be, the result of their sale, is booked as equity transactions and does not generate either goodwill or profits.

When an investment ceases to be consolidated due to a loss of control any interest retained in the entity is recalculated at fair value with the change in the carrying amount being recognised in the consolidated income statement. This fair value then becomes the initial carrying amount for the purposes of the subsequent recognition of the retained interest as an associate, jointly controlled entity or financial asset. In addition, any amount previously recognised in other comprehensive income in relation to the entity concerned is recorded as if the Group had disposed of the related assets or liabilities directly.

The sale options given to minority shareholders of subsidiary companies in relation to shareholdings in these companies are stated at the current value of the reimbursement, i.e., their exercise price and are carried under "Other liabilities".

b) Joint Arrangements

Joint arrangements are understood as combinations in which there are contractual agreements by virtue of which two or more companies hold an interest in companies that undertake operations or hold assets in such a way that any financial or operating decision is subject to the unanimous consent of the partners.

A joint arrangement is classed as a joint operation if the parties hold rights to its assets and have obligations in respect of its liabilities or as a joint venture if the venturers hold rights only to the investee's net assets.

Interests in joint operations are accounted for by proportionate consolidation method and interests in joint arrangements are recorded under the equity method.

Under the equity consolidation method, interests in joint arrangements are initially recognised at cost and are later adjusted to recognise Gas Natural Fenosa's share of post-acquisition profits and losses and movements in other comprehensive income.

At each reporting date, Gas Natural Fenosa determines whether there is objective evidence of the impairment of its investment in a joint venture. If impairment is identified, Gas Natural Fenosa calculates the amount of the impairment loss as the difference between the joint venture's recoverable amount and carrying amount, recognising it in the item "Profit/(loss) from equity-consolidated companies" in the consolidated income statement.

The assets and liabilities assigned to joint operations are recorded on the consolidated balance sheet in accordance with their nature and proportionally to Gas Natural Fenosa shareholding percentage. The income and expenses from joint operations are reflected in the consolidated income statement in accordance with their nature and proportionally to Gas Natural Fenosa shareholding percentage.

c) Associates

Associates are all entities over which Gas Natural Fenosa has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights.

Investments in associates are accounted under the equity method.

d) Consolidation scope

Appendix I includes the investee companies directly and indirectly owned by Gas Natural Fenosa that have been included in the consolidation scope.

Appendix II lists the main consolidation scope changes in 2017 and 2016, the most relevant being as follows.

2017

In 2017 the main change in scope corresponds to the sale in December 2017 of 17.2% of Gas Natural S.A. ESP and subsidiaries, reducing the percentage holding from 59.1% to 41.9%. As a result of losing the majority of voting rights and members of the Board of Directors Gas Natural S.A. ESP no longer controls the company, which henceforth will be regarded as an associate and will be carried using the equity method (Note 9).

2016

In 2016 the main changes in the consolidation scope related to the sale by Unión Fenosa Gas of the shares in Gasifica, S.A. and Planta de Regasificación de Sagunto, S.A. (Note 7), the sale of the holding in GNL Quintero, S.A. (Note 7), the sale of Gasco S.A. together with the purchase of an additional 37.88% in Gas Natural Chile S.A. (Note 9), the purchase of Vayu Limited (Note 31) and the deconsolidation of the holding in Electricaribe following the loss of control (Note 8).

3.4.2 Transactions in foreign currency

Items included in the financial statements of each of Gas Natural Fenosa's entities are measured using the currency of the primary economic environment in which the entity operates. The Consolidated financial statements are presented in Euros, which is the Gas Natural Fenosa presentational currency.

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at the year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the income statement.

The results and financial position of all Gas Natural Fenosa entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentational currency are translated into the presentational currency as follows:

- Assets and liabilities for each Balance sheet presented are translated at the closing rate at the date of that balance sheet;

- Income and expenses for each Income statement are translated at monthly average exchange rates, unless this average is not a reasonable approximation of the cumulative effect of the rates prevailing on the transaction dates, in which case income and expenses are translated at the rate on the dates of the transactions.

- All the currency translation differences are recognised in the Consolidated Statement of Comprehensive Income, and the cumulate amount under the heading Cumulative translation adjustments in equity.

The adjustments to goodwill and the fair value arising from the acquisition of a foreign company are treated as its assets and liabilities and are translated at the closing exchange rate.

The exchange rates against the euro (EUR) of the main currencies of Gas Natural Fenosa companies at 31 December 2017 and 2016 have been as follows:

	31 December 2017		31 December 2016	
	Closing Rate	Average Accumulated Rate	Closing Rate	Average Accumulated Rate
US Dollar (USD)	1.20	1.13	1.05	1.11
Argentinean Peso (ARS)	22.31	18.71	16.74	16.24
Brazilian Real (BRL)	3.97	3.61	3.44	3.86
Colombian Peso (COP)	3,579	3,337	3,163	3,376
Chilean Peso (CLP)	737.89	732.91	703.32	748.54
Mexican Peso (MXN)	23.67	21.34	21.78	20.66
Panamanian Balboa (PAB)	1.20	1.13	1.05	1.11
Moldovan Lei (MDL)	20.52	20.79	21.01	22.04

3.4.3 Intangible assets

a) Goodwill

Goodwill represents the excess of the cost of an acquisition over the fair value of Gas Natural Fenosa's share of the net identifiable assets of the acquired subsidiary, joint arrangements or associates acquired, at the date of acquisition. Goodwill on acquisitions of subsidiaries or joint arrangements is included in Intangible assets while goodwill related to acquisitions of associates is recorded under Investments using the equity method.

Goodwill derived from acquisitions carried out before 1 January 2004 is recorded at the amount recognized as such in the 31 December 2003 consolidated financial statements prepared using Spanish GAAP.

Goodwill is not amortised and it is tested annually to analyse possible impairment losses. It is recognised in the consolidated balance sheet at cost value less cumulative impairment losses.

The impairment of goodwill cannot be reversed.

b) Concessions under IFRIC 12 and other similar concessions

This heading records the cost of acquisition of concessions if they are acquired directly from a public entity or similar, the fair value attributed to the concession in the event of being acquired as part of a business combination or the cost of construction and improvements of infrastructures assigned to concessions, in accordance with IFRIC 12 "Service concession agreements".

The aforementioned assets related to the service concession agreements under IFRIC 12 are those that the licensor controls the services that Gas Natural Fenosa (operator) must provide and the significant residual stake in the infrastructure at the end of the agreement, are set forth in this section in accordance with the accounting model for intangible assets based on the nature of the economic profits to be received by the operator. The income and expenses on construction services or infrastructure improvements are recognized for their gross amount. Given that concession agreements do not specify remuneration for these concepts, it is assumed that fair value of income corresponds to incurred costs without margin.

The assets included in this accounts are amortised on a straight-line basis over the duration of each concession, except in the case of the Maghreb-Europe pipeline, which, in order to properly reflect the expected consumption scheme for the future economic profits, is based on the value of gas transported during the life of the right of use, which represents accumulated amortisation that is no less than what would be the result of using a straight-line amortisation method.

Furthermore, the concessions for electricity distribution and transmission in Spain and Chile, and the concessions for the gas distribution in Chile acquired, all of them, basically as part of a business combination has no legal or any other type of limit. Accordingly, since we are dealing with intangible assets with an undefined life, they are not amortised, although they are tested for possible impairment annually as per that set out in Note 3.4.5.

c) Computer software

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

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

d) Research costs

Research activities are expensed in the consolidated income statement as incurred.

e) Other intangible assets

Other intangible assets mainly include the following:

- The cost of acquisition of the exclusive re-gasification rights at the re-gasification plant in Peñuelas (Puerto Rico), which are amortised on a straight-line basis until the end of their term (2025).

- The licence costs for renewable generation farms, mainly acquired as part of a business combination, which will be amortised on a straight-line basis over their useful lives.

- Gas supply contracts and other contractual rights purchased as part of a business combination, which are valuated at fair value and amortised over the contract term that does not differ of expected consumption scheme.

There are no intangible assets with an undefined useful life apart from goodwill and the aforementioned concessions for electricity distribution and transmission and the concessions for gas distribution.

3.4.4 Property, plant and equipment

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

a) *Cost*

All property, plant and equipment are presented at cost of acquisition or production, or the value attributed to the asset in the event that it was acquired as part of a business combination.

The financial cost for the technical installation projects until the asset is ready to be brought into use, form part of property, plant and equipment.

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

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

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

The non-extractable gas necessary as a cushion for the exploitation of the underground storage units of natural gas is recorded as Property, plant and equipment ("cushion gas"), and depreciated over the useful life of the underground storage deposit.

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.

The future costs which Gas Natural Fenosa must meet in relation to the closure of certain facilities are included in the value of the assets at the restated value, including the respective provision (Note 3.4.16).

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

b) Depreciation

Assets are depreciated using the straight-line method, over their estimated useful life or, if lower, over the time of the concession agreement. Estimated useful lives are as follows:

	Estimated useful life years
Buildings	33-50
Gas tankers	25-30
Technical installations (pipeline network and transport)	20-40
Technical installations (hydro-electric plants)	14-65
Technical installations (thermal energy plants)	25-40
Technical installations (combined cycle gas turbine: CCGT)	35
Technical installations (nuclear energy plants)	40
Technical installations (wind farms)	25
Technical installations (electricity transmission lines)	30-40
Technical installations (electricity distribution network)	18-40
Computer hardware	4
Vehicles	6
Other	3-20

The hydro-electric plants are subject to the temporary administrative concession regime. Upon termination of the terms established for the administrative concessions, the plants revert to the Government in proper condition, which is achieved by stringent maintenance programs.
In the hydraulic facilities depreciation calculation the different types of elements that make them up are identified, separating investments in civil works (whose depreciation term depends on the period of the concession), the electromechanical equipment (40 years) and the rest of the assets (14 years), in any case according to the use of the plant and with the maximum limit of the concessions term (between the years 2022 and 2063).

Gas Natural Fenosa amortizes its nuclear power plants in a useful life of 40 years that corresponds to the theoretical life of its main components. These facilities operating licences usually covers successive 10-year periods, without being able to request its renewal until a moment close to the completion of each of them. However, considering the optimum performance of these facilities, as well as their maintenance programs, it is considered that the renewal of said permits may be obtained, at least, until reaching the period of 40 years of useful life.

During the first quarter of 2017 Gas Natural Fenosa concluded the technical studies it was carrying out on the estimation of the useful life of combined cycle plants and, in line with the practice followed by the main operators in the industry, the useful life of the combined cycle plants has been changed on a prospective basis from 25 to 35 years, with effect from 1 January 2017. The effect of this estimated useful life change on “Depreciation, amortisation and impairment losses” in the 2017 consolidated income statement is a Euros 87 million reduction in the depreciation charge. It is also expected that from 2018 this modification in the useful life would be a reduction in the annual depreciation similar to that recorded in 2017, and the amount will get less as approaching the end of the useful life of the plants.

Consequently, as from 1 October 2015, Gas Natural Fenosa prospectively adjusted the useful life of its wind farms from the estimated 20 years to 25 years. The effect of this estimated useful life change on the item “Depreciation, amortisation and impairment losses” in the 2015 consolidated income statement was a reduction of Euros 6 million in the depreciation charge.

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

An asset’s carrying amount is written down immediately to its recoverable amount if the asset’s carrying amount is greater than its estimated recoverable amount, i.e., when the asset is no longer useful such as due to a rerouting of the distribution pipeline (Note 3.4.5).

c) Exploration operations and production of gas

Operating costs, excluding drilling costs, are recognised in the income statement as they arise, using the successful-efforts method. If, as a result of test drilling, proven reserves are found that justify commercial development, costs are transferred to investments in zones with reserves; otherwise, they are charged to the income statement.

Costs of investments in zones with reserves are capitalised and depreciated over the estimated commercial life of the gas field, based on the relationship between annual production and proven reserves at the start of the depreciation period.

At the year end, or at any time when there is an indication that there may be asset impairment, the recoverable value is compared to their carrying value.

3.4.5 Asset impairment losses

Assets are tested for impairment provided that an event or change in circumstances indicates that their carrying amount might not be recoverable. Additionally, goodwill and intangible assets not in use or with indefinite useful lives are tested at least annually for impairment.

When the recoverable amount is lower than the asset's carrying amount, an impairment loss is recognised in the consolidated income statement for the difference between both. 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. Gas Natural Fenosa 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).

CGUs are defined using the following criteria:

- Gas distribution:
    - Gas distribution in Spain. The assets of the electricity distribution network in Spain make up a single CGU since the network comprises a group of interrelated assets the development, operation and maintenance of which is managed jointly.
    - Gas distribution in Latin America. A CGU is understood to exist for each country in which there are operations (Argentina, Brazil, Chile, Mexico and Peru) since the businesses are subject to different regulatory frameworks.

- Electricity distribution:

    - Electricity distribution in Spain. The development, operation and maintenance of the electricity distribution network is managed jointly.

    - Electricity distribution in Latin America. A CGU is understood to exist for each country in which there are operations (Argentina, Chile and Panama) since the businesses are subject to different regulatory frameworks.

- Gas. This includes the gas infrastructure and supply CGUs and the interest in Unión Fenosa Gas, which is tested for impairment separately.

- Electricity:

    - Electricity Spain. The power generation park in Spain is managed jointly and is centralised based on conditions of demand, where all power plants using different technologies play a major, complementary and necessary role in light of different market situations, providing the electricity required by customers at any given time. This model focuses, inter alia, on the existence of a single representative and settlement agent vis-á-vis the market, that operates through a single supply room, the entire generation and marketing business being under the same management. Therefore, a single CGU is understood to exist for the generation (including the different conventional and renewable generation technologies) and marketing of electricity in Spain, since they are managed and controlled globally on a centralised basis.

    - Global Power Generation (GPG). A CGU is understood to exist in each country in which there are operations since the businesses are subject to different regulatory frameworks and are managed independently. GPG's power generation park is located in Latin America (Brazil, Costa Rica, Mexico, Panama, Dominican Republic and Puerto Rico, the latter being consolidated using the equity method) and Australia.

- Other. Mainly includes the South African coal field CGU.

- In 2017 the following business lines have been classified as investments held for sale: gas distribution in Italy and Colombia, electricity distribution in Moldova, gas marketing in Italy and generation in Kenya (Note 3.3 and 9).

For those CGUs, requiring testing for impairment, cash flows have been based on the Strategic Plan approved by Gas Natural Fenosa updated by the most recent approved budgets possible, extrapolated for up to five years, on the basis of regulations and expectations regarding the development of the market based on available industry forecasts and historical experience of the performance of prices and output.

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 nominal growth rates used for each CGU or group of CGUs are as follows:

	Growth 2017 (%)	Growth 2016 (%)
Gas distribution in Spain	1.0	1.0
Gas distribution Latin America	1.2-3.0	2.6-3.0
Electricity distribution Spain	1.2	1.2
Electricity distribution Latin America	1.6 -3.0	1.6 -3.0
Unión Fenosa Gas	1.8	1.8
Electricity Spain	2.2	2.2
GPG	1.0-4.0	1.0-4.6
Discontinued operations		
Gas distribution Rest of Europe	n/a	1.0
Electricity distribution Latin America (Colombia)	n/a	3.0
Electricity distribution Rest of Europe	n/a	1.8

The parameters taken into account to determine the above 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 discount rates before tax used to calculate the recoverable value of each CGU or group of CGUs are as follows:

	Rates 2017 (%)	Rates 2016 (%)
Gas distribution in Spain	6.2	6.2
Gas distribution Latin America	10.0-16.0	10.0-17.0
Electricity distribution Spain	5.2	5.2
Electricity distribution Latin America	8.8-9.9	8.8-16.6
Unión Fenosa Gas	13.4	11.9
Electricity Spain	6.3	6.1
GPG	6.5-11.2	5.8-12.8
Discontinued operations		
Gas distribution Rest of Europe	n/a	5.9
Electricity distribution Latin America (Colombia)	n/a	16.6
Electricity distribution Rest of Europe	n/a	14.9

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

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

The Unión Fenosa Gas discount rate, using the same parameters as the above, is calculated taking into account the contribution of each line of business to the consolidated figure of Unión Fenosa Gas.

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

- Gas Distribution in Spain:

  - Regulated remuneration. Amount and growth of the compensation approved by the regulator.

  - Operation and maintenance costs. Estimated from the historical costs of the managed network.

  - Investments. Considering the investments necessary to maintain the regular use of the network and the quality of supply.

- Gas and electricity distribution Latin America

  - 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.

  - Energy cost. 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.

- Electricity distribution in Spain.

  - Regulated remuneration. Amount and increase in remuneration approved by the regulator.

  - Order IET /2660/2015 of 11th December which approved standard installations and unitary values of reference for investment, operation and maintenance by fixed asset and the remuneration for other regulated activities that will be applied in the first regulatory period which will run from 1 January 2016 to 31 December 2019.

  - 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.

- Unión Fenosa Gas:

  - 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.

  - Gas volumes to be obtained from each supply source.

  - Selling price of natural gas. Valued using predictive modelling based on the forecast performance of price curves and experience in the markets where Union Fenosa Gas operates.

- Electricity Spain:

  - Electricity generated. Market demand evolution has been estimated based on the consensus expressed by several international bodies. The share has been estimated based on Gas Natural Fenosa's market share in each technology and on the expected evolution of each technology's share of the total market.

  - Electricity price. Market electricity prices used have been calculated using models that cross expected demand with supply forecasts, taking into account the foreseeable evolution of generation capacity in Spain, based on sector forecasts.

- Fuel costs. Estimated by reference to long-term supply contracts concluded by Gas Natural Fenosa, the forecast evolution of price curves and market experience.

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

- Taxes laid down in Law 15/2012 (Note 2.4.2.1).

- Global Power Generation (GPG):

  - 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.

As a result of the above process, in 2017 the recoverable values of the CGUs' assets, calculated using the methodology described, were, except for the interest in Union Fenosa Gas higher than the carrying amounts recognised in these consolidated annual accounts.

In 2016 the impairment tests performed did not reveal the need to recognise additional impairment or reverse impairment recognised in the previous year, except for the holding in Unión Fenosa Gas, for which impairment was recognised (Note 7).

Gas Natural Fenosa 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 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 and gas supply costs	5%	-
Rate/ remuneration performance	-	5%
Operating and maintenance costs	5%	-
Investments	5%	-

These sensitivity analyses performed for each basic assumption independently would not alter the conclusions obtained as regards the recoverable amount being higher than CGUs' carrying amount except in the case of Unión Fenosa Gas (Note 7) whose recoverable value is roughly equivalent to its carrying amount; therefore, any negative change in the assumptions would result in the recoverable value being lower than the carrying amount. Therefore, a 50 basis point increase in the discount rate, without any change in the assumptions, would entail an impairment for Unión Fenosa Gas of Euros 58 million.

3.4.6 Financial assets and liabilities

Investments

Purchases and sales of investments are recognized on trade-date, which is the date on which Gas Natural Fenosa commits to purchase or sell the asset, and are classified under the following categories:

a) Loans and receivables

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

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

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

b) Held-to-maturity financial assets

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

c) Financial assets at fair value through profit of loss

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

d) Available for sale financial assets

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

They are recognised at fair value. Unrealised gains and losses that arise from changes in fair value are recorded in equity. When these assets are sold or undergo prolonged impairment, the accumulated adjustments to the reserves due to valuation adjustments are included in the Income statement as gains and losses.

The fair values of listed investments are based on listed prices (Level 1). 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 (Levels 2 and 3). If none of these techniques can be used to determine fair value, investments are carried at cost less any impairment loss.

Fair value measurements recognised in these consolidated annual accounts are classified using a fair value hierarchy that reflects the relevance of the variables employed to perform the measurement. This ranking has three levels:

- Level 1: Valuations based on the quotation price of identical instruments in an official market. The fair value is based on quoted market prices at the balance sheet date.

- Level 2: Valuations based on variables that are observable for the asset or liability. The fair value of financial assets included in this category is determined using valuation techniques. The valuation techniques maximize the use of observable market data when available and rely as little as possible on specific estimates done by Gas Natural Fenosa. If all significant inputs required to calculate the fair value are observable, the instrument is included in Level 2. If one or more of the significant inputs are not based on observable market data, the instrument is included in Level 3.

- Level 3: Valuations based on variables that are not based on observable market information.

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.

Receivables assignment agreements are treated as factoring without recourse provided that the risks and rewards inherent in ownership of the financial assets assigned are transferred.

<u>Cash and cash equivalents</u>

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.

<u>Borrowings</u>

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

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

<u>Trade and other payables</u>

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.

3.4.7 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.

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

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

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

- Derivatives listed on an official market are calculated on the basis of their year-end quotation (Level 1).

- Derivatives that are not traded on official markets are calculated on the basis of the discounting of cash flows based on year end market conditions, based on market conditions as at Consolidated balance sheet date or, for some non-financial items, on best estimation on forward curves of said non-financial item (Level 2 and 3).

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

Derivatives embedded in other financial instruments or in other host contracts are recorded separately as derivatives only when their financial characteristics and inherent risks are not strictly related to the instruments in which they are embedded and the whole item is not being carried at fair value through consolidated profit or 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 recognized 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 qualified as cash flow hedges are recognized in equity. The gain or loss relating to the ineffective portion is recognized immediately in the consolidated income statement.

Amounts accumulated in equity are reclassified to the income statement in the periods when the hedged item will affect the consolidated income statement.

c) Hedges of net foreign investments

The accounting treatment is similar to cash flow hedges. The variations in value of the effective part of the hedging instrument are carried on the consolidated balance sheet under “Cumulative translation differences”. The gain or loss from the non-effective part is recognised immediately under “Exchange differences” on the consolidated income statement. The accumulated amount of the valuation recorded under “Cumulative translation differences” is released to the consolidated income statement as the foreign investment that gave rise to it is sold.

2. Derivatives that do not qualify for hedge accounting

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

3. Energy purchase and sale agreements

During the normal course of its business Gas Natural Fenosa 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 he receives it or not. These agreements are executed and maintained in order to meet the needs of receipt of physical delivery of energy projected by Gas Natural Fenosa 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, fall out with the scope of IAS 39.

3.4.8 Non-current assets held for sale and discontinued activities

Gas Natural Fenosa classifies as assets held for sale all the assets and related liabilities for which active measures have been taken in order to sell them and if it is estimated that the sale will take place within the following twelve months.

Additionally, Gas Natural Fenosa 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.

Non-current assets held for sale are disclosed as follows on the consolidated balance sheet: the assets are carried under a single account “Non-current assets held for sale” and the liabilities are also carried under a single account called “Liabilities linked to non-current assets held for sale”. The profit or loss from discontinued activities is stated on a single line on the Consolidated income statement called “Profit for the year from discontinued operations net of tax”.

3.4.9 Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is determined using weighted average cost.

Costs of inventories include the cost of raw materials and those that are directly attributable to the acquisition and/or production, including the costs of transporting inventories to the current location.

The nuclear fuel is valued on the basis of the costs actually incurred in its acquisition and preparation. The consumption of nuclear fuel is charged to the income statement on the basis of the energy capacity consumed.

During 2016 the accounting policy for classifying greenhouse gas (CO_2) emission allowances as intangible fixed assets was revised. Following the relevant analysis, based on the consideration of these assets as inventories as they will not be recognised as assets, in general, on a lasting basis, and following the practice applied by the main industry operators, the carrying amount of the emission allowances recorded as intangible assets was reclassified to inventories. Emission allowances are stated at the lower of weighted average acquisition price and net realisable value. When the rights are delivered, they are derecognised against the provision recorded when the CO_2 emissions take place (Note 3.4.16).

Net realizable value is the estimated selling price in the ordinary course of business, less applicable variable selling expenses. For raw materials, the Group assesses whether or not the net realisable value of finished goods is greater than their production cost.

3.4.10 Share capital

Share capital is represented by ordinary shares.

Incremental costs directly attributable to the issue of new shares or options, net of tax, are deducted from equity as a deduction from Reserves.

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 recognized under "Reserves" in the consolidated balance sheet.

3.4.11 Earnings per share

Basic earnings per share are calculated as a quotient between Consolidated profit for the year attributable to equity holders of the company and the average weighted number of ordinary shares in circulation during this period, excluding the average number of shares of the parent Company held by the Group.

Diluted earnings per share are calculated as a quotient between Consolidated profit for the year attributable to the ordinary equity holders of the company 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.

3.4.12 Financial liabilities and equity instruments

Financial liabilities and equity instruments issued by Gas Natural Fenosa are classified based on the nature of the issue.

Gas Natural Fenosa 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.

3.4.13 Preference shares and subordinated perpetual debentures

The issues of preference shares and subordinated perpetual debentures are considered equity instruments if and only if:

- They do not include the contractual obligation for the issuer to repurchase them, under conditions involving certain amounts and at certain dates or determinable amounts and at determinable dates, or the right of the holder to demand their redemption.

- The payment of interest is at the discretion of the issuer.

In the case of issues of preference shares made by a subsidiary of the Group, which comply with the above conditions, the amount received is classified on the consolidated balance sheet under "Non-controlling interest".

3.4.14 Deferred income

This heading mainly includes:

- Capital grants relating basically to agreements with the Regional Governments for the gasification of municipalities and other investments in gas infrastructure, for which Gas Natural Fenosa has met all the conditions established, are stated at the amount granted.

- Income received for the construction of connection facilities for the gas or electricity distribution network (undertaken), which are booked for the cash received, as well as assignments received for these facilities, which are booked, in accordance with IFRIC 18, at their fair value, since both the cash and the facilities are received in consideration for an ongoing service of providing access to the network during the life of the facilities.

- Income from the extension of the pipeline network that will be financed by third parties.

Amounts under Deferred income are recognised through the consolidated income statement systematically on the basis of the useful life of the corresponding asset, thus offsetting the amortisation expense.

When the corresponding asset is replaced, the deferred income from the extension of the pipeline network financed by third parties is expensed at the carrying value of the assets replaced. The remaining amount of the deferred income is taken to profit and loss systematically over the useful life of the respective asset.

3.4.15 Provisions for employee obligations

a) Post-employment pension obligations and the like

- Defined contribution plans

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

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

The contributions made have been recorded under "Personnel costs" on the consolidated income statement.

- Defined benefit plans

For certain groups there are defined benefit liabilities relating to the payment of retirement pension, death and disability supplements, in accordance with the benefits agreed by the entity and which have been transferred out in Spain through single premium insurance policies under Royal Decree 1588/1999/15 October, which adopted the Regulations on the arrangement of company pension liabilities.

The liability recognised for the defined benefit pensions plans is the current value of the liability at the balance sheet date less the fair value of the plan-related assets. 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 directly in the equity item "Other comprehensive income", for the entire amount, in the period in which they arise.

Past-service costs are recognized immediately in consolidated income statement under “Personnel cost”.

b) Other post-employment benefit obligations

Some of Gas Natural Fenosa’s companies provide post-employment benefits to their employers. 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, directly in equity, to “Other comprehensive income”.

c) Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. Gas Natural Fenosa 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 Gas Natural Fenosa has decided to give its consent to voluntary redundancies once they have been requested by the employees.

3.4.16 Provisions

Provisions are recognized when Gas Natural Fenosa has a legal or implicit present obligation as a result of past events; it is more likely than 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.

Gas Natural Fenosa has the obligation to dismantle certain facilities at the end of their useful life, such as those related to nuclear power plants and mines, as well as carry out environmental restoration where these are located. To do so, it is recorded under Property. plant and equipment the current value of the cost that these tasks would amount, which, in the case of nuclear plants, includes the time until ENRESA, the public entity takes charge of the dismantling and management of radioactive waste, with a counter-entry under provisions for liabilities and charges. This estimate is reviewed annually so that the provision reflects the current value of the future costs by increasing or decreasing the value of the asset. The variation in the provision arising from its financial restatement is recorded under “Financial expenses”.

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.

In order to cover the obligation concerning the delivery of CO_2 emission allowances for emissions made during the year, Current provisions record the CO_2 allowances to be delivered valued at acquisition cost for allowances purchased recorded under Inventories and, if not all necessary emission allowances are held, at fair value for allowances pending purchase.

3.4.17 Leases

1) 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.

Gas Natural Fenosa acts as a lessee under a number of finance lease agreements. 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 consolidated balance sheet. The interest component of the finance charge is taken to the consolidated 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.

2) 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 consolidated income statement on a straight-line basis over the lease period.

3.4.18 Income tax

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 Consolidated annual accounts used the tax rates that are expected to be in force when the assets and liabilities are realised. No deferred tax liabilities are recognised for profits not distributed from the subsidiaries when Gas Natural Fenosa 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 income tax assets and credit taxes are recorded only when there are no doubts as to their future recoverability through the future tax profits that can be used to offset timing differences and make credit taxes effective.

When tax rates change, deferred tax assets and liabilities are reestimated. These amounts are charged or credited to the consolidated income statement or to the item "Other comprehensive income for the year" in the consolidated statement of comprehensive income, depending on the account to which the original amount was charged or credited.

3.4.19 Revenue and expenses recognition and payments for regulated activities

a) General

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

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

Sales are stated net of tax and discounts and the transactions between companies in the Gas Natural Fenosa are eliminated.

b) Revenues from the gas business and settlement for regulated activities

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

The regulatory framework of the natural gas sector in Spain regulates a payment procedure for the redistribution amongst companies in the sector of the net turnover obtained, so that each company receives the remuneration recognised for its regulated activities.

The remuneration of the regulated gas distribution activity is fixed for each distribution company for all its facilities according to the clients connected to them and the volume of gas supplied.

The remuneration of the regulated gas transport is fixed in respect of availability and continuity of supply of the companies owning transmission assets.

The remuneration for regulated gas transport and distribution assigned in the Ministerial Order in which it is determined each year is recorded as income.

At the date of preparation of these consolidated annual accounts, no final settlements from prior years are outstanding.

Order ETU/1977/2016 of 23 December recognised both the accumulated gas system deficit for 2014 and the mismatch between revenues and costs for 2015, which coincide with the amount approved in the respective final settlements for each year. Companies subject to the settlement system, which include Gas Natural Fenosa, are entitled to recover these amounts, as from 25 November 2016, in fifteen and five annual payments, respectively.

Order ETU/1283/2017 of 22 December recognises the mismatch between revenues and costs for 2016, which coincides with the amount approved in the final settlement for that year. Companies subject to the settlement system, including Gas Natural Fenosa, will be entitled to recover this amount in five annual payments as from 1 December 2017.

In December 2017 took place the irrevocable assignment without recourse of the accumulated deficit for 2014 and the mismatches for 2015 and 2016 (Note 8).

Revenue includes the amount of both last-resort gas sales and free market sales, since the last-resort supplier and the free-market supplier are deemed to be a principal agent and not a commission agent for the supply made.

The exchanges of gas that do not have a different value and do not include costs that causes differences in value are not classified as transactions that generate revenues and are not included, therefore, in the income figure.

c) Revenue from electricity business and settlement for regulated activities

Note 2.4 describes the basic aspects of the applicable regulations to the electricity sector.

The regulatory framework of the electricity sector in Spain regulates a payment procedure for the redistribution amongst companies in the sector of the net turnover obtained, so that each company receives the remuneration recognised for its regulated activities.

La retribución de las actividades reguladas de transporte y distribución eléctrica se registran como ingresos por el importe asignado en la Orden Ministerial que la determina cada año.

At the date of formulation of these Consolidated annual accounts the final payments for the period 2013-2015 have not been published, although it is not expected that the final payments will generate significant differences in relation to the estimates made.

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

Following the publication of Electricity Sector Law 24/2013, December 26 (Note 2.4), temporary mismatches between electricity system revenues and costs are funded by the companies subject to the settlement system, including Gas Natural Fenosa, generating the right to recover the relevant amount over the following five years, including interest at a market rate. Consequently, the financing for the electricity system revenue deficit is recognised as a financial asset since, on the basis of this regulation, Gas Natural Fenosa is entitled to a reimbursement and there are no future contingent factors. In 2014 and 2015, following the reforms that were undertaken, there has been no income shortfall in the sector, according to the data on provisional settlements for those years.

Revenue includes the amount of electricity sales in both the PVPC market and the free market, since the last-resort supplier and the free-market supplier are deemed to be a principal agent and not a commission agent for the supply made. Consequently, power purchases and sales are recognised for the total amount. Nonetheless, power purchases and sales from the pool made by the Group's generation and supply companies in the same time band are eliminated during the consolidation process.

d) Other income and expenses

Gas Natural Fenosa has power generation capacity assignment contracts with the Federal Electricity Commission for its combined-cycle plants in Mexico (CFE), for a 25-year term as from the start date of commercial operations. These contracts stipulate a pre-established collection schedule for the assignment of power supply capacity. As Gas Natural Fenosa has the capacity to operate and manage the plants, sells the power at market prices and retains the rewards and risks of operations, taking relevant decisions that will affect future cash flows, these contracts represent provisions of services and are thus recognised on a percentage-of-completion basis.

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 consolidated 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.

3.4.20 Cash Flow Statements

The consolidated cash flow statements have 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 Group revenues, as well as other activities that cannot be qualified as investing or financing.

b) Investing activities: acquisition, sale or disposal band other means of assets in the long-term and other investments not included in cash and cash equivalents.

c) Financing activities: activities that generate changes in the size and composition of equity and liabilities that do not form part of operating activities.

3.4.21 Significant accounting estimates and judgements

The preparation of the Consolidated annual accounts requires the use of estimates and assumptions. The valuation standards that require a large number of estimates are set out below:

a) *Intangible assets and property, plant and equipment (Notes 3.4.3 and 3.4.4)*

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 non-financial assets (Note 3.4.5)*

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

c) Derivatives and other financial instruments (Note 3.4.7)

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

The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. Gas Natural Fenosa 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 prices derivatives is determined using quoted forward price curves at the balance sheet date.

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

d) *Provisions for employee benefits (Note 3.4.15)*

A number of assumptions must be used to calculate pension costs, other costs of post-retirement benefits and other post-retirement liabilities. Gas Natural Fenosa 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 3.4.16)*

Gas Natural Fenosa makes an estimate of the amounts to be settled in the future, including amounts relating to, contractual obligations, outstanding litigation, future costs for dismantling and closure of certain facilities and 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 (Note3.4.18)*

The calculation of the income tax expense requires interpretations of tax legislation in the jurisdictions in which Gas Natural Fenosa operates. The determination of expected outcomes of outstanding disputes and litigation requires the preparation of significant estimates and judgment. Gas Natural Fenosa 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.

g) *Revenue recognition and settlement of regulated activities (Note 3.4.19)*

Revenues from energy sales are recognized when the goods are delivered to the customer based on periodical meter readings and include the estimated accrual of the value of the goods consumed as from the date of the meter reading until the close of the period. Estimated daily consumption is based on historical customer profiles taking into account seasonal adjustments and other factors than can be measured and may affect consumption. Historically, no material adjustments have been made relating to the amounts booked as unbilled income and none are expected in the future.

Certain aggregates for the electricity and gas system, including those relating to other companies which allow for the estimate of the overall settlement of the electricity system that must materialise in the respective final payments, could affect the calculation of the deficit in the payments for the electricity and gas regulated business in Spain.

Note 4. Segment financial information

An operating segment is a component that carries on business activities from which it may obtain ordinary revenue and incur costs, whose operating results are reviewed regularly by the Gas Natural SDG, S.A. Board of Directors when taking the company's operating decisions in order to decide on the resources that must be allocated to the segment and to evaluate its performance, in respect of which separate financial information is available.

As described in Notes 3.3 and 9, in 2017, under IFRS 5 have been regarded as discontinued operations, restating the consolidated profit and loss account for 2016, the following lines of business:

- Gas distribution in Italy.
- Gas distribution in Colombia.
- Electricity distribution in Moldova.
- Wholesale and retail gas supply in Italy within the gas segment.
- The electricity generation in Kenya, within the international electricity segment.

The profit and loss accounts for 2017 and 2016 for said lines of business are detailed in Note 9.

a) *Segment information*

The operating segments of Gas Natural Fenosa are:

- Gas distribution. This segment encompasses the regulated gas distribution business in Spain and Latin America.

  The gas distribution business in Spain includes the regulated gas distribution activity, the services for third-party access to the network, as well as the activities related to distribution. This also includes the liquefied petroleum gas (LPG) business.

  The gas distribution business in Latin America (Argentina, Brazil, Chile, Mexico and Peru) includes the regulated gas distribution activity and sales to customers at regulated prices. In Chile the gas supply and commercialisation business is also included.

- Electricity distribution. This segment encompasses the regulated electricity distribution business in Spain and Latin America.

  The electricity distribution business in Spain includes the regulated electricity distribution business, network services and other activities related to third party access to the distribution network.

  The electricity distribution business in Latin America consists of the regulated electricity distribution activity in Argentina, Chile, Panama and Colombia (Until 31 December 2016 in the case of Colombia).

- Gas. This includes the activities derived from Gas Infrastructures, Marketing and Unión Fenosa Gas.

  The infrastructures business includes the gas exploration, production and storage activities, It also covers the regasification process and the operation of the Maghreb-Europe gas pipeline.

  The marketing business groups together the wholesale gas supply and sale activities both in the liberalised Spanish market and abroad, the gas sale business and the sale of other products and services related to retail sales in the liberalised market in Spain, as well as the sale of gas at the last-resort tariff in Spain. It also includes the sea transport business.

  Unión Fenosa Gas' business (50%-owned by Gas Natural Fenosa and 50% by another shareholder, consolidated using the equity method) includes the Damietta (Egypt) liquefaction activities, sea transport and gas supply activities.

- Electricity. It includes electricity generation and sale in Spain and the International Electricity business.

  The Electricity business in Spain includes electricity production activity through combined cycle, coal, nuclear, hydro, co-generation and wind farm plants. and other special regime technologies, the supply of electricity to wholesale markets and the wholesaling and retailing of electricity in the deregulated Spanish market and the supply of electricity at the small consumer voluntary price (PVPC).

  The International Electricity business mainly includes the Group's international generation activities in Latin America (Mexico, Costa Rica, Dominican Republic, Panama, Brazil, Chile and Puerto Rico, the latter consolidated using the equity method through EcoEléctrica, L.P.) and other countries (Australia).

- Other. This includes the exploitation of the coal field owned by Kangra Coal (Proprietary), Ltd. in South Africa, the assets/liabilities and operating costs of the corporation and its sales to the different lines of business on the basis of utilisation, as well as other remaining activities.

Net financial income and income tax expense are not allocated to the operating segments, since both financing activities and the income tax effects are managed jointly.

Segment results and investments for the periods of reference are as follows:

Segment financial information – Income statement

2017	Gas distribution Spain	Gas distribution Latin American	Gas distribution Total	Electricity distribution Spain	Electricity distribution Latin American	Electricity distribution Total	Gas Infrastructures	Gas Marketing	Gas UF GAS	Gas Total	Electricity Spain	Electricity International	Electricity Total	Other	Eliminations	TOTAL
Consolidated Revenue	1,145	3,735	**4,880**	818	3,243	**4,061**	84	8,874	**-**	**8,958**	4,349	873	**5,222**	**185**		**23,306**
Revenue between segments	125	-	**125**	43	62	**105**	233	1,260	**-**	**1,493**	1,026	17	**1,043**	**252**		**3,018**
Sales by segment	1,270	3,735	**5,005**	861	3,305	**4,166**	317	10,134	**-**	**10,451**	5,375	890	**6,265**	**437**	**(3,018)**	**23,306**
Segment procurements	(67)	(2,615)	**(2,682)**	-	(2,486)	**(2,486)**	(1)	(9,366)	**-**	**(9,367)**	(4,270)	(511)	**(4,781)**	**(229)**	**2,866**	**(16,679)**
Net personnel expenses	(76)	(119)	**(195)**	(116)	(151)	**(267)**	(5)	(76)	**-**	**(81)**	(158)	(37)	**(195)**	**(293)**	**-**	**(1,031)**
Other operating income/expenses	(221)	(293)	**(514)**	(147)	(234)	**(381)**	(15)	(222)	**-**	**(237)**	(645)	(66)	**(711)**	**10**	**152**	**(1,681)**
EBITDA	906	708	**1,614**	598	434	**1,032**	296	470	**-**	**766**	302	276	**578**	**(75)**	**-**	**3,915**
Other results	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**-**
Depreciation, amortisation and impairment losses	(299)	(159)	**(458)**	(233)	(138)	**(371)**	(53)	(80)	**-**	**(133)**	(442)	(121)	**(563)**	**(123)**	**-**	**(1,648)**
Impairment of credit losses	(8)	(26)	**(34)**	-	(50)	**(50)**	-	(37)	**-**	**(37)**	(31)	-	**(31)**	**(3)**	**-**	**(155)**
Operating profit	599	523	**1,122**	365	246	**611**	243	353	**-**	**596**	(171)	155	**(16)**	**(201)**	**-**	**2,112**
Net financial income	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**(699)**
Results of equity-consolidated companies	-	10	**10**	-	17	**17**	-	-	(88)	**(88)**	13	58	**71**	**4**	**-**	**14**
Income before tax	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**1,427**
Corporate income tax	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**(190)**
Profit/(loss) for the year from continuing operations	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**1,237**
Profit/(loss) for the year from discontinued operations	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**460**
Profit for the year	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**1,697**

2016 (*)	Gas distribution Spain	Gas distribution Latin American	Gas distribution Total	Electricity distribution Spain	Electricity distribution Latin American	Electricity distribution Total	Gas Infrastructures	Gas Marketing	Gas UF GAS	Gas Total	Electricity Spain	Electricity International	Electricity Total	Other	Eliminations	TOTAL
Consolidated Revenue	1,075	2,802	**3,877**	789	4,673	**5,462**	27	7,471	**-**	**7,498**	4,217	720	**4,937**	**134**		**21,908**
Revenue between segments	123	-	**123**	44	-	**44**	297	1,148	**-**	**1,445**	1,062	18	**1,080**	**230**		**2,922**
Sales by segment	1,198	2,802	**4,000**	833	4,673	**5,506**	324	8,619	**-**	**8,943**	5,279	738	**6,017**	**364**	**(2,922)**	**21,908**
Segment procurements	(33)	(1,840)	**(1,873)**	-	(3,408)	**(3,408)**	(4)	(7,813)	**-**	**(7,817)**	(3,813)	(385)	**(4,198)**	**(95)**	**2,780**	**(14,611)**
Net personnel expenses	(68)	(105)	**(173)**	(85)	(216)	**(301)**	(5)	(65)	**-**	**(70)**	(138)	(38)	**(176)**	**(254)**	**-**	**(974)**
Other operating income/expenses	(208)	(240)	**(448)**	(145)	(360)	**(505)**	(15)	(217)	**-**	**(232)**	(613)	(76)	**(689)**	**73**	**142**	**(1,659)**
EBITDA	889	617	**1,506**	603	689	**1,292**	300	524	**-**	**824**	715	239	**954**	**88**	**-**	**4,664**
Other results	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**122**	**-**	**122**
Depreciation, amortisation and impairment losses	(291)	(146)	**(437)**	(222)	(162)	**(384)**	(58)	(60)	**-**	**(118)**	(523)	(124)	**(647)**	**(120)**	**-**	**(1,707)**
Impairment of credit losses	(2)	(19)	**(21)**	-	(215)	**(215)**	-	(36)	**-**	**(36)**	(38)	-	**(38)**	**(5)**	**-**	**(315)**
Operating profit	596	452	**1,048**	381	312	**693**	242	428	**-**	**670**	154	115	**269**	**84**	**-**	**2,764**
Net financial income	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**(815)**
Results of equity-consolidated companies	-	16	**16**	-	9	**9**	-	-	(176)	**(176)**	2	49	**51**	**2**	**-**	**(98)**
Income before tax	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**1,851**
Corporate income tax	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**(333)**
Profit/(loss) for the year from continuing operations	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**1,518**
Profit/(loss) for the year from discontinued operations	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**193**
Profit for the year	-	-	**-**	-	-	**-**	-	-	**-**	**-**	-	-	**-**	**-**	**-**	**1,711**

(*) The consolidated income statement for 2016 has been restated reclassifying to discontinued operations (Note 3.3 and 9).

Segmental financial information – Assets, liabilities and investments

	Gas distribution				Electricity distribution				Gas				Electricity					
2017	Spain	Italy	Latin America	Total	Spain	Moldova	Latin America	Total	Infra-structures	Market-ing	UF GAS	Total	Spain	International	Total	Other	Eliminations	TOTAL
Operating assets (b)	4,068	-	4,548	**8,616**	5,090	-	5,230	**10,320**	477	3,147	-	**3,624**	8,598	1,711	**10,309**	1,205	(832)	**33,242**
Investments under equity method	-	-	44	**44**	7	-	22	**29**	-	-	925	**925**	116	358	**474**	28	-	**1,500**
Operating liabilities (b)	(838)	-	(532)	**(1,370)**	(1,058)	-	(702)	**(1,760)**	(54)	(1,284)	-	**(1,338)**	(1,024)	(131)	**(1,155)**	(1,030)	836	**(5,817)**
Investment in intangible assets (c)	15	-	173	**188**	35	-	24	**59**	11	1	-	**12**	7	-	**7**	123	-	**389**
Invest. in property, plant & equipment (d)	197	-	199	**396**	217	-	326	**543**	7	47	-	**54**	171	168	**339**	61	-	**1,393**
Business combinations (Note 31)	-	-	-	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	-	-	**-**

	Gas distribution				Electricity distribution				Gas				Electricity					
2016 [a]	Spain	Italy	Latin America	Total	Spain	Moldova	Latin America	Total	Infra-structures	Marketing	UF GAS	Total	Spain	International	Total	Other	Eliminations	TOTAL
Operating assets (b)	4,113	528	5,031	**9,672**	4,939	149	5,223	**10,311**	520	3,247	-	**3,767**	8,761	1,979	**10,740**	1,115	(689)	**34,916**
Investments under equity method	-	-	10	**10**	6	-	54	**60**	-	-	1,034	**1,034**	94	344	**438**	33	-	**1,575**
Operating liabilities (b)	(768)	(42)	(796)	**(1,606)**	(900)	(32)	(804)	**(1,736)**	(10)	(1,404)	-	**(1,414)**	(1,035)	(145)	**(1,180)**	(984)	699	**(6,221)**
Investment in intangible assets (c)	20	30	136	**186**	30	-	44	**74**	4	6	-	**10**	5	3	**8**	124	-	**402**
Invest. in property, plant & equipment (d)	673	1	168	**842**	235	13	344	**592**	9	455	-	**464**	100	85	**185**	32	-	**2,115**
Business combinations (Note 31)	-	-	-	**-**	-	-	-	**-**	-	32	-	**32**	-	-	**-**	-	-	**32**

(a) 2016 includes the assets and liabilities of the gas distribution business in Italy and Colombia, electricity distribution in Moldova, gas marketing in Italy and electricity generation in Kenya which have been reclassified to discontinued operations in the profit and loss account (Note 3.3 and 9). Operating assets and liabilities at 31 December 2016 in Gas Distribution in Colombia amounted Euros 366 million and Euros 104 million respectively while intangible and tangible investments amounted Euros 23 million and Euros 6 million; regarding to operating assets and liabilities of international generation in Kenya they amounted Euros 93 million and Euros 13 million and had material investments of Euros 5 million.

(b) There follows a breakdown of the reconciliation of "Operating assets" and "Operating liabilities" with consolidated "Total assets" and "Total liabilities":

	2017	2016
Operating assets	**33,242**	**34,916**
Goodwill	4,760	5,036
Investments carried under the equity method	1,500	1,575
Non-current financial assets	1,315	1,907
Deferred tax assets	849	872
Non-current assets held for sale (Note 9)	1,682	-
Derivative financial instruments (see Note 11)	38	46
Public administrations (Note 11)	71	144
Current tax assets	178	162
Other current financial assets	462	389
Cash and cash equivalents	3,225	2,067
Total assets	**47,322**	**47,114**

	2017	2016
Operating liabilities	**(5,817)**	**(6,221)**
Equity	(18,305)	(19,005)
Non-current financial liabilities	(15,916)	(15,003)
Finance lease liability (Notes 18 and 20)	(933)	(1,067)
Deferred tax liabilities	(2,312)	(2,509)
Liabilities related to non-current assets held for sale (Note 9)	(621)	-
Current financial liabilities	(2,543)	(2,599)
Derivative financial instruments (Notes 19 and 20)	(90)	(48)
Dividend payable (Note 20)	(45)	(37)
Public administrations (Note 19)	(593)	(519)
Current tax liabilities	(147)	(106)
Total liabilities	**(47,322)**	**(47,114)**

(c) Includes the investment in "Intangible assets" (Note 5), broken down by operating segment.
(d) Includes the investment in "Property, plant and equipment" (Note 6), broken down by operating segment.

b) Reporting by geographic area

Gas Natural Fenosa's net revenue by country of destination is analysed below:

	2017	2016 (1)
Spain	10,765	10,101
Rest of Europe	2,711	2,343
France	1,282	1,409
Portugal	416	347
Italy	257	183
United Kingdom	150	132
Ireland	141	54
Belgium	133	84
Netherlands	129	84
Other Europe	203	50
Latin America	8,495	8,731
Chile	3,447	3,009
Brazil	1,883	1,369
Mexico	1,455	1,094
Panama	799	785
Argentina	574	661
Puerto Rico	201	243
Dominican Republic	118	95
Colombia	9	1,463
Rest of Latin America	9	12
Other	1,335	733
India	372	217
Japan	153	20
Egypt	112	201
Rest of countries	698	295
Total	**23,306**	**21,908**

(*) The consolidated income statement for 2016 has been restated reclassifying to discontinued operations (Note 3.3 and 9).

The assets of Gas Natural Fenosa, which include operating assets, as described above, and the investments booked using the equity method, are assigned based on their location:

	At 31/12/2017	At 31/12/2016
Spain	21,748	21,706
Rest of Europe	384	1,162
Latin American	11,877	12,558
Other	733	1,065
Total	**34,742**	**36,491**

The investments in property, plant and equipment and other intangible assets of Gas Natural Fenosa, as described above, assigned according to location of the assets are as follows:

	At 31/12/2017	At 31/12/2016
Spain	820	1,672
Rest of Europe	38	50
Latin American	871	773
Other	53	22
Total	**1,782**	**2,517**

Note 5. Intangible assets

The movement in 2017 and 2016 in intangible assets is as follows:

	Concessions IFRIC 12	Other concessions and similar	Computer software	Other intangible assets	Subtotal	Goodwill	Total
Gross cost	2,229	3,496	1,131	1,423	**8,279**	4,962	**13,241**
Sinking fund and impairment losses	(878)	(675)	(718)	(445)	**(2,716)**	-	**(2,716)**
Carrying amount at 01/01/2016	**1,351**	**2,821**	**413**	**978**	**5,563**	**4,962**	**10,525**
Investment (Note 4)	151	13	215	23	**402**	-	**402**
Divestment	-	-	(1)	-	**(1)**	-	**(1)**
Amortisation charge and impairment losses	(78)	(41)	(133)	(76)	**(328)**	-	**(328)**
Currency translation differences	184	158	2	5	**349**	55	**404**
Business combinations (Note 31)	-	-	-	39	**39**	19	**58**
Reclassifications and other(2)	-	-	(5)	(135)	**(140)**	-	**(140)**
Carrying amount at 31/12/16	**1,608**	**2,951**	**491**	**834**	**5,884**	**5,036**	**10,920**
Gross cost	2,661	3,662	1,341	1,374	**9,038**	5,036	**14,074**
Sinking fund and impairment losses	(1,053)	(711)	(850)	(540)	**(3,154)**	-	**(3,154)**
Carrying amount at 31/12/16	**1,608**	**2,951**	**491**	**834**	**5,884**	**5,036**	**10,920**
Investment (Note 4)	186	21	170	12	**389**	-	**389**
Amortisation charge and impairment losses	(86)	(42)	(131)	(65)	**(324)**	-	**(324)**
Currency translation differences	(165)	(111)	(7)	(7)	**(290)**	(110)	**(400)**
Reclassifications and other(2)	(468)	5	(29)	(6)	**(498)**	(166)	**(664)**
Carrying amount at 31/12/2017	**1,075**	**2,824**	**494**	**768**	**5,161**	**4,760**	**9,921**
Gross cost	1,662	3,489	1,430	1,371	**7,952**	**4,760**	**12,712**
Sinking fund and impairment losses	(587)	(665)	(936)	(603)	**(2,791)**	**-**	**(2,791)**
Carrying amount at 31/12/2017	**1,075**	**2,824**	**494**	**768**	**5,161**	**4,760**	**9,921**

(1) Mainly includes the reclassification of CO_2 emission allowances to Inventories for Euros 104 million (Note 3.4.9) and the derecongition of the Electricaribe balances due to its deconsolidation following the loss of control (Note 8).

(2) Mainly includes the transfers to "Non-current assets held for sale" to the date on which this classification applies (Note 9).

Note 4 includes a breakdown of investments in intangible assets by segment.

IFRIC Concessions includes concessions regarded as intangible assets under IFRIC 12 "Service concession agreements" (Note 32).

The heading "Other concessions and similar" includes principally:

- The Maghreb-Europe pipeline concession (Note 32) amounting to Euros 164 million at 31 December 2017 (Euros 212 million at 31 December 2016).

- The indefinite useful according the following detail:

	31,12,2017	**31,12,2016**
Electricity distribution Spain	684	684
Electricity distribution Chile	1,097	1,139
Gas distribution Chile	856	893

The heading "Other intangible assets" mainly includes:

- Licences to renewable generation farms totalling Euros 169 million at 31 December 2017 (Euros 181 million at 31 December 2016). Includes Euros 21 milion (Euros 23 milion en 2016) from the business combination with Ibereólica Cabo leones II S.A. was included in 2016 (Note 31).

- The exclusive regasification rights in the Peñuelas regasification plant (Puerto Rico) totalling Euros 17 million at 31 December 2017 (Euros 24 million at 31 December 2016).

- The value of gas supply contracts and other contractual rights acquired as a result of the businesses combinations involving CGE for an amount of Euros 165 million at 31 December 2017 (Euros 184 million at 31 December 2016); Unión Fenosa for an amount of Euros 358 million at 31 December 2017 (Euros 389 million at 31 December 2016) and Vayu Limited for an amount of Euros 13 million at 31 December 2017 (Euros 14 million at 31 December 2016) (Note 31).

Set out below is a summary of goodwill assignment by CGU or CGU groups:

2017	Gas distribution	Electricity distribution	Gas	Electricity	Other	Total
Spain	-	1,070	-	2,708	-	3,778
Latin American	112	418	-	424	-	954
Rest	-	-	16	-	12	28
	112	**1,488**	**16**	**3,132**	**12**	**4,760**

2016	Gas distribution	Electricity distribution	Gas	Electricity	Other	Total
Spain	-	1,070	-	2,708	-	3,778
Latin American	124	449	-	482	-	1,055
Rest	143	11	16	18	15	203
	267	**1,530**	**16**	**3,208**	**15**	**5,036**

The impairment tests have been carried out at 31 December 2017 and 2016. On the basis of the analysis of goodwill and intangible assets with an undefined useful life, no need to recognise impairment came to light (Note 3.4.5).

At 31 December 2017, Gas Natural Fenosa records investment commitments totalling Euros 33 million relating basically to the development of the gas distribution network with concessions regarded as intangible assets under IFRIC 12.

The intangible assets include, at 31 December 2017, fully amortised assets still in use totalling Euros 529 million (Euros 521 million at 31 December 2016).

Note 6. Property, plant and equipment

The movements in the accounts in 2017 and 2016 under property, plant and equipment and their respective accumulated depreciation and provisions have been as follows:

	Land and buildings	Gas installations	Electricity generation plants	Plant for electricity transmission and distribution	Gas tankers	Other Property, plant and equipment	PPE under construction	Total
Gross cost	817	10,194	12,484	8,670	693	1,140	891	**34,889**
Sinking fund and impairment losses	(134)	(5,116)	(3,767)	(1,525)	(216)	(438)	-	**(11,196)**
Carrying amount at 01/01/2016	**683**	**5,078**	**8,717**	**7,145**	**477**	**702**	**891**	**23,693**
Investment (Note 4)	26	781	50	316	425	63	454	**2,115**
Divestment	(157)	(9)	(2)	-	-	(25)	(19)	**(212)**
Depreciation and Impairment charge	(23)	(379)	(591)	(339)	(29)	(70)	-	**(1,431)**
Currency translation differences	29	53	11	245	-	(1)	30	**367**
Reclassifications and other (1)	(13)	94	145	(723)	-	(44)	(364)	**(905)**
Carrying amount at 31/12/16	**545**	**5,618**	**8,330**	**6,644**	**873**	**625**	**992**	**23,627**
Gross cost	668	10,972	12,666	8,269	1,118	1,042	992	**35,727**
Sinking fund and impairment losses	(123)	(5,354)	(4,336)	(1,625)	(245)	(417)	-	**(12,100)**
Carrying amount at 31/12/16	**545**	**5,618**	**8,330**	**6,644**	**873**	**625**	**992**	**23,627**
Investment (Note 4)	25	315	140	297	-	46	570	**1,393**
Divestment	(19)	(2)	(3)	(3)	-	(5)	(4)	**(36)**
Depreciation and Impairment charge	(22)	(391)	(522)	(322)	(52)	(61)	-	**(1,370)**
Currency translation differences	(6)	(121)	(211)	(160)	-	(60)	(51)	**(609)**
Reclassifications and other (2)	-	(43)	44	60	-	(10)	(402)	**(351)**
Carrying amount at 31/12/2017	**523**	**5,376**	**7,778**	**6,516**	**821**	**535**	**1,105**	**22,654**
Gross cost	644	11,020	12,454	8,399	1,118	987	1,105	35,727
Sinking fund and impairment losses	(121)	(5,644)	(4,676)	(1,883)	(297)	(452)	-	(13,073)
Carrying amount at 31/12/2017	**523**	**5,376**	**7,778**	**6,516**	**821**	**535**	**1,105**	**22,654**

(1) As well as the recurring reclassification of PPE under construction, it mainly includes the derecognition of the Electricaribe balances due to the deconsolidation of the holding following the loss of control (Note 8).
(2) Mainly includes the transfers to “Non-current assets held for sale” to the date on which this classification applies (Note 9).

Note 4 include a breakdown of investments in property, plant and equipment by segment.

In November 2017 Gas Natural Fenosa 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. Additionally, in December 2017 sold the building located in calle Ombú, Madrid, for Euros 26 million, generating a capital gain before income tax of Euros 15 million (Note 27).

In December 2016 Gas Natural Fenosa sold four buildings located in Madrid (Avenida San Luis 77, Antonio López 193, A Canto 11-13 and Avenida América 38) for Euros 206 million, generating a pre-tax capital gain of Euros 51 million (Note 27). For each of these buildings, an operating lease agreement was concluded without any purchase option for a term of 10 years, which may be extended for a further five years except for the building in Avenida América 38 (Note 35). At the date of the transaction, the remaining useful lives of the properties was considerably greater than the maximum lease period, in all cases.

The heading “Gas tankers” at 31 December 2017 includes the present value at the acquisition date of committed payments to charter gas tankers under finance leases (Note 18), net of depreciation. At 31 December 2017 Gas Natural Fenosa owns six oil tankers under finance leases following the inclusion of two new vessels for Euros 425 million in 2016 (Note 18).

At 31 December 2017, the item “Other fixed assets” includes the carrying amount of investments in areas with reserves, totalling Euros 206 million (Euros 293 million at 31 December 2016), basically relating to the investments in the coalfield of the company Kangra Coal (Proprietary), Ltd. in South Africa and exploration and development costs of Euros 21 million (Euros 22 million at 31 December 2016).
Set out below is a breakdown of fixed assets in course of construction by business area:

	31.12.2017	31.12.2016
Gas distribution	114	109
Electricity distribution	530	528
Electricity	420	329
Rest	41	26
Total	**1,105**	**992**

At 31 December 2017, Gas Natural Fenosa had no significant real estate investments.

At 31 December 2017, property, plant and equipment include fully-depreciated assets still in use totalling Euros 2,059 million (Euros 2,011 million at 31 December 2016).

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

At 31 December 2017, Gas Natural Fenosa records investment commitments totalling Euros 689 million relating basically to the construction of two gas tankers (Note 35), the construction of new electricity generation facilities and the development of the gas and electricity distribution network.

The financial expenses capitalised in 2017 in fixed assets projects during their construction total Euros 8 million (Euros 12 million in 2016). The financial expenses capitalised in 2017 account for 1.1% of total financial costs on net borrowings (1.3% in 2016). The average capitalisation rate for 2017 and 2016 was 4.0% and 4.1%, respectively.

Note 7. Investments in companies

Associates and jointly-controlled entities

Set out below is a breakdown of equity-consolidated investments:

	At 31/12/2017	At 31/12/2016
Associates	49	46
Jointly-controlled entities	1,451	1,529
Total	**1,500**	**1,575**

Appendix I lists all the associates and jointly-controlled entities in which Gas Natural Fenosa holds an interest, stating their activity and the percentage of the shareholding and equity interest.

The most significant shareholdings are Unión Fenosa Gas and EcoEléctrica L.P. (Note 4).

Movements during 2017 and 2016 in equity-consolidated investments, including a breakdown of the most significant shareholdings, are as follows:

	Unión Fenosa Gas	EcoEléctrica, L.P.	Other jointly-controlled entities	Total jointly-controlled entities	Associates	Total
Value of shareholding at 1/1/16	**1,209**	**309**	**167**	**1,685**	**45**	**1,730**
Investment	-	-	5	**5**	-	**5**
Divestitures (1)	-	-	(52)	**(52)**	-	**(52)**
Shares of profits/(losses)	(176)	49	27	**(100)**	2	**(98)**
Business combinations (Note 31)	-	-	-	**-**	-	**-**
Dividends received	(2)	(27)	(13)	**(42)**	(1)	**(43)**
Currency translation differences	1	13	4	**18**	-	**18**
Other comprehensive income	4	1	4	**9**	-	**9**
Reclassifications and other	(2)	(1)	9	**6**	-	**6**
Value of shareholding at 31/12/16	**1,034**	**344**	**151**	**1,529**	**46**	**1,575**
Investment	-	-	14	**14**	-	**14**
Divestment	-	-	(5)	**(5)**	-	**(5)**
Shares of profits/(losses)	(88)	58	38	**8**	6	**14**
Business combinations (Note 31)	-	-	-	**-**	-	**-**
Dividends received	-	-	(18)	**(18)**	-	**(18)**
Currency translation differences	(23)	(41)	(8)	**(72)**	-	**(72)**
Other comprehensive income	2	(3)	-	**(1)**	(1)	**(2)**
Reclassifications and other	-	-	(4)	**(4)**	(2)	**(6)**
Value of shareholding at 31/12/17	**925**	**358**	**168**	**1,451**	**49**	**1,500**

(1) On 29 June 2016 Gas Natural Fenosa, through the company Aprovisionadora Global de Energía (AGESA), a subsidiary of Gas Natural Chile, S.A., concluded an agreement for the sale of 20.0% of the interest in GNL Quintero, S.A. (Chile) with Enagás for USD 200 million, which following the adjustments for dividends at the year end stood at USD 197 million (Euros 182 million). The operation was concluded in November 2016 and resulted in a pre-tax capital gain of approximately Euros 128 million (Note 28).

In 2017 the investments relate to a Euros 14 million capital increase in Nueva Generadora del Sur, S.A. (Note 30).

In April 2016, Unión Fenosa Gas (consolidated by the equity method) sold its 21% holding in Regasificadora del Noroeste, S.A. (Reganosa), through Gasifica, S.A., to the Galicia regional government and to Grupo Tojeiro for an amount of Euros 28 million, generating an after-tax capital gain of Euros 1 million for Gas Natural Fenosa.

In June 2016 Unión Fenosa Gas reached an agreement with Enagás for the sale, through Infraestructuras de Gas S.A., of its 42.5% interest in Planta de regasificación de Sagunto, S.A. (Saggas) for Euros 106 million. This transaction took place in July 2016, generating an after-tax capital gain of Euros 21 million for Gas Natural Fenosa.

In 2016 an impairment of Euros 94 million was recognised with respect to the interest in Unión Fenosa Gas due to the need to update the assumptions concerning the supply cost in view of the forecast evolution of the energy scenario for Unión Fenosa Gas (Note 3.4.5). Accumulated impairment recorded in Unión Fenosa Gas amounts 628 million basically as a result of a substantial breach by the Egyptian supplier of agreements to restore gas deliveries at the Damietta liquefaction plant in Egypt (Notes 3.4.5 and 35).

There follows a breakdown of assets, liabilities, revenue and results of Gas Natural Fenosa's main interests in jointly-controlled entities (by shareholding percentage):

	At 31.12.2017		At 31.12.2016	
	Unión Fenosa Gas	**EcoEléctrica, L.P.**	**Unión Fenosa Gas**	**EcoEléctrica, L.P.**
Non-current assets	1,392	261	1,537	313
Current assets	231	107	266	96
Cash and cash equivalents	65	40	100	18
Non-current liabilities	(565)	(3)	(623)	(32)
Non-current financial liabilities	(159)	-	(181)	(27)
Current liabilities	(133)	(7)	(146)	(33)
Current financial liabilities	(21)	-	(34)	(25)
Net assets	**925**	**358**	**1,034**	**344**
Net borrowings (1)	115	(40)	115	34

(1) Net borrowings: Non-current financial liabilities+Current financial liabilities-Cash and cash equivalents.

	2017		2016	
	Unión Fenosa Gas	**EcoEléctrica, L.P.**	**Unión Fenosa Gas**	**EcoEléctrica, L.P.**
Revenue	723	151	578	155
Procurements	(692)	(55)	(545)	(63)
Personnel costs	(8)	(4)	(9)	(5)
Other operating income/expenses	(13)	(12)	(22)	(13)
Gross operating reults	**10**	**80**	**2**	**74**
Amortisation charge	(102)	(16)	(130)	(19)
Impairment of credit losses	-	(2)	-	1
Operating profit	**(92)**	**62**	**(128)**	**56**
Net financial income/(expense)	(21)	(1)	1	(4)
Results of equity-consolidated companies	1	-	10	-
Income before tax	**(112)**	**61**	**(117)**	**52**
Corporate income tax	20	(3)	37	(3)
Attributed to non-controlling interests	4		(2)	-
Profit/(loss) attributed for the year from continuing operations	**(88)**	**58**	**(82)**	**49**
Impairment of shareholding			(94)	-
Share of profits	**(88)**	**58**	**(176)**	**49**

There are no contingent liabilities affecting interests in jointly-controlled entities.

Acquisition and sale contractual commitments in jointly-controlled entities at 31 December 2017 and 31 December de 2016 are as follows:

Acquisition	**At 31.12.17**	**At 31.12.16**
Energy purchases (1)	5,103	5,189
Energy transmission (2)	120	145
Total contractual obligations	**5,223**	**5,334**

Sale	**At 31.12.17**	**At 31.12.16**
Energy sales (3)	1,665	1,859
Provision of capacity assignment services (4)	166	232
Total contractual obligations	**1,831**	**2,091**

(1) Reflects the long-term commitments for natural gas purchases of Unión Fenosa Gas and EcoEléctrica L.P.
(2) Reflects operating costs associated with charter contracts for gas tankers under finance leases for Unión Fenosa Gas.
(3) Reflects Union Fenosa Gas long-term commitments to sell natural gas under gas sale contracts.
(4) It reflects service provision commitments under power generation capacity assignment contracts of EcoEléctrica L.P. to Puerto Rico Electricity Power Authority.

Certain investment projects related to interests in jointly-controlled entities have been financed by means of specific structures (project finance) which include pledges on the shares in the project companies. At 31 December 2017, the outstanding balance of this type of financing totals Euros 237 million (Euros 303 million at 31 December 2016).

Joint operations

Gas Natural Fenosa participates in different joint ventures that meet the conditions indicated in Note 3.4.1.b and which are described in Appendix I, section 3. The relevant interests in joint ventures at 31 December 2017 and 2016 are as follows:

	2017	2016
Comunidad de Bienes Central Nuclear de Almaraz	11.3%	11.3%
Comunidad de Bienes Central Nuclear de Trillo	34.5%	34.5%
Comunidad de Bienes Central Térmica de Anllares	66.7%	66.7%

The contribution from the joint operations to Gas Natural Fenosa's assets, liabilities, revenue and results is analysed below:

	At 31/12/2017	At 31/12/2016
Non-current assets	524	562
Current assets	95	120
Cash and cash equivalents	1	1
Non-current liabilities	(75)	(75)
Non-current financial liabilities	-	-
Current liabilities	(91)	(91)
Current financial liabilities	(11)	(13)
Net assets	**453**	**516**
Net borrowings (1)	10	12

(1) Net borrowings: Non-current financial liabilities+Current financial liabilities-Cash and cash equivalents.

	2017	2016
Revenue	287	226
Operating expenses	(194)	(192)
Gross operating reults	**93**	**34**
Depreciation, amortisation and impairment losses	(61)	(57)
Operating profit	**32**	**(23)**
Net financial income/(expense)	-	-
Income before tax	**32**	**(23)**
Corporate income tax	(8)	6
Profit/(loss) attributed for the year from continuing operations	**24**	**(17)**

Note 8. Financial assets

The breakdown of financial assets, excluding those carried under “Trade and other receivables” (Note 11) and “Cash and other cash equivalents” (Note 12), at 31 December 2017 and 2016, classified according to their nature and account, is as follows:

At 31 December 2017	Available for sale	Loans and receivables	Investments held to maturity	Hedging derivatives	Fair value through profit or loss	Total
Equity instruments	560	-	-	-	-	**560**
Derivatives (Note 17)	-	-	-	15	-	**15**
Other financial assets	-	739	1	-	-	**740**
Non-current financial assets	**560**	**739**	**1**	**15**	**-**	**1,315**
Derivatives (Note 17)	-	-	-	65	-	**65**
Other financial assets	-	395	2	-	-	**397**
Current financial assets	**-**	**395**	**2**	**65**	**-**	**462**
Total	**560**	**1,134**	**3**	**80**	**-**	**1,777**

At 31 December 2016	Available for sale	Loans and receivables	Investments held to maturity	Hedging derivatives	Fair value through profit or loss	Total
Equity instruments	619	-	-	-	-	**619**
Derivatives (Note 17)	-	-	-	111	-	**111**
Other financial assets	-	1,175	2	-	-	**1,177**
Non-current financial assets	**619**	**1,175**	**2**	**111**	**-**	**1,907**
Derivatives (Note 17)	-	-	-	1	-	**1**
Other financial assets	-	388	-	-	-	**388**
Current financial assets	**-**	**388**	**-**	**1**	**-**	**389**
Total	**619**	**1,563**	**2**	**112**	**-**	**2,296**

Financial assets recognised at fair value at 31 December 2017 and at 31 December 2016 are classified as follows:

	31 December 2017				31 December 2016			
Financial assets	**Level 1 (Listed price on active markets)**	**Level 2 (Observable variables)**	**Level 3 (Non-observables variables)**	**Total**	**Level 1 (Listed price on active markets)**	**Level 2 (Observable variables)**	**Level 3 (Non-observables variables)**	**Total**
Available for sale	-	-	560	**560**	-	-	619	**619**
Hedging derivatives	-	80	-	**80**	-	112	-	**112**
Fair value through profit or loss	-	-	-	**-**	-	-	-	**-**
Total	**-**	**80**	**560**	**640**	**-**	**112**	**619**	**731**

Available-for-sale financial assets

The movement of Available for sale financial assets in 2017 and 2016, according with the method applied for calculating their fair value is as follows:

	2017				2016			
	Level 1 (Listed price on active markets)	Level 2 (Observable variables)	Level 3 (Non-observables variables)	Total	Level 1 (Listed price on active markets)	Level 2 (Observable variables)	Level 3 (Non-observables variables)	Total
At 1 January	**-**	**-**	**619**	**619**	**-**	**-**	**141**	**141**
Additions	-	-	-	-	-	-	-	-
Changes recognised directly in equity	-	-	(54)	(54)	-	-	-	-
Currency translation differences	-	-	(2)	(2)	-	-	1	1
Transfers and other (1)	-	-	(3)	(3)	-	-	477	477
At 31 December	**-**	**-**	**560**	**560**	**-**	**-**	**619**	**619**

(1) At 31 December 2016 it mainly included the transfer of Electricaribe balances due to the deconsolidation of the holding following a loss of control.

At 31 December 2017, "Available-for-sale financial assets" basically includes:

- The 14.9% shareholding in Medgaz, S.A., the company that operates the submarine gas pipeline between Algeria and Spain, amounting to Euros 95 million (Euros 90 million at 31 December 2016) whose fair value is determined based on the discount of cash flows for future dividends.

- A 2.23% holding in Richards Bay Coal Terminals Ltd, a company that operates a coal export terminal in South Africa amounting to Euros 40 million (Euros 41 million at 31 December 2016) whose fair value is determined based on its cost because it is the best estimate available.

- The 85.4% shareholding in Electrificadora del Caribe, S.A. ESP ("Electricaribe") amounting to Euros 416 million (Euros 475 million at 31 December 2016).

During 2016 Electricaribe underwent major cash difficulties due to the acts and omissions of the Republic of Colombia in relation to the non-payment of a considerable number of customer invoices, mostly with obligatory supply arrangements, as well as a significant consumption fraud. As a result, within the framework of the Treaty for the reciprocal protection of investments between Spain and Colombia, on 12 July 2016 Gas Natural Fenosa commenced discussions to seek a negotiated solution to the extremely difficult situation in which Electricaribe finds itself. In the event of an expropriation or similar event, the treaty demands that the corresponding indemnity be equivalent to the fair market value of the investment prior to the expropriation.

On 14 November 2016 the Superintendence for Residential Public Services of the Republic of Colombia ("the Superintendence") ordered, as a necessary measure to ensure the provision of electrical energy services, the government take-over of Electricaribe, as well as the separation of the members of the governing body and the general manager, and their replacement by a special agent appointed by the Superintendence. In the fulfilment of his functions, this agent replaced the executive personnel appointed by Gas Natural Fenosa and centralised decision-making on the information to be supplied to Gas Natural Fenosa. Therefore, at 31 December 2016 Gas Natural Fenosa had lost control and any significant influence over Electricaribe as it does not take part in, and has no direct information about, material business activities or decisions. On 11 January 2017 the Superidentence agreed to extend this takeover until 14 March 2017, and announced that Electricaribe would be liquidated on that date. On 22 March 2017 Gas Natural Fenosa submitted the documentation required to commence arbitration proceedings before the Tribunal of the United Nations Commission on International Trade Law (UNCITRAL) in order to recover the company within a feasible regulatory framework or, failing that, to receive compensation in accordance with the fair value of the company, estimated at over USD 1,000 million. The formal commencement of arbitration has been requested before the Tribunal of the UNCITRAL which, like the World Bank International Centre for the Settlement of Investment Disputes (ICSID), is regarded as the most suitable forum for resolving disagreements in the bilateral treaty for the reciprocal promotion and protection of investments between the Republic of Colombia and Spain.

In addition, Gas Natural Fenosa has an insurance policy for political risks for all its companies, which in the case of Electricaribe enables it to recover up to USD 500 million in the event of expropriation and discriminatory laws or regulations.

On 9 June 2017 Electricaribe entered into a contract with the public institution “Financiera de Desarrollo Nacional” with a view to this institution assessing and defining possible alternatives for structuring and implementing the definitive solution for the continuity of the provision of energy services on the Caribbean coast. Subsequently an international business bank was engaged. The government take-over is still in effect.

In the light of the above events and in accordance with IFRS 10, on 31 December 2016 Electricaribe ceased to be consolidated on the consolidated balance sheet of Gas Natural Fenosa. Its assets, liabilities and non-controlling interests have been derecognised for a net amount of Euros 475 million and the relevant negative exchange differences amounting to Euros 30 million have been transferred to the income statement. In addition, under IAS 39, the investment in Electricaribe was been recorded at fair value (Euros 475 million) under Available-for-sale financial assets. As the investment in Electricaribe involves unlisted equity instruments and therefore no quoted share price is available, it was valued on Level 3 and a prudent approach was applied in the valuation due to the uncertainty surrounding the current situation, resulting in an amount that does not differ from its carrying amount. The valuation of Electricaribe at 31 December 2016 was performed using a methodology similar to the one described in Note 3.4.5. The main assumptions taken into consideration referred to forecast tariff trends, energy costs, operating and maintenance costs and investments. The discount rate used was 16.6% and the growth rate was 3.0%.

At 31 December 2017 there has been no change in the parameters to which the main assumptions for the measurement of the holding in Electricaribe refer or in the processes described above that could lead to a better evaluation of its fair value. As a result, the amount recorded under “Available-for-sale financial assets” has not changed, except for the effect derived from exchange rate fluctuations.

However, Gas Natural Fenosa believes that the final amount that may reasonably be expected to be recognised by the agencies and courts which, as the case may be, will decide on the applicable price or indemnity based on fair market value, will be higher than the figure mentioned above.

A breakdown of the assets, liabilities and non-controlling interests of Electricaribe recognised in the consolidated balance sheet of Gas Natural Fenosa which were derecognised at 31 December 2016 is as follows:

	At 31/12/2016
Intangible assets	6
Property, plant and equipment	929
Non-current financial assets	63
Deferred tax assets	157
NON-CURRENT ASSETS	**1,155**
Trade and other receivables	633
Other current financial assets	20
Cash and cash equivalents	42
CURRENT ASSETS	**695**
TOTAL ASSETS	**1,850**
NON-CONTROLLING INTERESTS	**70**
Non-current provisions	265
Non-current financial liabilities	85
Deferred tax liabilities	4
NON-CURRENT LIABILITIES	**354**
Current financial liabilities	493
Trade and other payables	450
Other current liabilities	8
CURRENT LIABILITIES	**951**
TOTAL NON-CONTROLLING INTERESTS AND LIABILITIES	**1,375**

The income statement contributed by Electricaribe in 2016 to the consolidated income statement is as follows:

	2016
Revenue	1,453
Procurements	(984)
Other operating income	3
Personnel costs	(53)
Other operating expenses	(166)
Gross operating results	**253**
Depreciation, amortisation and impairment losses	(40)
Impairment of credit losses	(194)
OPERATING PROFIT	**19**
Financial income	5
Financial expenses	(65)
Exchange differences	(1)
NET FINANCIAL INCOME/(EXPENSE)	**(61)**
PROFIT BEFORE TAXES	**(42)**
Corporate income tax	(10)
CONSOLIDATED PROFIT FOR THE YEAR	**(52)**
Attributable to:	
the parent company	(44)
Non-controlling interests	(8)

Loans and receivables

The breakdown at 31 December 2017 and 2016 is as follows:

	At 31/12/2017	At 31/12/2016
Commercial loans	41	56
Gas system income deficit financing	19	357
Deposits and guarantees deposits	135	138
Receivable, revenue from capacity services	85	74
Other loans	459	550
Loans and other receivables non-current	**739**	**1,175**
Commercial loans	70	62
Electricity system income deficit financing	91	106
Gas system income deficit financing	145	144
Dividend receivable	2	8
Other loans	87	68
Loans and other receivables current	**395**	**388**
Total	**1,134**	**1,563**

The breakdown by maturities at December 2017 and 2016 is as follows:

Maturities	At 31/12/2017	At 31/12/2016
No later than 1 year	395	388
Between 1 year and 5 years	289	500
More than 5 years	450	675
Total	**1,134**	**1,563**

The fair values and carrying amounts of these assets do not differ significantly.

“Commercial loans” mainly include the credits for the sale of gas and electricity installations. The respective interest rates (between 5% and 11% for loans from 1 to 5 years) are adjusted to market interest rates for this type of loans and duration.

The item “Electricity system income deficit financing” relates to temporary mismatches between electricity system income and costs funded by Gas Natural Fenosa pursuant to Law 24/2013, December 26 (Note 2.4), generating a recovery right over the following five years and interest at a market rate. The amount of this financing has been entirely recognised as a short-term item on the understanding that it is a temporary mismatch that will be recovered through system settlements within one year.

The heading "Gas system revenue deficit financing" includes temporary mismatches between gas system revenues and costs accumulated in 2017, funded by Gas Natural Fenosa pursuant to Law 18/2014 of 17 October (Note 2.1.1.2). This amount will be recovered through the gas system settlements. The amount pending receipt following the settlements for the year generates a recovery right in the following five years for the remaining amount financed, plus interest at a market rate. The amount of this financing has been recognised in long term and short term items based on the estimated recovery period.

In December 2017 the irrevocable assignment without recourse of the accumulated deficit for 2014, whose nominal amount was Euros 315 million, and the mismatches for 2015 and 2016 (Euros 40 million) to various financial institutions took place, transferring all associated risks and rewards. All the balances at the date of the assignment have therefore been derecognised.

The item "Deposits and guarantees deposits" basically include amounts deposited with the competent Public Administrations, under applicable legislation, in respect of guarantees and deposits received from customers when contracts are concluded to secure the supply of electricity and natural gas (Note 18).

The heading "Receivable, revenue from capacity services" relates to revenue yet to be billed in respect of the levelling of the term of the service contracts for electricity generation capacity assignment with the Mexican Federal Electricity Commission (Note 3.4.19.d).

"Other loans" includes, basically:

- a loan of Euros 169 million (Euros 192 million at 31 December 2016) for financing ContourGlobal La Rioja. S.L. for the sale of the Arrúbal combined cycle plant (La Rioja), which took place on 28 July 2011, of which Euros 16 million is classified under current assets (Euros 15 million in 2016). The loan, which is secured by the shares of this company and by its assets, bears annual interest at a market rate and matures in 2021.

- the value of generation concessions in Costa Rica that are deemed to be credits, pursuant to IFRIC 12 "Service concession arrangements" (Note 3.4.3.b and Note 32), in the amount of Euros 229 million (Euros 276 million at 31 December 2016), of which Euros 13 million is classified in current assets (Euros 12 million in 2016). These credits are classified in the item "Loans and receivables" as they represent an unconditional right to receive cash in fixed or determinable amounts.

Hedging derivatives

The variables upon which the valuation of the hedging derivatives reflected under this heading are based and observable in an active market (Level 2).

Note 17 shows the details of the derivative financial instruments.

Note 9. Non-current assets and disposal groups of assets held for sale and discontinued operations

Non-current assets and liabilities held for sale classified at 31 December 2017

A 31 December 2017, non-current assets held for sale relate to the gas distribution and marketing business in Italy, gas distribution and marketing in Colombia, electricity distribution in Moldova and power generation in Kenya.

As Gas Natural Fenosa has a firm commitment to sell these assets that are clearly identified, the process is under way, it is considered that the sale is highly probable and it is expected to be completed in 2018, the accounting balances of these assets and liabilities have been transferred to "Non-current assets held for sale" and "Liabilities related to non-current assets held for sale", in accordance with IFRS 5 "Non-current assets held for sale and discontinued operations". In addition, it was considered that these are discontinued operations as they are components classified as held for sale which represented a significant and separate line of business or area of operation. Therefore, all income and expenses pertaining to these lines of business for 2017 and 2016 are disclosed under "Profit for the year from discontinued operations, net of taxes".

On 13 October 2017, Gas Natural Fenosa concluded, in separate agreements with 2i Rete Gas and Edison, the sale of its gas distribution and marketing companies in Italy for a total amount of Euros 759 million. On 1 February 2018, following the approval of Italian antitrust authorities, Gas Natural Fenosa has completed the disposal of its gas distribution companies. The sale of the gas supply company is expected to be completed during the first quarter of 2018, subject to the pertinent approval of European antitrust authorities. The transactions are expected to generate overall after-tax capital gains for Gas Natural Fenosa of approximately Euros 190 million. From the date of the agreement, these assets have been considered as non-current assets held for sale.

On 17 November 2017, Gas Natural Fenosa entered into a binding agreement with Brookfield Infrastructure for the sale of its 59.1% interest in Gas Natural SA ESP, a Colombian company engaged in the distribution and retail sale of gas, for 1,678,927 million Colombian pesos (Euros 468 million). The transaction was structured in two phases, the first of which was to be carried out through successive operations on the Colombian stock exchange in December 2017, which would entail the loss of control over Gas Natural S.A. ESP. The remaining interest is to be subsequently transferred by means of a public share offering once certain conditions precedent have been met, mainly the obtainment by the acquiring company of certain administrative authorisations in Colombia, which are expected to be completed in the first half of 2018. From the date of the agreement, these assets have been considered as non-current assets held for sale.

On 20, 21 and 22 December 2017 Gas Natural Fenosa sold 17.2% of its holding in Gas Natural S.A. ESP, for an amount of Euros 134 million which decreased from 59.1% to 41.9%. Following this change in the shareholder structure, at an extraordinary general meeting held on 29 December 2017 the shareholders of Gas Natural S.A. ESP approved the restructuring of its Board of Directors, which is now formed by five members of whom two are appointed by Gas Natural Fenosa, which no longer has a majority representation.

Due to the loss of the majority of the voting rights and members on the Board of Directors of Gas Natural S.A. ESP by Gas Natural Fenosa, the existence of a loss of control at 31 December 2017 has been concluded for accounting purposes. The accounting treatment applied to this transaction has been based on IFRS 10 in relation to the loss of control by a parent over a subsidiary, derecognising all the assets and liabilities of Gas Natural S.A. ESP at carrying value, recognising the fair value of the consideration received for the 17.2% interest and the remaining interest of 41.9 % at fair value, which in this case is the price set in the binding agreement concluded with Brookfield Infrastructure. The resulting difference has been recognised as a profit under after-tax profits of Euros 350 million in "Profit for the year from discontinued operations net of taxes", which includes both the capital gain from the sale of the 17.2% holding for Euros 106 million and the impact of the fair value measurement of the remaining 41.9% interest at Euros 244 million.

Finally, as a result of the strategic review of its business and positioning in various countries, Gas Natural Fenosa has decided to carry out competitive sales processes for its electricity distribution business in Moldova and power generation business in Kenya. These processes are part of the efforts to optimise

Gas Natural Fenosa's business portfolio and the continuous review of its activities and geographies regarded as non-strategic. To estimate the fair value less costs to sell as required by IFRS 5, a Level 3 valuation has been carried out using assumptions similar to those described in Note 3.4.5 and taking into consideration the prices of indicative offers received to date, resulting in a decrease in the carrying amount of the investment in Kenya of Euros 24 million, which is included in profits from discontinued operations net of taxes. At 31 December 2017 these assets have been considered as non-current assets held for sale.

Non-current assets and liabilities held for sale classified at 31 December 2016

On 18 December 2015 Gas Natural Fenosa, which owned a controlling interest through CGE of 56.62% in the Chilean company Gasco, S.A., entered into an agreement with a group of shareholders with an interest of 22.4% in Gasco S.A., named "Familia Perez Cruz", to split Gasco, S.A. into two companies, one devoted to the natural gas business which would remain under the control of Gas Natural Fenosa and the other to the liquefied petroleum gas business (LPG) which would be controlled by the Perez Cruz Family. Following completion of the split, on 6 July 2016 each party launched a public share offering in order to obtain a 100% interest in its company in order to carry out its own independent project. On 8 August 2016 Gas Natural Fenosa reported the sale of the shares in Gasco S.A. totalling 160,197 million Chilean pesos (Euros 220 million), generating a net capital gain of Euros 4 million, in addition to the success of the takeover bid for Gas Natural Chile, S.A. acquiring an additional 37.88% interest for a total of 223,404 million Chilean pesos (Euros 306 million). As a result, Gas Natural Fenosa's controlling interest in Gas Natural Chile, S.A. increased to 94.50%.

In addition, it was considered a discontinued operation since it was a component classified as held for sale which represented a significant line of business, separate from the rest. Therefore, all income and expenses pertaining to the LPG business for 2016 are presented under "Profit for the year from discontinued operations, net of taxes".

At 31 December 2017, the detail by nature of assets classified as held for sale and the associated liabilities is as follows:

	Gas distribution Italy	Gas distribution Columbia	Electricity distribution Moldova	Gas supply Italy	International Electricity Kenya	Total
Intangible assets	597	-	6	35	-	638
Property, plant and equipment	26	-	116	3	43	188
Investments recorded using the equity method	-	327	-	-	-	327
Non-current financial assets	2	-	15	1	-	18
Deferred tax assets	25	-	-	6	-	31
NON-CURRENT ASSETS	**650**	**327**	**137**	**45**	**43**	**1,202**
Inventories	1	-	-	31	8	40
Trade and other receivables	60	-	51	175	15	301
Other current financial assets	1	-	-	2	-	3
Cash and cash equivalents	86	-	49	1	-	136
CURRENT ASSETS	**148**	**-**	**100**	**209**	**23**	**480**
TOTAL ASSETS	**798**	**327**	**237**	**254**	**66**	**1,682**
Grants	-	-	9	-	-	9
Non-current provisions	6	-	-	2	-	8
Non-current financial liabilities	44	-	3	-	-	47
Deferred tax liabilities	20	-	2	-	9	31
Other non-current liabilities	-	-	-	19	-	19
NON-CURRENT LIABILITIES	**70**	**-**	**14**	**21**	**9**	**114**
Current financial liabilities	219	-	3	69	37	328
Trade and other payables	40	-	29	90	4	163
Other current liabilities	11	-	-	-	5	16
CURRENT LIABILITIES	**270**	**-**	**32**	**159**	**46**	**507**
TOTAL LIABILITIES	**340**	**-**	**46**	**180**	**55**	**621**

Breakdowns by nature of the heading “Profit for the year from discontinued operations net of taxes” in the consolidated income statement for 2017 and 2016 are as follows:

2017	Gas distribution Italy	Gas distribution Columbia	Electricity distribution Moldova	Gas marketing Italy	International Electricity Kenya	Total
Revenue	85	745	203	140	53	1,226
Procurements	(1)	(511)	(162)	(91)	(25)	(790)
Other operating income	36	11	-	4	1	52
Personnel costs	(12)	(14)	(7)	(6)	(2)	(41)
Other operating expenses	(49)	(89)	(16)	(25)	(8)	(187)
Release of fixed assets grants to income and other	-	-	-	-	-	-
GROSS OPERATING PROFIT	**59**	**142**	**18**	**22**	**19**	**260**
Depreciation, amortisation and impairment expenses	(18)	(13)	(6)	(1)	(8)	(46)
Impairment of credit losses	-	(3)	-	(10)	-	(13)
Other results (1)	-	350	-	-	(24)	326
OPERATING PROFIT	**41**	**476**	**12**	**11**	**(13)**	**527**
Financial income	1	18	5	-	-	24
Financial expenses	(3)	(13)	(1)	-	(4)	(21)
Exchange differences	-	-	(1)	-	-	(1)
NET FINANCIAL INCOME/(EXPENSE)	**(2)**	**5**	**3**	**-**	**(4)**	**2**
Profit/(loss) on equity method companies	-	-	-	-	-	-
PROFIT BEFORE TAXES	**39**	**481**	**15**	**11**	**(17)**	**529**
Corporate income tax	(9)	(51)	(3)	(4)	(2)	(69)
PROFIT FOR THE YEAR FROM DISCONTINUED OPERATIONS	**30**	**430**	**12**	**7**	**(19)**	**460**
Attributable to:						
the parent company	30	393	12	7	(14)	428
Non-controlling interests	-	37	-	-	(5)	32

(1) Gas Distribution Colombia includes the capital gain on the sale of the shareholding and the impact of the fair-value measurement of the remaining interest. International Electricity Kenya includes the reduction in the carrying amount of the investment to measure it at fair value less costs to sale.

2016	Gas distribution Italy	Gas distribution Columbia	Electricity distribution Moldova	Gas marketing Italy	International Electricity Kenya	Restated data under NIIF 5(1)	GLP(2)	Total
Revenue	88	779	226	140	43	**1,276**	391	**1,667**
Procurements	(1)	(531)	(169)	(92)	(16)	**(809)**	(263)	**(1,072)**
Other operating income	21	-	3	-	1	**25**	2	**27**
Personnel costs	(11)	(13)	(6)	(7)	(2)	**(39)**	(26)	**(65)**
Other operating expenses	(37)	(72)	(12)	(20)	(8)	**(149)**	(36)	**(185)**
Release of fixed assets grants to income and other	2	-	-	-	-	**2**	-	**2**
GROSS OPERATING PROFIT	**62**	**163**	**42**	**21**	**18**	**306**	**68**	**374**
Depreciation, amortisation and impairment expenses	(24)	(13)	(5)	(2)	(8)	**(52)**	-	**(52)**
Impairment of credit losses	-	(4)	-	(8)	-	**(12)**	-	**(12)**
Other results	-	-	-	-	-	**-**	4	**4**
OPERATING PROFIT	**38**	**146**	**37**	**11**	**10**	**242**	**72**	**314**
Financial income	-	7		-	-	**7**	1	**8**
Financial expenses	(3)	(6)	(2)	-	(6)	**(17)**	(15)	**(32)**
Exchange differences						**-**	(1)	**(1)**
NET FINANCIAL INCOME/(EXPENSE)	**(3)**	**1**	**(2)**	**-**	**(6)**	**(10)**	**(15)**	**(25)**
Profit/(loss) on equity method companies	-	-	-	-	-	**-**	1	**1**
PROFIT BEFORE TAXES	**35**	**147**	**35**	**11**	**4**	**232**	**58**	**290**
Corporate income tax	(10)	(60)	(5)	(5)	(3)	**(83)**	(14)	**(97)**
PROFIT FOR THE YEAR AFTER TAXES FROM DISCONTINUED OPERATIONS	**25**	**87**	**30**	**6**	**1**	**149**	**44**	**193**
Attributable to:								
the parent company	25	48	30	6	1	**110**	22	**132**
Non-controlling interests	-	39	-	-	-	**39**	22	**61**

(1) Note 3.3.

(1) Relates to the period 1 January 2016 to 8 August 2016 (date on which the shares were sold).

Total comprehensive income on this activity in the years ended 31 December 2017 and 2016 breaks down as follows:

2017	Gas distribution Italy	Gas distribution Columbia	Electricity distribution Moldova	Gas marketing Italy	International Electricity Kenya	GLP	Total
Consolidated profit/(loss) for the year	30	430	12	7	(19)	-	460
Other comprehensive income recognised directly in equity:							
Currency translation differences	-	(13)	(6)	-	(8)	-	(27)
Releases to income statement:							
Currency translation differences	-	13	-	-	-	-	13
Total comprehensive income for the year	**30**	**430**	**6**	**7**	**(27)**	**-**	**446**

2016	Gas distribution Italy	Gas distribution Columbia	Electricity distribution Moldova	Gas marketing Italy	International Electricity Kenya	GLP1	Total
Consolidated profit/(loss) for the year	25	87	30	6	1	44	193
Other comprehensive income recognised directly in equity:							
Currency translation differences	-	3	4	-	2	27	36
Releases to income statement:							
Currency translation differences	-	-	-	-	-	(6)	(6)
Total comprehensive income for the year	**25**	**90**	**34**	**6**	**3**	**65**	**223**

(1) Relates to the period 1 January 2016 to 8 August 2016 (date on which the shares were sold).

The cash flows from discontinued operations included in the consolidated cash flow statements are:

2017 Cash flow from:	Gas distribution Italy	Gas distribution Columbia	Electricity distribution Moldova	Gas marketing Italy	International Electricity Kenya	GLP	Total
Operation	42	88	53	13	8	-	204
Investment	(28)	(23)	(15)	(3)	(1)	-	(70)
Financing	-	(75)	(17)	(10)	(7)	-	(109)

2016 Cash flow from:	Gas distribution Italy	Gas distribution Columbia	Electricity distribution Moldova	Gas marketing Italy	International Electricity Kenya	GLP[(1)]	Total
Operation	37	70	33	5	25	46	216
Investment	(31)	(28)	(15)	(3)	(7)	(17)	(101)
Financing	(9)	(52)	3	(1)	(18)	(32)	(109)

[(1)] Relates to the period 1 January 2016 to 8 August 2016 (date on which the shares were sold).

Transactions between the companies making up the discontinued business with other group companies are not significant. Therefore, intragroup cash flows with the discontinued business are not significant.

Note 10. Inventories

The breakdown of Inventories is as follows:

	At 31/12/2017	At 31/12/2016
Natural gas and liquefied gas	388	421
Coal and fuel oil	62	76
Nuclear fuel	57	65
CO_2 emission allowances	68	60
Raw materials and other inventories	145	136
Total	**720**	**758**

At 31 December 2017, Gas Natural Fenosa has commitments for the acquisition of inventories amounting to Euros 36 million (Euros 35 million at 31 December 2016), of which Euros 35 million relates to nuclear fuel (Euros 34 million at 31 December de 2016) and Euros 1 million relates to CO_2 (Euros 1 million at 31 December 2016).

Gas inventories basically include the inventories of gas deposited in underground storage units, sea transport, plants and pipelines.

Note 11. Trade and other receivables

The breakdown of this account is as follows:

	At 31/12/2017	At 31/12/2016
Trade receivables	4,910	4,939
Receivables with related companies (Note 33)	87	85
Impairment of credit losses provision	(650)	(676)
Trade receivables	4,347	4,348
Public Administrations	71	144
Prepayments	81	70
Derivative financial instruments (see Note 17)	38	46
Sundry receivables	279	229
Other receivables	469	489
Current income tax asset	178	162
Total	**4,994**	**4,999**

The fair values and carrying amounts of these assets do not differ significantly.

In general, the outstanding invoices do not accrue interest as they fall due in an average period of 20 days.

The movement in the impairment on credit losses is as follows:

	2017	2016
At 1 January	**(676)**	**(890)**
Net charge on Impairment of credit losses	(155)	(327)
Write offs	123	336
Currency translation differences	14	(21)
Transfers and other (1)	44	226
At 31 December	**(650)**	**(676)**

(1) In 2016 it mainly includes the derecognition of the Electricaribe balances due to the deconsolidation of the holding following the loss of control (Note 8).
In 2017 it mainly includes the transfers to “Non-current assets held for sale” to the date on which this classification applies (Note 9).

Note 12. Cash and cash equivalents

Cash and cash equivalents include:

	At 31/12/2017	At 31/12/2016
Cash at banks and in hand	1,946	985
Short term investments (Spain and rest of Europe)	1,192	618
Short term investments (International)	87	464
Total	**3,225**	**2,067**

The investments in cash equivalents mature in less than three months and bear a weighted effective interest rate 1.6% at 31 December 2017 (0.4% at 31 December 2016).

At 31 December 2017 and 2016 there are not sovereign debt collocations and unexist restrictions of significant value to the cash withdrawals.

Note 13. Equity

The main elements of Equity are broke down as follows:

Share capital and share premium

The variations in 2017 and 2016 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 01 January 2016	**1,000,689,341**	**1,001**	**3,808**	**4,809**
Variation	-	-	-	-
At 31 December 2016	**1,000,689,341**	**1,001**	**3,808**	**4,809**
Variation	-	-	-	-
At 31 December 2017	**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 Companies Act 2010.

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 representative holdings in the share capital of Gas Natural SDG, S.A. at 31 December 2017, in accordance with the public information available or the communication issued by the Company itself, are as follows:

	Interest in share capital %	
	2017	**2016**
- Fundación Bancaria Caixa d'Estalvis i Pensions de Barcelona,"la Caixa"(1)	24.4	24.4
- Repsol, S.A.	20.1	20.1
- Global Infrastructure Partners III (2)	20.0	20.0
- Sonatrach	4.0	4.0

(1) Through Criteria Caixa S.A.U.
(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.

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

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

The share price at the end of 2017 of Gas Natural SDG, S.A. is Euros 19.25 (Euros 17.91 at 31 December 2016).

Reserves

"Reserves" includes the following reserves:

	2017	**2016**
Legal reserve	200	200
Statutory reserve	100	100
Revaluation Reserve Royal Decree-Law 7/96	-	225
Goodwill reserve	191	496
Voluntary reserves	7,200	6,603
Other reserves	2,213	1,925
	9,904	**9,549**

At the annual general meeting of Gas Natural SDG, S.A. held on 20 April 2017, the shareholders agreed to the transfer to Voluntary Reserves of Euros 305 million from the Goodwill Reserve and Euros 225 million from the Royal Decree-Law 7/96 Revaluation 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 articles of association of Gas Natural SDG, S.A., 2% of net income for the year must be allocated to the statutory reserves until it reaches at least 10% of share capital.

Revaluation reserve

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

Goodwill reserve

Law 22/2015 on Auditing 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.

Treasury shares

Movements during 2017 and 2016 involving the treasury shares of Gas Natural SDG, S.A. are as follows:

	Number of shares	In million euro	% Capital
At 01 January 2016	-	-	-
Acquisitions	3,049,189	53	0.3%
Disposals	(2,298,644)	(40)	(0.2%)
At 31 December 2016	**750,545**	**13**	**0.1%**
Acquisitions	7,623,586	147	0.8%
Delivered to employees	(336,625)	(7)	-
Disposals	(8,037,506)	(153)	(0.8%)
At 31 December 2017	**-**	**-**	-

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 2017 the profit made on transactions involving treasury shares of Gas Natural Fenosa amounted to Euros 0.5 million, recognised under "Other reserves" (Euros 0.4 million profit in 2016).

Movements during 2017 and 2016 involving the treasury shares of Compañía General de Electricidad, S.A. and CGE Gas Natural, S.A. are as follows:

	Number of shares		In million euro
	Compañía General de Electricidad, S.A.	CGE Gas Natural, S.A.	
At 01 January 2016	-		-
Acquisitions	8,695,395	8,695,395	8
Disposals and others	-	-	-
At 31 December 2016	**8,695,395**	**8,695,395**	**8**
Acquisitions	6,466,178	5,373,555	9
Disposals and others	(8,695,395)	(8,695,395)	(8)
At 31 December 2017	**6,466,178**	**5,373,555**	**9**

The shares recorded in 2016 were acquired following the merger in which Compañía General de Electricidad, S.A. was absorbed into Gas Natural Fenosa Chile, S.A., as a result of which the shareholders of both companies obtained a right of withdrawal under which they sold their shares to the company. This right was exercised by 44 shareholders owning 8,695,395 shares in Compañía General de Electricidad, S.A., which was subsequently split into two companies (Compañía General de Electricidad, S.A. and CGE Gas Natural, S.A.). One year having elapsed, these shares have been redeemed.

The shares registered in 2017 were acquired from shareholders that held rights of withdrawal following the merger by absorption of Transnet, S.A., Emel Norte, S.A. and Emelat Inversiones, S.A. into Compañía General de Electricidad on 8 February 2017 and 27 July 2017, and following the merger by absorption of Gas Natural Chile, S.A. into CGE Gas Natural, S.A. on 31 May 2017.

Treasury shares acquired resulting from the right of withdrawal must be disposed of in the securities market within a maximum of one year, at the end of which they must be redeemed if they have not been sold.

Earnings per share

The earnings per share are calculated by dividing the net income attributable to the equity holders of the parent Company by the average weighted number of ordinary shares in circulation during the year.

	At 31/12/2017	At 31/12/2016
Profit attributable to equity holders of the parent company	1,360	1,347
Weighted average number of ordinary shares in issue	1,000,478,210	1,000,468,342
Earnings per share from continuing operations (in euro):		
- Basic	0.93	1.22
- Diluted	0.93	1.22
Earnings per share from discontinued operations (in Euros):		
- Basic	0.43	0.13
- Diluted	0.43	0.13

The average weighted number of ordinary shares used in the calculation of earnings per share in 2017 and 2016 is as follows:

	2017	2016
Weighted average number of ordinary shares	1,000,689,341	1,000,689,341
Weighted average number of treasury shares	(211,131)	(220,999)
Weighted average number of shares in issue	1,000,478,210	1,000,468,342

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

Dividends

Set out below is a breakdown of the payments of dividends made in 2017 and 2016:

	31.12.17			31.12.16		
	% of Nominal	**Euros per share**	**Amount**	**% of Nominal**	**Euros per share**	**Amount**
Ordinary shares	100%	1.00	1,001	133%	1.330	1,331
Other shares (without voting rights, redeemable, etc.)	-	-	-	-	-	-
Total dividends paid	**100%**	**1.00**	**1,001**	**133%**	**1.330**	**1,331**
a) Dividends charged to income statement	100%	1.00	1,001	133%	1.330	1,331
b) Dividends charged to reserves or share premium account	-	-	-	-	-	-
c) Dividends in kind	-	-	-	-	-	-

Additionally, dividends paid to non-controlling shareholders in 2017 amounted to Euros 283 million (Euros 195 million in 2016). See "Non-controlling interest" section of this note, so the total of dividends paid amounted to Euros 1,284 million (Euros 1,526 million in 2016).

2017

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

On 25 July 2017 the Board of Directors approved the payment of an interim dividend out of 2017 profits of Euros 0.330 per share, for a total of Euros 330 million, paid on 27 September 2017.

The Parent company had sufficient liquidity to pay out the interim dividend at the approval date, pursuant to the Spanish Companies Act 2010. The Parent company's provisional liquidity statement drawn up by the Directors at 25 July 2017 is as follows:

Profit after tax		449
Reserves to be recognised		-
Maximum amount distributable		449
Forecast interim dividend payment		330
Cash resources	301	
Debt issue and undrawn credit facilities	6,940	
Total liquidity		7,241

On 6 February 2018, the Board of Directors approved the following proposal for the distribution of Gas Natural SDG, S.A.'s net profit for 2017, for submission to the Annual General Meeting:

Available for distribution	
Profit/(loss)	1,024
Gas	
To Voluntary reserve	23
To Dividend	1,001

This proposal for the distribution of profits prepared by the Board for approval by the Annual General Meeting includes the payment of a supplementary dividend of Euros 0.67 per share for each qualifying share outstanding at the proposed date of payment, 27 June 2018.

The voting rights attaching to the treasury shares, except for the right to the free assignment of new shares, will be allocated proportionally to the remaining shares.

2016

This included the payment of an interim dividend of Euros 0.408 per share out of 2015 profits, for a total amount of Euros 408 million, agreed on 30 October 2015 and paid out on 8 January 2016.

The General Shareholders Meeting held on 4 May 2016 approved a complementary dividend of Euros 0.592 per share for a total of Euros 593 million, paid on 30 June 2016.

On 22 July 2016 the Board of Directors approved the payment of an interim dividend out of 2016 profits of Euros 0.330 per share, for a total of Euros 330 million, paid on 27 September 2016.

Adjustments for changes in value

Below is the movement of Adjustments due to change in value:

	Available-for-sale financial assets	Hedging operations	Investments recorded using the equity method	Tax effect	Total reserves for revaluation of assets and liabilities	Currency translation differences	Total
1.1.2016	**5**	**(144)**	**(15)**	**39**	**(115)**	**(498)**	**(613)**
Change in market value	4	111	2	(32)	**85**	283	368
Taken to income statement	-	106	9	(30)	**85**	32	117
Other	-	(1)	-	-	**(1)**	-	(1)
31.12.2016	**9**	**72**	**(4)**	**(23)**	**54**	**(183)**	**(129)**
Change in market value	(54)	(113)	(4)	13	(158)	(729)	(887)
Taken to income statement	-	(1)	3	1	3	13	16
Other	-	-	-	-	-	-	-
31.12.2017	**(45)**	**(42)**	**(5)**	**(9)**	**(101)**	**(899)**	**(1,000)**

The item “Currency translation differences" includes the exchange differences described in Note 3.4.2 as a result of the euro's fluctuation against the main currencies of Gas Natural Fenosa's foreign companies.

Non-controlling interests

	Non-controlling interests
Balance at 01/01/2016	**4,151**
Total comprehensive income for the year	470
Distribution of dividends	(214)
Sale of Gasco, S.A.	(196)
Purchase 37.88% Gas Natural Chile, S.A.	(314)
Payments return on other equity instruments	(58)
Loss of control Electricaribe (Note 8)	(70)
Business combinations (Note 31)	8
Other changes	3
Balance at 31/12/2016	**3,780**
Total comprehensive income for the year	162
Distribution of dividends	(233)
Sale of Gas Natural, S.A. ESP (Note 9)	(73)
Payments return on other equity instruments	(58)
Other changes	(7)
Balance at 31/12/2017	**3,571**

In August 2017 the sale of 20% of the Gas Distribution Spain business to a long-term infrastructure investor consortium made up of Allianz Capital Partners (ACP) and Canada Pension Plan Investment

Board (CPPIB) was agreed for Euros 1,500 million. The transaction is expected to be completed in 2018 subject to the pertinent authorisations. In addition, the transfer does not lead to a loss of control by Gas Natural Fenosa and therefore it will continue to be consolidated using the full consolidation method.

The most significant movements for 2017 relate to:

- Derecognition of non-controlling interests pertaining to Gas Natural S.A. ESP due to the sale of 17.2% and loss of control at 31 December 2017 (Note 9)

- Other changes:

  As a result of the redemption of treasury shares in Chile, the heading Non-controlling interests has been reduced by Euros 8 million.

The most significant movements for 2016 relate to:

- On 8 August 2016 the liquefied petroleum gas business was sold in Chile, generating a net capital gain of Euros 4 million and a reduction in “Non-controlling interests” of Euros 196 million (Note 9).

- On the same date, following the successful takeover bid for Gas Natural Chile, S.A. an additional 37.88% of its capital was acquired for Euros 306 million. As this is an acquisition of non-controlling interests, it was recognised as an equity transaction, entailing a decrease in Non-controlling interests of Euros 314 million and an increase in Reserves of Euros 2 million.

- Other changes:

  In December 2016, an additional 6.9% of Gas Galicia, S.A. was acquired for Euros 6 million, taking the controlling interest to 68.5%. As this is an acquisition of non-controlling interests, it was recognised as an equity transaction, entailing a decrease in "Non-controlling interests" of Euros 3 million and a decrease in "Reserves" of Euros 3 million.

  At 31 December 2016 it also included the acquisition of other additional investments in subsidiaries of Euros 6 million.

Subordinated debentures

Gas Natural Fenosa Finance, B.V issued, in previous years, the following perpetual subordinated debentures for an aggregate amount of Euros 1,500 million:

Issuance	Nominal	Early redemption option	Coupon
November 2014	1,000	2022	4.125%
April 2015	500	2024	3.375%

Nonetheless, Gas Natural Fenosa must pay it if dividends are paid out or the decision to exercise the early redemption option is taken.

Although no contractual maturity has been established for these debentures, Gas Natural Fenosa Finance, B.V. has the option to redeem them early on the early redemption option date and subsequently on every interest payment date.

Gas Natural Fenosa recognised the cash received in “Non-controlling interests” under equity in the consolidated balance sheet on the understanding that the issues did not meet the conditions to be considered as a financial liability, because Gas Natural Fenosa Finance B.V. does not have a contractual commitment to hand over cash or any other financial asset nor any obligation to exchange financial assets or liabilities; the circumstances whereby it would be obligated in this respect are entirely at the discretion of Gas Natural Fenosa Finance, B.V.

The interest accrued in 2017 and 2016 amounts to Euros 58 million and has been recognised in “Non-controlling interests” in the consolidated income statement for 2017 and 2016.

Preferred shares

Unión Fenosa Preferentes, S.A.U. carried out in 2005 a preference share issue for a nominal amount of Euros 750 million, which was bought back in cash Euros 640 million in 2015, so the rest has remained outstanding.

Dividend were variable non-accumulative: it will accrued an interest of Euribor at three months plus a spread of 1.65%. The dividend will be paid by calendar quarters in arrears, depending on the existence of distributable profit of Gas Natural Fenosa,(considering as such the lesser of the net profit declared by the Gas Natural Fenosa and the net profit of Gas Natural SDG, S.A. as guarantor) and the payment of Gas Natural SDG, S.A. dividend. Unión Fenosa Preferentes, S.A.U. will have the option but not the obligation to pay the shareholders remuneration in kind by increasing the nominal value of the preference shares.

The shares are perpetual, with the option for the issuer of redemptions at par value.

Gas Natural Fenosa has recognised the cash received in “Non-controlling interests” under equity in the consolidated balance sheet on the understanding that the issues did not meet the conditions to be considered as a financial liability, because Unión Fenosa Preferentes, S.A.U. does not have a contractual commitment to hand over cash or any other financial asset nor any obligation to exchange financial assets or liabilities; the circumstances whereby it would be obligated in this respect are entirely at the discretion of Unión Fenosa Preferentes, S.A.U.

Set out below is a breakdown of the most significant non-controlling interests:

	2017			2016		
Company	**Attributed equity**	**Consolidated profit for the year**	**Dividends and other remuneration**	**Attributed equity**	**Consolidated profit for the year**	**Dividends and other remuneration**
Metrogas, S.A.	596	27	15	605	46	13
Companhia Distribuidora de Gás do Río de Janeiro, S.A.	176	41	25	205	35	12
Global Power Generation, S.A	84	(3)	14	114	(2)	19
Fuerza y Energía de Tuxpan S.A. de CV	101	9	-	115	10	-
Empresa de Distribución Eléctrica Metro Oeste, S.A.	89	8	-	101	11	-
Ecoelectrica L.P.	102	17	-	83	14	14
Kangra Coal (Proprietary), Ltd	59	(2)	-	75	(6)	-
Europe Maghreb Pipeline, Ltd.	54	56	56	63	40	42
Gas Natural Mexico, S.A. de CV	61	7	1	61	7	3
Gas Natural, S.A. ESP	-	25	35	49	29	28
Ceg Río, S.A.	43	10	4	46	6	3
Aprovisionadora global de energía, S.A. (1)	45	15	40	39	65	32
Other companies	549	67	42	612	50	47
Subtotal	**1,959**	**277**	**232**	**2,168**	**305**	**213**
Preferred shares	110	2	1	110	1	1
Subordinated perpetual debentures	1,502	58	58	1,502	58	58
Other equity instruments	**1,612**	**60**	**59**	**1,612**	**59**	**59**
Total	**3,571**	**337**	**291**	**3,780**	**364**	**272**

(1) 2016 profits include the impact on non-controlling interests of the capital gain on the sale of GNL Quintero S.A. (Note 7) for Euros 39 million.

Dividends paid to non-controlling interests in 2016 amounted to Euros 283 million (Euros 195 million in 2016).

Set out below are financial highlights for the most significant non-controlling shareholdings (amounts at 100%):

	31 December 2017			31 December 2016		
Company	**Total assets**	**Non-current liabilities**	**Current liabilities**	**Total assets**	**Non-current liabilities**	**Current liabilities**
Metrogas, S.A.	2,138	(726)	(75)	2,216	(759)	(88)
Companhia Distribuidora de Gás do Río de Janeiro, S.A.	853	(239)	(217)	909	(205)	(239)
Global Power Generation, S.A.	420	(4)	(80)	542	(5)	(86)
Fuerza y Energía de Tuxpan S.A. de CV	987	(117)	(43)	1,151	(174)	(33)
Empresa de Distribución Eléctrica Metro Oeste, S.A.	921	(321)	(294)	920	(218)	(350)
Ecoelectrica L.P.	368	(3)	(7)	409	(32)	(33)
Kangra Coal (Proprietary), Ltd	295	(81)	(5)	377	(101)	(8)
Europe Maghreb Pipeline, Ltd.	256	(1)	(17)	292	(1)	(15)

Gas Natural Mexico, S.A. de CV	819	(202)	(211)	809	(314)	(90)
Gas Natural, S.A. ESP	-	-	-	334	(68)	(145)
Ceg Río, S.A.	271	(96)	(64)	277	(85)	(74)
Aprovisionadora global de energía, S.A.	151	(32)	(18)	181	(18)	(72)

Appendix I contains a breakdown of Gas Natural Fenosa's investee companies, stating their activity and the percentage of the shareholding and equity interest.

The analysis performed to determine that Gas Natural Fenosa exercises control over the consolidated entities identified no cases requiring a complex judgement, since Gas Natural Fenosa is entitled to variable returns from its involvement in the investee and has the capacity to influence those returns through its power in the investee, based on Gas Natural Fenosa's representatives on the Board of Directors and its participation in significant decisions. Additionally, in general terms, there are no significant restrictions, such as protective rights, on Gas Natural Fenosa's capacity to access or utilise assets, or to settle liabilities.

Note 14. Deferred income

The breakdown and the movements under this heading in 2017 and 2016 have been as follows:

	Capital grants	Revenues from pipeline networks and branch lines	Other	Total
At 01/01/2016	**168**	**588**	**97**	**853**
Amount received	6	38	5	49
Release to income	(9)	(25)	(9)	(43)
Currency translation differences	1	(1)	(2)	(2)
Transfers and other	(10)	(2)	(3)	(15)
At 31/12/2016	**156**	**598**	**88**	**842**
Amount received	4	48	2	54
Release to income	(10)	(25)	(7)	(42)
Currency translation differences	(2)	(3)	(2)	(7)
Assets and liabilities held for sale (Note 9)	(10)	-	-	(10)
Transfers and other	(17)	-	22	5
At 31/12/2017	**121**	**618**	**103**	**842**

This heading mainly includes:

- Capital grants relating basically to agreements with the Regional Governments and other entities for the gasification of municipalities and other investments in gas infrastructure, for which Gas Natural Fenosa has met all the conditions established, are stated at the amount granted.
- Income received for the construction of connection facilities for the gas or electricity distribution network (undertaken), which are booked for the cash received, as well as assignments received for these facilities, which are booked, in accordance with IFRIC 18, at their fair value, since both the cash and the facilities are received in consideration for an ongoing service of providing access to the network during the life of the facilities.
- In section “Other” mainly includes income from the extension of the pipeline network that will be financed by third parties.

Note 15. Provisions

The breakdown of provisions at 31 December 2017 and 2016 is as follows:

	At 31/12/2017	At 31/12/2016
Provisions for employee obligations	465	489
Other provisions	664	759
Non-current provisions	**1,129**	**1,248**
Current provisions	183	158
Total	**1,312**	**1,406**

Provisions for employee obligations

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

	2017			2016		
	Pensions and other similar obligations	Other obligations with personnel	Total	Pensions and other similar obligations	Other obligations with personnel	Total
At 1 January	**479**	**10**	**489**	**650**	**9**	**659**
Contributions charged to profits	23	9	32	42	10	52
Payments during the year	(29)	-	(29)	(44)	-	(44)
Currency translation differences	(10)	-	(10)	25	-	25
Changes recognised directly in equity	(5)	-	(5)	51	-	51
Transfers and other applications (2)	(3)	(9)	(12)	(245)	(9)	(254)
At 31 December	**455**	**10**	**465**	**479**	**10**	**489**

(1) In 2017 it mainly includes the transfers to "Non-current assets held for sale" to the date on which this classification applies (Note 9). In 2016 it mainly included the derecognition of the Electricaribe balances due to the deconsolidation of the holding following the loss of control (Note 8).

Pensions and other similar obligations

The breakdown of the provisions for post-employment pension obligations by country is as follows:

Breakdown by country	At 31/12/2017	At 31/12/2016	At 01/01/2016
Spain (1)	342	368	362
Colombia (2)	-	-	196
Brazil (3)	50	40	25
Chile (4)	50	54	48
Mexico (5)	11	11	14
Rest	2	6	5
Total	**455**	**479**	**650**

1) Pension plans and other post-employment benefits in Spain

Most of the post-employment obligations of Gas Natural Fenosa in Spain consist of the contribution of defined amount to occupational pension plan systems. Nevertheless, at 31 December 2017 and 31 December 2016, Gas Natural Fenosa 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.

2) Pension plans and other post-employment benefits in Colombia

In 2016 the following obligations existed with certain employees of the Colombian company Electrificadora del Caribe, S.A. E.S.P:

- Pension liabilities for retired personnel.
- Electricity for current and retired personnel.
- Healthcare and other post-retirement aid.

3) Pension Plans and Other post-employment benefits in Brazil

At 31 December 2017 and at 31 December 2016, Gas Natural Fenosa has the following benefits for certain employees in Brazil:

- Defined post-employment benefits plan, covering retirement, death on the job and disability pensions and overall amounts.
- Post-employment healthcare plan.
- Other defined post-employment benefit plans that guarantee temporary pensions, life-time pensions and overall amounts depending on seniority.

4) Pension plans and Other post-employment benefits in Chile

At 31 December 2017 and 2016 Gas Natural Fenosa has the following benefits in force for certain employees in Chile:

- Termination benefits for employees due to retirement, dismissal or death, calculated based on length of service.
- Pension supplements for employees hired prior to 1992 in some electricity distribution companies.
- Length-of-service awards payable at 5, 10, 15, 20, 25 and 30 years of service.

5) Pension Plans and Other post-employment benefits in Mexico

At 31 December 2017 and at 31 December 2016, Gas Natural Fenosa has the following benefits for certain employees in Mexico:

- Length-of-service award payable after 15 years of service
- Severance indemnity for employees without the service requirement, payable in the event of death at work, incapacity or redundancy.
- Severance indemnity equivalent to three months' salary plus 20 days' salary per year of service.
- Additional compensation only in the event of retirement equal to 1% of the base salary per year of service.

The breakdown of the provisions for pensions and liabilities, by country, recognised in the consolidated balance sheet and the fair value of the plan-related assets is as follows:

	2017				2016				
	Spain	**Brazil**	**Chile**	**Mexico**	**Spain**	**Colombia**	**Brazil**	**Chile**	**Mexico**
Present value of obligations									
At 1 January	**1,203**	**146**	**54**	**12**	**1,173**	**196**	**96**	**48**	**14**
Service cost for the year	6	-	2	1	**5**	**-**	**-**	**4**	**-**
Interest cost	15	15	3	1	**23**	**17**	**15**	**3**	**1**
Changes recognised in equity	(47)	19	(1)	(1)	**77**	**35**	**22**	**-**	**-**
Benefits paid	(74)	(11)	(6)	-	**(75)**	**(22)**	**(11)**	**(5)**	**-**
Currency translation differences	-	(20)	(3)	(1)	**-**	**17**	**24**	**4**	**(3)**
Transfers and other (1)	-	-	1	-	**-**	**(243)**	**-**	**-**	**-**
At 31 December	**1,103**	**149**	**50**	**12**	**1,203**	**-**	**146**	**54**	**12**
Fair value of plan assets									
At 1 January	**835**	**106**	**-**	**1**	**811**	**-**	**71**	**-**	**-**
Expected yield	10	11	-	-	**15**	**-**	**12**	**-**	**-**
Contributions	7	3	-	-	**(2)**	**-**	**4**	**-**	**-**
Changes recognised in equity	(29)	4	-	-	**71**	**-**	**13**	**-**	**-**
Benefits paid	(62)	(11)	-	-	**(60)**	**-**	**(11)**	**-**	**-**
Currency translation differences	-	(14)	-	-	**-**	**-**	**17**	**-**	**-**
Transfers and other	-	-	-	-	**-**	**-**	**-**	**-**	**1**
At 31 December	**761**	**99**	**-**	**1**	**835**	**-**	**106**	**-**	**1**
Provisions for pensions and similar obligations	**342**	**50**	**50**	**11**	**368**	**-**	**40**	**54**	**11**

(1) It mainly includes the derecognition of the Electricaribe balances due to the deconsolidation of the holding following the loss of control (Note 8).

The amounts recognised in the consolidated income statement for the above-mentioned pension plans are as follows:

	2017				2016				
	Spain	Brazil	Chile	Mexico	Spain	Colombia	Brazil	Chile	Mexico
Service cost for the year	6	-	2	1	5	-	-	4	-
Past service cost	-	-	-	-	-	-	-	-	-
Interest cost	15	15	3	1	23	17	15	3	1
Expected return on plan assets	(9)	(11)	-	-	(15)	-	(12)	-	-
Total charge to the income statement	**12**	**4**	**5**	**2**	**13**	**17**	**3**	**7**	**1**

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

	2017				2016				
	Spain	Brazil	Chile	Mexico	Spain	Colombia	Brazil	Chile	Mexico
1 to 5 years	2	-	-	-	5	-	-	-	-
5 to 10 years	22	2	28	3	37	-	2	29	2
More than 10 years	318	48	22	8	326	-	38	25	9
Provisions for pensions and similar obligations	**342**	**50**	**50**	**11**	**368**	**-**	**40**	**54**	**11**

The weighted average term of defined benefit commitments is as follows:

	2017				2016				
Years	Spain	Brazil	Chile	Mexico	Spain	Colombia	Brazil	Chile	Mexico
Weighted average term of pension commitments	11.66	10.10	10.10	17.76	11.33	-	9.84	10.26	19.45

Movements in the liability recognised in the consolidated balance sheet are as follows:

	2017				2016				
	Spain	Brazil	Chile	Mexico	Spain	Colombia	Brazil	Chile	Mexico
At 1 January	**368**	**40**	**54**	**11**	**362**	**196**	**25**	**48**	**14**
Charge against the income statement	11	4	5	2	13	17	3	7	1
Contributions paid	(19)	(3)	(6)	-	(13)	(22)	(4)	(5)	-
Changes recognised in equity	(18)	15	(1)	-	6	35	9	-	-
Transfers	-	-	1	(1)	-	(243)	-	-	(1)
Currency translation differences	-	(6)	(3)	(1)	-	17	7	4	(3)
Other	-	-	-	-	-	-	-	-	-
Business Combinations	-	-	-	-	-	-	-	-	-
Discontinued operations	-	-	-	-	-	-	-	-	-
At 31 December	**342**	**50**	**50**	**11**	**368**	**-**	**40**	**54**	**11**

The amount of cumulative actuarial gains and losses recognised directly in equity is negative by Euros 102 million in 2017 (Spain: negative by Euros 37 million, Brazil: negative by Euros 57 million, Chile: negative by Euros 4 million, and Mexico: negative by Euros 4 million). In 2016, the cumulative negative figure was Euros 107 million (Spain: negative by Euros 55 million, Brazil: negative by Euros 42 million, Chile: negative by Euros 5 million, and Mexico: negative by Euros 5 million).

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

	2017				2016				
	Spain	Brazil	Chile	Mexico	Spain	Colombia	Brazil	Chile	Mexico
Financial assumptions	(23)	21	(2)	(1)	39	21	3	-	-
Demographic assumptions	-	-	-	-	-	-	-	-	-
Experience	5	1	1	-	(33)	14	6	-	-
Limits on assets	-	(7)	-	-	-	-	-	-	-
At 31 December	**(18)**	**15**	**(1)**	**(1)**	**6**	**35**	**9**	**-**	**-**

The main categories of assets, expressed as a percentage of the total fair value of the assets are as:

	2017				2016				
% of total	Spain	Brazil	Chile	Mexico	Spain	Colombia	Brazil	Chile	Mexico
Shares	-	14%	-	-	-	-	16%	-	-
Bonds	100%	79%	-	100%	100%	-	76%	-	100%
Real estate and other assets	-	7%	-	-	-	-	8%	-	-

Real yields on the plan-related assets in 2017, relating basically to Spain and Brazil, have been Euros 21 million (Euros 27 million in 2016).

The main annual actuarial assumptions used were as follows:

	At 31/12/2017				At 31/12/2016				
	Spain	Brazil	Chile	Mexico	Spain	Colombia	Brazil	Chile	Mexico
Discount rate (1)	0.0 a 2.25%	10.7%	1.9%	7.25%	0.0 a 1.8%	7.5%	11.9%	1.7%	7.0%
Expected return on plan assets (1)	0.0 a 2.25%	10.7%	-	7.25%	0.0 a 1.8%	-	11.9%	-	7.0%
Future salary increases (1)	2.0%	7.7%	2.0%	5.5%	2.0%	4.5%	6.6%	2.0%	5.5%
Future pension increases (1)	2.0%	5.5%	NA	3.4%	2.0%	3.5%	5.5%	NA	3.4%
Inflation rate (1)	2.0%	5.5%	2.7%	4.0%	2.0%	3.5%	5.5%	3.0%	4.0%
Mortality table	PERMF 2000	AT-2000	RV-2010	EMSSA 2009	PERMF 2000	RV08	AT-2000	RV-2009	EMSSA 2009
Life expectancy:									
Men									
Retired in the current year	22.9	20.45	18.36	22.56	22.5	18.45	20.45	19.58	22.56
Retiring within 20 years	42.7	37.94	35.57	39.53	42.5	36.69	37.94	20.47	39.53
Women									
Retired in the current year	27.4	23.02	23.24	25.04	27.0	22.18	23.02	29.07	25.04
Retiring within 20 years	48.6	41.44	41.89	44.81	48.4	40.39	41.44	29.75	44.81

(1) annual

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

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

Benefits payable and estimated contributions to be made for 2018 in million euros are as follows:

	Benefits				Contributions			
	Spain	Brazil	Chile	Mexico	Spain	Brazil	Chile	Mexico
Post-employment	58	8	-	-	11	1	2	-
Post-employment medical	-	-	-	-	3	2	-	-
Long term	-	-	-	-	-	-	-	-
At 31 December	**58**	**8**	**-**	**-**	**14**	**3**	**2**	**-**

The following table includes the effect of a 1% variation in the inflation rate, a 1% change in the discount rate and a 1% change in the cost of healthcare over the provisions and actuarial costs:

	Inflation + 1%	Discount +1%	Healthcare +1%
Present value of obligations	111	(132)	19
Fair value of plan assets	(11)	(67)	-
Provision for pensions	**100**	**(65)**	**19**
Service cost for the year	2	(2)	-
Interest cost	3	8	1
Expected return on plan assets	-	(6)	-

Other obligations with personnel

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

At 31 December 2017 a provision has been recorded corresponding to the remuneration programmes 2015-2017, 2016-2018 and 2017-2019 amounting to Euros 19 million (Euros 19 million at 31 December

2016), of which Euros 9 million are classified as non-current in 2017 (Euros 9 million 2016).

Other current and non-current provisions

Movements in current and non-current provisions are as follows:

	Non-current provisions			Current provisions	Total
	Due to facility closure costs	Other provisions	Total		
At 01/01/2016	**428**	**401**	**829**	**193**	**1,022**
Appropriations/reversals charged to income statement:					
– Appropriations due to financial update	10	1	11	-	**11**
– Appropriations charged to other results	-	15	15	56	**71**
– Reversals	-	(24)	(24)	(1)	**(25)**
Appropriations/reversals charged to fixed assets:	(1)	-	(1)	-	**(1)**
Payments	(4)	(30)	(34)	(112)	**(146)**
Business combinations (Note 31)	-	-	-	-	**-**
Currency translation differences	4	3	7	2	**9**
Transfers and other (1)	(23)	(21)	(44)	20	**(24)**
At 31/12/2016	**414**	**345**	**759**	**158**	**917**
Appropriations/reversals charged to income statement:					
– Appropriations due to financial update	6	2	8	-	**8**
– Appropriations charged to other results	-	16	16	125	**141**
– Reversals	(6)	(10)	(16)	-	**(16)**
Appropriations/reversals charged to fixed assets:	5	-	5	-	**5**
Payments	(3)	(2)	(5)	(88)	**(93)**
Currency translation differences	(1)	(7)	(8)	(13)	**(21)**
Transfers and other (2)	(7)	(88)	(95)	1	**(94)**
At 31/12/2017	**408**	**256**	**664**	**183**	**847**

(1) It mainly includes the derecognition of the Electricaribe balances due to the deconsolidation of the holding following the loss of control (Note 8).

(2) it mainly includes the transfers to “Non-current assets held for sale to the date on which this classification applies (Note 9) as well as the application, in the amount of Euros 93 million, of the provision for the tax assessments related to export deductions in 2003-2005, as a result of the judgment dismissing the Supreme Court (Note 21), that has been offset by the compensation done with balances to be returned by the Public Treasury.

The item “provisions due to facility closure costs” includes provisions for obligations arising from decommissioning, restoration and other costs related basically to electricity generation facilities.

The item “Other provisions” mainly includes provisions posted to cover obligations derived principally from tax claims (Note 21), lawsuits and arbitration, insurance and other liabilities. Note 35 “Commitments and contingent liabilities” includes further information on contingent liabilities.

The item “Current provisions” relates mainly to CO_2 emissions estimated for the year in the amount of Euros 66 million at 31 December 2017 (Euros 56 million in 2016).

No provision for onerous contracts was deemed necessary at 31 December 2017 or 2016.

The estimated payment periods for the obligations provisioned in this item are Euros 398 million in between one and five years (Euros 306 million at 31 December 2016), Euros 98 million in between five and 10 years (Euros 86 million at 31 December 2016) and Euros 365 million after more than 10 years (Euros 367 million at 31 December 2016).

Note 16. Financial liabilities

The breakdown of financial liabilities at 31 December 2017 and 2016 is as follows:

	At 31/12/2017	At 31/12/2016
Issuing of debentures and other negotiable obligations	10,726	10,098
Borrowings from financial institutions	5,140	4,837
Derivative financial instruments	48	62
Other financial liabilities	2	6
Non-current financial liabilities	**15,916**	**15,003**
Issuing of debentures and other negotiable obligations	1,488	1,563
Borrowings from financial institutions	988	856
Derivative financial instruments	1	18
Other financial liabilities	66	162
Current financial labilities	**2,543**	**2,599**
Total	**18,459**	**17,602**

Financial liabilities recognised at fair value at 31 December 2017 and at 31 December 2016 are classified as follows:

	31 December 2017				**31 December 2016**			
Financial liabilities	**Level 1 (Listed price on active markets)**	**Level 2 (observables variables)**	**Level 3 (Non-observables variables)**	**Total**	**Level 1 (Listed price on active markets)**	**Level 2 (observables variables)**	**Level 3 (Non-observables variables)**	**Total**
Fair value through profit or loss	-	-	-	**-**	-	-	-	**-**
Hedging derivatives	-	49	-	**49**	-	80	-	**80**
Total	**-**	**49**	**-**	**49**	**-**	**80**	**-**	**80**

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

	Carrying amount		**Fair value**	
	At 31/12/2017	**At 31/12/2016**	**At 31/12/2017**	**At 31/12/2016**
Issuing of debentures and other negotiable securities	10,726	10,098	11,776	11,389
Loans from financial institutions and other financial liabilities	5,142	4,843	5,176	4,874

The fair value of the listed bond issues is estimated on the basis of their market price (Level 1). 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 2017 and 31 December 2016 on borrowings with similar credit and maturity characteristics. These valuations are based on the quotation price of similar financial instruments in an official market or on observable information in an official market (Level 2).

The following tables describe consolidated gross financial liabilities by instrument at 31 December 2017 and 31 December 2016 and their maturity profile, taking into account the impact of the derivative hedges.

	2018	2019	2020	2021	2022	2023 and later years	Total
At 31 December 2017:							
Issuing of debentures and other negotiable securities							
Fixed	1,426	1,234	1,137	1,436	768	6,150	12,151
Floating	63	-	-	-	-	-	63
Institutional Banks and other financial institutions							
Fixed	185	150	170	170	137	1,272	2,084
Floating	80	76	76	78	57	28	395
Commercial Banks and other financial liabilities							
Fixed	64	163	350	114	185	3	879
Floating	725	517	944	231	470	-	2,887
Total Fixed	1,675	1,547	1,657	1,720	1,090	7,425	15,114
Total Floating	868	593	1,020	309	527	28	3,345
Total	**2,543**	**2,140**	**2,677**	**2,029**	**1,617**	**7,453**	**18,459**

	2017	2018	2019	2020	2021	2022 and later years	Total
At 31 December 2016:							
Issuing of debentures and other negotiable securities							
Fixed	1,429	1,568	1,241	1,659	1,553	3,992	11,442
Floating	133	23	63	-	-	-	219
Institutional Banks and other financial institutions							
Fixed	229	163	127	127	84	93	823
Floating	138	108	82	78	121	624	1,151
Commercial Banks and other financial liabilities							
Fixed	134	30	484	146	125	5	924
Floating	536	791	881	385	390	60	3,043
Total Fixed	1,792	1,761	1,852	1,932	1,762	4,090	13,189
Total Floating	807	922	1,026	463	511	684	4,413
Total	**2,599**	**2,683**	**2,878**	**2,395**	**2,273**	**4,774**	**17,602**

Had the impact of the derivatives on financial liabilities been excluded, the financial debt at fixed rate would amount to Euros 13,008 million at 31 December 2017 (Euros 11,636 million at 31 December 2016) and, at floating rates, Euros 5,403 million at 31 December 2017 (Euros 5,886 million at 31 December 2016).

The following table describes consolidated gross financial debt denominated by currency at 31 December 2017 and 31 December 2016 and its maturity profile, taking into account the impact of the derivative hedges:

	2018	2019	2020	2021	2022	2023 and later years	Total
At 31 December 2017:							
Euro debt	1,634	1,626	1,863	1,864	1,411	6,710	15,108
Foreign Currency Debt:							
US Dollar	230	175	272	93	102	3	875
Chilean peso	414	194	334	71	62	689	1,764
Mexican peso	128	41	43	-	42	51	305
Brazilian real	108	89	157	-	-	-	354
Colombian peso	-	1	-	-	-	-	1
Argentinian peso	29	14	8	1	-	-	52
Rest	-	-	-	-	-	-	-
Total	**2,543**	**2,140**	**2,677**	**2,029**	**1,617**	**7,453**	**18,459**

	2017	2018	2019	2020	2021	2022 and later years	Total
At 31 December 2016:							
Euro debt	1,944	1,923	1,951	2,113	2,086	3,961	13,978
Foreign Currency Debt:							
US Dollar	288	20	502	1	106	5	922
Chilean peso	133	408	167	281	81	751	1,821
Mexican peso	3	136	102	-	-	57	298
Brazilian real	159	179	74	-	-	-	412
Colombian peso	61	9	75	-	-	-	145
Argentinian peso	11	8	7	-	-	-	26
Rest	-	-	-	-	-	-	-
Total	**2,599**	**2,683**	**2,878**	**2,395**	**2,273**	**4,774**	**17,602**

Financial debt in euros have borne an effective average interest rate of 2.96% at 31 December 2016 (3.57% at 31 December 2016) while financial debt in foreign currency have borne an effective average interest rate of 6.03% in 2017 (7.13% at 31 December 2016) including derivative instruments assigned to each transaction.

At 31 December 2017, Gas Natural Fenosa has credit facilities totalling Euros 7,796 million (Euros 8,192 million at 31 December 2016), of which Euros 7,283 million has not been drawn down (Euros 7,642 million at 31 December 2016).

Bank borrowings totalling Euros 2,687 million (Euros 2,308 million at 31 December 2016) are subject to the fulfilment of certain financial ratios.

Most of the drawn financial debt includes a clause that relates to the change of control whose trigger depends on some of these events happening at the same time: not belonging to none of the present reference shareholders in a significant percentage; losing the Rating Agencies investment grade or non-capacity to fulfil the financial obligations of the contract.

Specifically, bonds issued amounting to Euros 11,205 million, would be susceptible to early maturing as long as this change of control may produce more than two steps or two full notches falling in at least two of the three ratings it may have as well as all the ratings falling under investment grade and provided that the Rating Agency express that this reduction in the rating is due to the change of control.

Likewise, there are borrowings amounting to Euros 2,851 million that could be subject to early repayment in case of a change of control. Most of this amount correspond to infrastructure financial founds from de European Inversion Bank than require, apart from the change of control event, a reduction in the rating and have specific repayment terms longer than the early repayment scenarios.

At the formulation date of these Consolidated annual accounts, Gas Natural Fenosa 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.

Certain investment projects financed by means of specific structures (project finance) which include pledges on the shares in the project companies have concluded in 2017. At 31 December 2016, the outstanding balance of this type of financing totalled Euros 13 million.

We set out below the most relevant financial instruments:

Issuing of debentures and other negotiable securities

In 2017 and 2016 the evolution of the issues of debt securities has been as follows:

	At 1.1.2017	Issuances	Buy-backs or redemptions	Adjustments, exch. rates & other	At 31.12.2017
Issued in a European Union Member State which required the filing of a prospectus	**10,262**	6,694	(5,794)	(204)	**10,958**
Issued in a European Union Member State which did not require the filing of a prospectus	**-**	-	-	-	**-**
Issued outside a European Union Member State	**1,399**	-	(8)	(135)	**1,256**
Total	**11,661**	**6,694**	**(5,802)**	**(339)**	**12,214**

	At 1.1.2016	Issuances	Buy-backs or redemptions	Adjustments, exch. rates & other	At 31.12.2016
Issued in a European Union Member State which required the filing of a prospectus	**10,857**	5,125	(5,725)	5	**10,262**
Issued in a European Union Member State which did not require the filing of a prospectus	**-**	-	-	-	**-**
Issued outside a European Union Member State	**1,466**	-	(116)	49	**1,399**
Total	**12,323**	**5,125**	**(5,841)**	**54**	**11,661**

In april 2017 Bonds issuance under its EMTN programme amounting to Euros 1,000 million was used to implement the repurchase of debentures for Euros 1,000 million maturing in 2018, 2020 and 2021. In accordance with IAS 39, there have been no substantial variations in the debt instrument and therefore the carrying amount of the liability has been adjusted based on the relevant costs and incurred commissions, which are amortised over the remaining useful life of the adjusted liability.

An analysis of the most relevant characteristics of the main issuance programmes for debentures and other negotiable securities by Gas Natural Fenosa is as follows, excluding the impact of accrued unpaid interest:

At 31 december 2017							
Program/Company	**Country**	**Year of formalization**	**Currency**	**Program limit**	**Nominal arranged**	**Available**	**Issues year**
Euro Commercial Paper program (ECP)							
Gas Natural Fenosa Finance B.V.	Netherlands	2010	Euros	1,000	-	1,000	4,594
European Medium Term Notes program (EMTN)							
Gas Natural Capital Markets, S.A. and Gas Natural Fenosa Finance B.V.	Netherlands /Spain	1999	Euros	15,000	11,205	3,795	2,100
Negotiable bonds and Certificates Programme							
Empresa de Distribución Eléctrica Metro-Oeste, S.A.	Panama	2010	US dollars	42	-	42	-
Gas Natural México S.A. de C.V.	Mexico	2011	Mexican pesos	422	180	242	-
Gas Natural BAN, S.A.	Argentina	2015	Argentinean Pesos	22	-	22	-
CGE Group	Chile	2015	Chilean pesos	1,924	771	1,153	-

At 31 december 2016							
Program/Company	**Country**	**Year of formalization**	**Currency**	**Program limit**	**Nominal arranged**	**Available**	**Issues year**
Euro Commercial Paper program (ECP)							
Gas Natural Fenosa Finance B.V.	Netherlands	2010	Euros	1,000	100	900	4,225
European Medium Term Notes program (EMTN)							
Gas Natural Capital Markets, S.A. and Gas Natural Fenosa Finance B.V.	Netherlands /Spain	1999	Euros	14,000	10,205	3,795	900
Negotiable bonds and Certificates Programme							
Empresa de Distribución Eléctrica Metro-Oeste, S.A.	Panama	2010	US dollars	47	-	47	-
Gas Natural México S.A. de C.V.	Mexico	2011	Mexican pesos	530	196	334	-
Gas Natural BAN, S.A.	Argentina	2015	Argentinean pesos	22	-	22	-
Gas Natural S.A. ESP	Colombia	2012	Colombian pesos	158	95	63	-
CGE Group	Chile	2015	Chilean pesos	2,319	801	1,518	-

The breakdown of the nominal issue balance is as follows:

Issue	Issued Nominal 2017	2016	Maturity	Coupon %
July 2009	500	500	2019	6.375
November 2009	631	750	2021	5.125
January 2010	686	850	2020	4.500
January 2010	513	700	2018	4.125
February 2011	-	600	2017	5.625
May 2011	500	500	2019	5.375
February 2012	586	750	2018	5.000
September 2012	434	800	2020	6.000
October 2012	-	500	2017	4.125
January 2013	600	600	2023	3.875
January 2013 (1)	204	204	2019	2.125
April 2013	750	750	2022	3.875
July 2013 (2)	101	101	2023	3.974
October 2013	500	500	2021	3.500
March 2014	500	500	2024	2.875
May 2014	200	200	2023	2.625
January 2015	500	500	2025	1.375
April 2016	600	600	2026	1.250
April 2016	300	300	2021	0.515
January 2017	1,000	-	2027	1.375
April 2017	1,000	-	2024	1.125
October 2017	300	-	2029	1.875
November 2017	800	-	2025	0.875
Total	**11,205**	**10,205**		

(1) CHF 250 million as nominal value.
(2) NOK 800 million as nominal value

Bonds issuance under its EMTN programme in april 2017 amounting to Euros 1,000 million was used to implement the repurchase of debentures for Euros 1,000 million maturing in 2018, 2020 and 2021.

Preference shares

In May 2003, the subsidiary Unión Fenosa Financial Services USA, L.L.C., issued preference shares for a nominal amount of Euros 609 million with the following characteristics:

- Dividend: variable, non-accumulative, until 20 May 2013, was Euribor at three months plus a spread of 0.25% capped at 7% and a minimum of 4.25%; as from that date, Euribor at three months plus a spread of 4%.
- Term: perpetual, with the option for the issuer of reducing in advance all or part of the shareholding after 20 May 2013. Any redemptions will be made at par value.
- Remuneration: the dividend payment will be preferential and not accumulative and depends on whether distributable consolidation profit is reported or the payment of a dividend to its ordinary shareholders.
- Voting rights: none

On 16 April 2013, Gas Natural Fenosa's Board of Directors approved a bid for the preferred shares. A cash bid was made to purchase the shares at 93% of their nominal amount; on 16 May 2013, once the acceptance period had ended, the aggregate nominal amount of the acceptances confirmed was Euros 539 million. 88.56% of the issue's nominal amount.

On 22 February 2016, all said outstanding preference shares were redeemed at par value. The balance totalled Euros 69 million and accrued interest at a rate of 3.849%.

Borrowings from financial institutions

European bank loans (commercial / institutional banks)

At 31 December 2017, bank borrowings include bank loans of Euros 1,644 million (Euros 1,520 million at 31 December 2016) while no credit lines had been utilised (Euros 233 million at 31 December 2016).

During 2017, two long-term operations with institutional credit institutions were arranged, one with a term of 20 years and a 4-year grace period for Euros 450 million with the European Investment Bank (EIB) and another with a term of 12 years and a 2-year grace period for Euros 200 million with the Official Credit Institute (ICO), which as at 31 December 2017 had been fully drawn down.

EIB has granted financing to Gas Natural Fenosa which at 31 December 2017 is fully drawn down, in the amount of Euros 2,240 million (Euros 1,835 million drawn down and Euros 300 million available at 31 December 2016). On the other hand, borrowings from the ICO total Euros 234 million, maturing in 2029 at the latest (Euros 112 million at 31 December 2016).

Loans from Latin American banks (commercial / institutional banks)

At 31 December 2017 borrowings from various Latin American banks totalled Euros 2,012 million (Euros 1,978 million at 31 December 2016). The geographic breakdown of these loans is as follows:

Country	31,12,2017	31,12,2016
Chile	1,034	998
Panama	475	409
Brazil	354	412
Mexico	126	106
Colombia	1	48
Other	22	5
	2,012	**1,978**

Of the total bank borrowings in Latin America at 31 December 2017, 99% relates to commercial banks and the remaining 1% to institutional banks.

Other financial liabilities

At 31 December 2016, the heading "Other financial liabilities" basically includes the 10-year finance lease entered into in 2007 with financial institutions for the power islands at the Sagunto combined cycle plant (Note 6), which matured in 2017.

The breakdown of the minimum payments for the finance leases are as follows:

	At 31/12/2017			At 31/12/2016		
	Nominal value	Discount	Present value	Nominal value	Discount	Present value
Less than 1 year	-	-	**-**	52	(2)	**50**
Between 1 and 5 years	-	-	**-**	-	-	**-**
Total	**-**	**-**	**-**	**52**	**(2)**	**50**

Note 17. Risk management and derivative financial instruments

Risk management

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

- Guaranteeing that the most relevant risks are correctly identified, evaluated and managed.

- Segregation at the operating level of the risk management functions.

- Assuring that the level of its risk exposure for Gas Natural Fenosa in its business is in line with the objective risk profile and achievement of its annual, strategic objectives.

- Ensuring the appropriate determination and review of the risk profile by the Risk Committee, proposing global limits by risk category, and assigning them to the Business Units.

On 23 June 2016 UK voters supported the departure of their country from the European Union ("Brexit"). Although the exit of the UK will be accompanied by lengthy negotiations the duration of which is currently unknown, the first repercussions have already arisen in both the capital and currency markets. However, Gas Natural Fenosa's exposure to the risk derived from Brexit is practically zero.

Interest rate risk

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

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

Gas Natural Fenosa employs financial swaps to manage exposure to interest rate fluctuations, swapping floating rates for fixed rates.

The financial debt structure at 31 December 2017 and 2016 (Note 16), after taking into account the hedges arranged through derivatives, is as follows:

	At 31/12/2017	**At 31/12/2016**
Fixed interest rate	15,114	13,189
Floating interest rate	3,345	4,413
Total	**18,459**	**17,602**

The floating interest rate is mainly subject to the fluctuations of the EURIBOR, the LIBOR and the indexed rates of Mexico, Brazil, Argentina and Chile.

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

	Increase/decrease in interest rates (basis points)	Effect on profit before tax	Effect on equity before tax
2017	+50	(17)	133
	-50	17	(133)
2016	+50	(22)	83
	-50	22	(83)

Exchange rate risk

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

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

In order to mitigate these risks Gas Natural Fenosa 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 within the limits approved for hedging instruments.

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

		Effect on profit before tax	Effect on equity before tax
2017	+5%	-	7
	-5%	-	(7)
2016	+5%	-	12
	-5%	-	(10)

Additionally, net assets of foreign companies that have a non-euro functional currency are subject to foreign exchange risk when their financial statements are translated to euros during the consolidation process. Exposure to risk countries where there is more than one exchange rate is immaterial. At 31 December 2017 Gas Natural Fenosa's equity denominated in Argentinian pesos totals Euros 44 million (Euros 47 million at 31 December 2016) representing a pre-tax impact on equity of Euros 2 million at 5% sensitivity (Euros 2 million at 31 December 2016).

Commodity price risk

A large portion of Gas Natural Fenosa's operating expenses are linked to gas purchased to supply customers or generate electricity at combined cycle plants. Therefore, Gas Natural Fenosa is exposed to gas price fluctuation risk, whose determination is basically subject to the prices of crude oil and its by-products. Additionally, in the electricity generation business Gas Natural Fenosa is exposed to CO_2 emission allowances fluctuation risk and electricity prices variations.

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

The risk involved in the electricity ad CO2 emission allowances trading operations carried out by Gas Natural Fenosa is not significant, due to the low volume of these operations and the limits established, both in terms of amount and maturity.

The sensitivity of profit and equity (Value adjustments) to the variation in the fair value of derivative contracts to hedge commodity prices is as follows:

	Increase / decrease in the purchase price of gas	Effect on profit before tax	Effect on equity before tax
2017	+10%	-	(16)
	-10%	-	16
2016	+10%	-	44
	-10%	-	(44)

	Increase/decrease in the electricity sale price	Effect on profit before tax	Effect on equity before tax
2017	+10%	-	12
	-10%	-	(12)
2016	+10%	-	27
	-10%	-	(27)

Gas Natural Fenosa 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 Gas Natural Fenosa's results.

- Gas and electricity. Profit margins on gas and electricity supply activities are directly affected by commodity prices. In this regard, Gas Natural Fenosa has a risk policy that stipulates the tolerance range, based on applicable risk limits, among other aspects. Measures employed to keep risk within the stipulated limits include active supply management, balanced acquisitions and sales 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.

Gas Natural Fenosa 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.

With regard to credit risk in relation to trade receivables, these are reflected in the consolidated balance sheet net of provisions for bad debts (Note 11), estimated by Gas Natural Fenosa 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 holding "BB "ratings or higher, in accordance with the credits ratings granted by Moody's, S&P and Fitch. No significant defaults or losses arose in 2017 or 2016.

The main guarantees negotiated are bank guarantees, guarantees and deposits. At 31 December 2017, Gas Natural Fenosa had received guarantees totalling Euros 41 million to cover the risk of large industrial customers (Euros 155 million at 31 December 2016). In 2017, bank guarantees amounting to Euros 2 million were enforced (Euros 1 million at 31 December 2016).

At 31 December 2017 and 2016 Gas Natural Fenosa does not have significant concentrations of credit risk. The risk of concentration is minimised through diversification, managing and combining various areas of impact. Firstly, by having a customer base that is broadly distributed on an international scale; secondly, a diverse product range, from energy supply to the implementation of tailored energy solutions; thirdly, there are different customer types, such as residential customers, self-employed entrepreneurs and small and large businesses in both the public and private sectors and in different segments of the economy.

The breakdown of the age of financial receivables overdue but not considered bad debts at 31 December 2017 and 2016 is as follows:

	At 31/12/2017	At 31/12/2016
Less than 90 days	534	326
90 – 180 days	97	89
More than 180	21	14
Total	**652**	**429**

The impaired financial assets are broken down in Note 11.

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.

Liquidity risk

Gas Natural Fenosa 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.

Available cash resources at 31 December 2017 and 2016 are analysed below:

Liquidity source	Availability 2017	Availability 2016
Undrawn credit facilities (Note 16)	7,283	7,642
Undrawn loans	42	352
Cash and cash equivalents (Note 12)	3,225	2,067
Total	**10,550**	**10,061**

There is also additional capacity to issue debt in the capital markets unused for Euros 6,254 million (Note 16).

The breakdown of the maturities of the financial liabilities at 31 December 2017 and 2016 is as follows:

	2018	2019	2020	2021	2022	2023 and later years	Total
At 31 December 2017							
Trade and other payables	(3,920)	-	-	-	-	-	(3,920)
Loans and other financial payables	(3,121)	(2,723)	(3,205)	(2,519)	(2,071)	(8,744)	(22,383)
Financial derivatives	62	6	(2)	(5)	-	(30)	31
Other liabilities	(93)	(149)	(73)	(51)	(51)	(541)	(958)
Total (1)	**(7,072)**	**(2,866)**	**(3,280)**	**(2,575)**	**(2,122)**	**(9,315)**	**(27,230)**

	2017	2018	2019	2020	2021	2022 and later years	Total
At 31 December 2016							
Trade and other payables	(4,072)	-	-	-	-	-	(4,072)
Loans and other financial payables	(3,327)	(3,371)	(3,499)	(2,914)	(2,678)	(5,709)	(21,498)
Financial derivatives	(16)	31	23	-	(11)	7	34
Other liabilities	(104)	(97)	(165)	(87)	(81)	(615)	(1,149)
Total (1)	**(7,519)**	**(3,437)**	**(3,641)**	**(3,001)**	**(2,770)**	**(6,317)**	**(26,685)**

(1) The amounts are undiscounted contractual cash flows and, accordingly, differ from the amounts included in the balance sheet and in Note 16.

Capital management

The main purpose of capital management of Gas Natural Fenosa 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.

Gas Natural Fenosa considers the following to be indicators of the objectives set for capital management: maintaining, after the acquisition of Unión Fenosa, a long-term leverage ratio of approximately 50%.

The long-term credit rating of Gas Natural Fenosa is as follows:

	2017	2016
Moody’s	Baa2	Baa2
Standard & Poor’s	BBB	BBB
Fitch	BBB+	BBB+

Its leverage rating is as follows:

	2017	2016
Net financial liabilities:	**15,154**	**15,423**
Non-current financial liabilities (Note 16)	15,916	15,003
Current financial liabilities (Note 16)	2,543	2,599
Cash and cash equivalents (Note 12)	(3,225)	(2,067)
Derivatives (Note 17)	(80)	(112)
Equity:	**18,305**	**19,005**
Equity holders of the Company (Note 13)	14,734	15,225
Non-controlling interests (Note 13)	3,571	3,780
Leverage (Net financial liabilities / (Net financial liabilties + Net equity))	**45.3%**	**44.8%**

Derivative financial instruments

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

	At 31/12/2017		At 31/12/2016	
	Assets	Liabilities	Assets	Liabilities
Hedging derivative financial instruments	**15**	**48**	**111**	**62**
Cash flow hedge				
- Interest rate	14	42	85	22
- Price of commodities	-	-	-	-
Fair value hedge				
- Interest rate and foreign exchange rate	1	6	26	40
Other financial instruments	**-**	**-**	**-**	**-**
Derivative financial instruments – non current	**15**	**48**	**111**	**62**
Hedging derivative financial instruments	**99**	**85**	**46**	**61**
Cash flow hedge				
- Interest rate	44	-	1	6
- Exchange rate	18	1	9	-
- Price of commodities	32	83	36	42
Fair value hedge				
- Interest rate and foreign exchange rate	-	-	-	-
- Exchange rate	5	1	-	13
Other financial instruments	**4**	**6**	**1**	**5**
- Price of commodities	4	6	1	5
- Exchange rate	-	-	-	-
Derivative financial instruments current	**103**	**91**	**47**	**66**
Total	**118**	**139**	**158**	**128**

The fair value of derivatives is determined based on observable variables in an active market (Level 2).

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

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

	2017		2016	
	Operating results	Financial results	Operating results	Financial results
Cash flow hedge	24	(23)	(81)	(25)
Fair value hedge	-	(15)	(10)	(28)
Other financial instruments	(3)	(2)	(25)	(1)
Total	**(21)**	**(40)**	**(116)**	**(54)**

The breakdown of derivatives at 31 December 2017 and 2016, their fair value and maturities of their notional values is as follows:

	Fair value	31/12/2017 Notional value						
		2018	**2019**	**2020**	**2021**	**2022**	**Subsequent years**	**Total**
INTEREST RATE HEDGES:								
Cash flow hedges:								
Financial swaps (EUR)	(9)	95	95	844	63	91	2,484	3,672
Financial swaps (USD)	1	228	-	-	-	-	-	228
Financial swaps (MXN)	43	200	-	-	-	-	-	200
Financial swaps (CHF)	6	-	204	-	-	-	-	204
Financial swaps (NOK)	(25)	-	-	-	-	-	101	101
Financial swaps (COP)	-	-	-	-	-	-	-	-
EXCHANGE RATE HEDGES:								
Cash flow hedges:								
Foreign exchange insurance (USD)	8	647	-	-	-	-	-	647
Foreign exchange insurance (GBP)	-	30	-	-	-	-	-	30
Foreign exchange insurance (EUR) (1)	2	38	-	-	-	-	-	38
Foreign exchange insurance (COP)	(1)	54	-	-	-	-	-	54
Foreign exchange insurance (AUD)	-	-	42	-	-	-	-	42
Foreign exchange insurance (BRL)	8	60	-	-	-	-	-	60
Fair value hedges:								
Financial swaps (CLP)	(5)	-	-	-	160	-	-	160
Financial swaps (MXN)	-	-	-	-	-	-	-	-
Foreign exchange insurance (BRL)	-	19	-	-	-	-	-	19
Foreign exchange insurance (USD)	4	333	-	-	-	-	-	333
Foreign exchange insurance (DHN)	-	10	-	-	-	-	-	10
Foreign exchange insurance (EUR) (1)	-	69	-	-	-	-	-	69
COMMODITIES HEDGES:								
Cash flow hedges:								
Commodities price derivatives (EUR)	20	149	8	-	-	-	-	157
Commodities price derivatives (USD)	(71)	342	115	9	9	18	24	517
OTHERS:								
Commodities price derivatives (EUR)	(2)	4	-	-	-	-	-	4
Foreign exchange derivatives (USD)	-	-	-	-	-	-	-	-
TOTAL	**(21)**	**2,278**	**464**	**853**	**232**	**109**	**2,609**	**6,545**

(1) Arranged by companies using a functional currency other than the euro.

	Fair value	31.12.16 Notional value						
		2017	2018	2019	2020	2021	Subsequent years	Total
INTEREST RATE HEDGES:								
Cash flow hedges:								
Financial swaps (EUR)	23	684	-	-	-	-	1,500	2,184
Financial swaps (USD)	(2)	223	259	-	-	-	-	482
Financial swaps (MXN)	32	57	200	-	-	-	-	257
Financial swaps (CHF)	26	-	-	204	-	-	-	204
Financial swaps (NOK)	(21)	-	-	-	-	-	101	101
Financial swaps (COP)	-	-	-	-	-	-	-	-
EXCHANGE RATE HEDGES:								
Cash flow hedges:								
Foreign exchange insurance (USD)	9	213	-	-	-	-	-	213
Foreign exchange insurance (GBP)	-	13	-	-	-	-	-	13
Fair value hedges:								
Financial swaps (CLP)	(14)	-	-	60	-	160	-	220
Financial swaps (MXN)	-	-	-	-	-	-	-	-
Foreign exchange insurance (BRL)	-	-	-	-	-	-	-	-
Foreign exchange insurance (USD)	(13)	374	-	-	-	-	-	374
Foreign exchange insurance (DHN)	-	7	-	-	-	-	-	7
COMMODITIES HEDGES:								
Cash flow hedges:								
Commodities price derivatives (EUR)	23	309	54	4	-	-	-	367
Commodities price derivatives (USD)	(29)	281	139	131	-	-	-	551
OTHERS:								
Commodities price derivatives (EUR)	(4)	13	-	-	-	-	-	13
Foreign exchange derivatives (USD)	-	-	-	-	-	-	-	-
TOTAL	**30**	**2,174**	**652**	**399**	**-**	**160**	**1,601**	**4,986**

Note 18. Other non-current liabilities

The breakdown of this heading at 31 December 2017 and 2016 is as follows:

	At 31/12/2017	At 31/12/2016
Finance lease liabilities (1)	839	965
Deposits and guarantees deposits (2)	206	221
Other liabilities (3)	165	145
Total	**1,210**	**1,331**

There are no significant differences between the carrying values and the fair values of the items in the account “Other non-current liabilities”.

(1) Finance lease liabilities

The main finance lease liabilities recognised in this item at 31 December are as follows:

- In 2003 Gas Natural Fenosa acquired two gas transport tankers to transport liquefied natural gas with a capacity of 276,000 m^3 through finance lease agreements. The duration of the contracts is 20 years, maturing in 2023.

- In 2007 and 2009 two 138,000 m^3 tankers were acquired, together with Repsol, under 25-year time-charter agreements, extendable for consecutive 5-year periods. In 2014, Gas Natural Fenosa and Shell entered into an agreement, as part of the sale of the Repsol Group's liquefied natural gas business, to obtain exclusive use of each of the two tankers, Gas Natural Fenosa using the tanker acquired in 2009 under a time charter expiring in 2029 and extendable for consecutive five-year periods.

- In March 2014, Gas Natural Fenosa acquired a 173,000 m^3 tanker to carry liquefied natural gas under an 18-year finance lease expiring in 2032.

- In November 2016, Gas Natural Fenosa acquired two tankers to carry liquefied natural gas each with a capacity of 176.300 m^3 under a 20-year finance lease expiring in 2036.

Minimum lease payments are as follows:

	At 31/12/2017			At 31/12/2016		
	Nominal value	Discount	Present value	Nominal value	Discount	Presen t value
Less than 1 year	100	(6)	**94**	110	(7)	**103**
Between 1 and 5 years	402	(80)	**322**	439	(86)	**353**
More than 5 years	940	(423)	**517**	1,190	(578)	**612**
Total	**1,442**	**(509)**	**933**	**1,739**	**(671)**	**1,068**

The effective average interest rate on the liabilities for finance lease agreements at 31 December 2017 is 6.6% (6.5% at 31 December 2016).

(2) Deposits and guarantees deposits

The item "deposits and guarantees deposits" basically includes amounts received from customers under contracts for the supply of electricity and natural gas, deposited with the competent Public Administrations (Note 8) as stipulated by law, and amounts received from customers to secure supplies of liquefied natural gas.

(3) Other liabilities

This includes the purchase commitment (without a premium) made to Sinca Inbursa, S.A. de C.V. (Inbursa) on 22 September 2008 covering 14.125% of Gas Natural México, S.A. de C.V. and 14% of Sistemas de Administración, S.A. de C.V. The maturity date of this commitment is May 2019, when Ibursa will be able to offer all shares held at that time to Gas Natural Fenosa, which will be obligated to purchase them. The acquisition price will be the market value of each share, based on the investees' results. As a result of the commitment, this sale is recognized as a deferred payment and the repurchase commitment percentage is still allocated to the Parent company. The liability recognised in this item at 31 December 2017 totals Euros 77 million, representing the present value of the amount repayable (Euros 74 million at 31 December 2016).

Note 19. Trade and other payables

The breakdown at 31 December 2017 and 2016 is as follows:

	At 31/12/2017	At 31/12/2016
Trade payables	2,810	3,204
Trade payables with related parties (Note 33)	74	51
Amounts due to associates	1	19
Trade payables	2,885	3,274
Public Administrations	593	519
Derivative financial instruments (see Note 17)	88	48
Amounts due to employees	189	96
Other payables	18	29
Other payables	888	692
Current tax liabilities	147	106
Total	**3,920**	**4,072**

At 31 December 2017, Euros 110 million was recognised under the heading Personnel (outstanding remuneration) in relation to termination benefits resulting from agreements with employees to terminate their employment contracts.

The fair value and carrying value of these liabilities do not differ significantly.

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 periods of payments, according to the maximum legal limit under Law 15/2010 of 5 July, which laid down measures against slow payers in Spain, is as follows:

	2017	2016
	Amount	**Amount**
Total payments	12,256	11,533
Total payments outstanding	403	417
Average supplier payment period (days) (1)	25	28
Transactions paid ratio (days) (2)	24	27
Transactions pending payment ratio (days) (3)	34	30

(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.

Note 20. Other current liabilities

The breakdown in 2017 and 2016 is as follows:

	At 31/12/2017	At 31/12/2016
Dividend payable	45	37
Expenses accrued pending payment	172	174
Finance lease liabilities (Note 18)	94	103
Derivative financial instruments (Note 17)	2	-
Other liabilities	28	33
Total	**341**	**347**

Note 21. Tax situation

Gas Natural SDG, S.A. 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 2017 is indicated in Appendix III.

The rest of the Gas Natural Fenosa companies file individual tax returns under their respective regimes, barring a number of Italian subsidiaries that form their own tax consolidated group, which in 2017 were reclassified as held for sale.

Set out below is the reconciliation between "Income tax" recognised and the amount that would be obtained by applying the nominal tax rate in force in the parent company's country (Spain) to "Profit/(loss) before taxes" for 2017 and 2016:

	2017	%	2016[1]	%
Profit before tax	**1,427**		**1,851**	
Statutory tax	**357**	**25.0%**	**463**	**25.0%**
Effect of net results under equity method	(4)	(0.3%)	25	1.4%
Application of tax rates of foreign companies	(28)	(2.0%)	(35)	(1.9%)
Tax deductions	(18)	(1.3%)	(13)	(0.7%)
Remeasurement deferred taxes on mergers	(117)	(8.2%)	(128)	(6.9%)
Remeasurement deferred taxes	1	0.1%	21	1.1%
Other items	(1)	(0.1%)	-	-
Corporate income tax	**190**	**13.3%**	**333**	**18.0%**
Breakdown of current/deferred expense:				
Current-year tax	348		388	
Deferred tax	(158)		(55)	
Corporate income tax	**190**		**333**	

(1) The consolidated income statement for 2016 has been restated reclassifying to discontinued operations under IFRS 5 (Notes 3.3 and 9).

As part of business reorganisation corporate streamlining process in Chile, on 14 December 2016, Compañía General de Electricidad, S.A. carried out a vertical merger with its subsidiary Transnet. The resulting goodwill was allocated to the value for tax purposes of the non-monetary assets received from the absorbed company (electricity transmission networks), equivalent to its carrying amount at the date of the operation, generating a decrease in deferred tax liabilities of Euros 128 million with a balancing entry under Corporate income tax in the consolidated income statement.

On 30 November 2017, following the business reorganization and corporate streamlining process in Chile, Compañía General de Electricidad, S.A. carried out a vertical merger of its subsidiaries CGE Distribución, S.A., Compañía Nacional de Fuerza Eléctrica, S.A. and Empresa Eléctrica Atacama, S.A. The resulting goodwill was allocated to the value for tax purposes of the non-monetary assets received from the absorbed company (electricity distribution networks), equivalent to its carrying amount at the date of the operation, generating a decrease in deferred tax liabilities of Euros 117 million with a balancing entry under Corporate income tax in the consolidated income statement.

On 26 December 2016, Law No. 1819 on Structural Tax Reform was enacted in Colombia, which provides for a progressive reduction in income tax for 2017, 2018 and 2019. As a result, deferred taxes were revalued at the expected reversal rate, with an increase of Euros 21 million in the expense recorded under Corporate income tax in the consolidated income statement.

On 29 December 2017, Decree 1112/2017 on Tax Reform was published in Argentina which provides for a progressive reduction in income tax from 35% to 30% for 2018 to 2019 and 25% from 2020 onward. As a result, deferred taxes were revalued at the expected reversal rate, with a higher expense recorded under Corporate income tax in the consolidated income statement for an amount of Euros 1 million.

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 2016 these measures did not have a significant impact on the financial statements of Gas Natural Fenosa.

Income qualifying for the tax credit for reinvestment of extraordinary profits provided by Article 42 of the revised Corporate Income Tax Act introduced under Royal Decree-Law 4/2004 of March 5 (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 on the sale	Amount reinvested	Income qualifying for deduction	Year reinvested
2011	4	4	2	2011
2012	1	1	-	2012
2013	1	1	1	2013
2014	414	414	210	2014
Total	**420**	**420**	**213**	

The reinvestment was made in fixed assets used in business activities and was carried out by both the parent company the other companies 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) and the investments in which it has been used in prior years are explained below:

Year of sale	Amount obtained on the sale	Amount reinvested	Capital gain	Capital gain included in tax base	Capital gain pending inclusion in tax base
2002	917	917	462	19	443
2003	141	141	79	-	79
2004	292	292	177	9	168
2005	432	432	300	1	299
2006	309	309	226	-	226
2007	105	105	93	-	93
2009	161	161	87	-	87
2010	799	799	560	-	560
2011	450	450	394	-	394
2012	38	38	32	-	32
TOTAL	**3,644**	**3,644**	**2,410**	**29**	**2,381**

The reinvestment was made in fixed assets related to economic activities carried out by the transferring Company or any other company included in the Consolidated Tax Group by virtue of the provisions of article 75 of the Corporate Income Tax Act.

The breakdown of the tax effect relating to each component of “Other comprehensive income” of the Consolidated Statement of Comprehensive Income for the year is as follows:

	At 31/12/2017			At 31/12/2016		
	Gross	Tax effect	Net	Gross	Tax effect	Net
Measurement of available-for-sale financial assets	(54)	-	(54)	4	(1)	3
Cash flow hedges	(111)	13	(98)	228	(61)	167
Currency translation differences	(890)	-	(890)	428	-	428
Actuarial gains and loss (Note 15)	5	-	5	(51)	13	(38)
Total	**(1,050)**	**13**	**(1,037)**	**609**	**(49)**	**560**

Set out below is an analysis of and movements in deferred taxes:

Deferred tax assets	Provisions for employee benefit obligations	Provision of depreciation of receivables and other provisions	Tax credits (1)	Depreciation/amortisation differences	Financial instruments and asset valuation	Other	Total
At 01/01/2015	**179**	**258**	**93**	**328**	**67**	**145**	**1,070**
Charged/(credited) to income statement	(7)	(10)	(16)	(15)	(39)	(7)	(94)
Movements related to equity adjustments	17	-	-	-	(4)	-	13
Currency translation differences	5	13	5	2	(6)	(1)	18
Transfers and other (2)	(33)	(96)	(15)	(8)	21	(4)	(135)
At 31/12/2016	**161**	**165**	**67**	**307**	**39**	**133**	**872**
Charged/(credited) to income statement	26	26	(21)	(10)	2	3	26
Movements related to equity adjustments	-	-	-	-	8	-	8
Currency translation differences	(3)	(9)	(8)	(9)	14	(10)	(25)
Transfers and other (2)	1	(2)	-	(25)	1	(6)	(31)
At 31/12/2017	**185**	**180**	**38**	**263**	**64**	**120**	**850**

(1) At 31 December 2016 and 2015 the tax credits mainly relate to tax loss carry forwards from various CGE companies basically generated by the application of the accelerated depreciation tax incentive. The recover of these credits is reasonably assured as they are not subject to any time limit and pertain to companies that historically generate recurring profits.

(2) It mainly includes the derecognition of the Electricaribe balances due to the deconsolidation of the holding following the loss of control (Note 8) and the transfers to "Non-current assets held for sale" to the date on which this classification applies (Note 9) in 2017.

Deferred tax liabilities	Depreciation/amortisation differences	Deferred gains	Business combination valuation (1)	Financial instruments and asset valuation	Other	Total
At 01/01/2016	**893**	**209**	**1,368**	**(2)**	**75**	**2,543**
Charged/(credited) to income statement (2)	(119)	-	(51)	1	20	(149)
Business combinations (Note 31)	-	-	8	-	-	8
Movements related to equity adjustments	-	-	-	20	-	20
Currency translation differences	61	-	6	-	4	71
Transfers and other (3)	-	-	(9)	25	-	16
At 31/12/2016	**835**	**209**	**1,322**	**44**	**99**	**2,509**
Charged/(credited) to income statement (2)	(119)	-	(40)	-	27	(132)
Business combinations (Note 31)	-	-	-	-	-	-
Movements related to equity adjustments	-	-	-	(3)	-	(3)
Currency translation differences	(21)	-	-	(12)	1	(32)
Transfers and other (3)	(28)	(12)	5	2	3	(30)
At 31/12/2017	**667**	**197**	**1,287**	**31**	**130**	**2,312**

(1) The heading "Business combination valuation" includes the tax effect of the portion of the merger difference resulting from the absorption of Unión Fenosa, S.A. by Gas Natural SDG, S.A. in 2009, allocated to net assets acquired, which will not have tax effects. It also includes the tax effect of the allocation of the acquisition price of CGE by Gas Natural Fenosa in 2014 and of various prior acquisitions completed by CGE.

(2) The decrease in deferred tax liabilities of Euros 128 million in 2016 resulting from the Transnet merger mentioned above is included under "Depreciation/amortisation differences" and of Euros 117 million in 2017 resulting from the merger operation of Compañía General de Electricidad mentioned above.

(3) It mainly includes the derecognition of the Electricaribe balances due to the deconsolidation of the holding following the loss of control (Note 8) in 2016 and the transfer to "Non-current assets held for sale" to the date on which this classification applies (Note 9) in 2017.

At 31 December 2017 the tax credits that have not been recorded totalled Euros 27 million (Euros 30 million at 31 December 2016).

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

In general, the other Gas Natural Fenosa companies are open to inspection for the following periods:

Country	Period
Argentina	2011-2017
Brazil	2012-2017
Colombia	2015-2017
Chile	2014-2017
Italy	2013-2017
Mexico	2012-2017
Panama	2011-2017

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 (Note 15) for and amounted to Euros 93 million, which has been fully offset by balances to be returned by the Public Treasury in favour of Gas Natural Fenosa.

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. In any case, Gas Natural Fenosa considers that any such liabilities will not have a significant effect on these annual accounts.

Gas Natural Fenosa has recorded provisions for obligations deriving from a number of tax claims or uncertain tax treatments. There are no cases which are individually significant (Note 15).

Note 22. Sales

The breakdown of this heading for 2017 and 2016 is as follows:

	2017	**2016 (1)**
Sales of gas and access to distribution networks	12,944	10,612
Sales of electricity and access to distribution networks	8,833	9,808
Rental of facilities, maintenance and other services	1,431	1,412
Other sales	98	76
Total	**23,306**	**21,908**

(1) The consolidated income statement for 2016 has been restated, reclassifying the gas distribution business in Italy and Colombia, electricity distribution in Moldova, gas retailing in Italy and electricity generation in Kenya to discontinued operations under IFRS 5 (Notes 3.3 and 9).

Note 23. Procurements

The breakdown of this heading for 2017 and 2016 is as follows:

	2017	**2016 (1)**
Energy purchases	14,279	12,265
Access to transmission networks	1,798	1,900
Other purchases and changes in inventories	602	446
Total	**16,679**	**14,611**

(1) The consolidated income statement for 2016 has been restated reclassifying to discontinued operations under IFRS 5 (Notes 3.3 and 9).

Note 24. Other operating income

The breakdown of this heading for 2017 and 2016 is as follows:

	2017	**2016 (1)**
Other management income	237	238
Operating grants	1	2
Total	**238**	**240**

(1) The consolidated income statement for 2016 has been restated to discontinued operations under IFRS 5 (Notes 3.3 and 9).

The item “Other management income” includes income from services relating to the construction or improvement of concession infrastructures under IFRIC 12 in the amount of Euros 146 million (Euros 114 million in 2016); whose fair value is estimated by reference to the expenses incurred (Note 26), with no margin.

Note 25. Personnel costs

The breakdown of this heading for 2017 and 2016 is as follows:

	2017	2016 (1)
Wages and salaries	772	801
Termination indemnites	126	22
Social security costs	134	128
Defined contribution plans	44	42
Defined benefit plans (Note 15)	9	9
Own work capitalised	(122)	(109)
Other	68	81
Total	**1,031**	**974**

(1) The consolidated income statement for 2016 has been restated reclassifying to discontinued operations under IFRS 5 (Notes 3.3 and 9).

The average number of Gas Natural Fenosa employees was 15,374 in 2017 and 17,926 in 2016, analysed by category as follows:

	2017	2016(1)
Executives	1,406	1,394
Middle managers	2,793	2,771
Specialists	4,644	4,980
Workers	6,531	8,781
Total	**15,374**	**17,926**

(1) Restated under IFRS 5 (Note 3.3 and 9).

The average number of employees in the year with disability equal to or greater than 33% is as follows, by category:

	2017	2016(1)
Executives	8	7
Middle managers	22	19
Specialists	82	56
Workers	114	142
Total	**226**	**224**

(1) Restated under IFRS 5 (Note 3.3 and 9).

The number of employees of Gas Natural Fenosa at the end of 2017 and 2016 broken down by category, gender and geographical area, is as follows:

	2017		2016(1)	
	Men	**Women**	**Men**	**Women**
Executives	1,033	363	1,026	342
Middle managers	2,171	586	2,065	546
Specialists	3,192	1,681	3,264	1,602
Workers	4,522	1,827	4,803	1,854
Total	**10,918**	**4,457**	**11,158**	**4,344**

(1) Restated under IFRS 5 (Note 3.3 and 9).

	2017	2016(1)
Spain	7,350	7,378
Rest of Europe	176	169
Latin American	7,039	7,113
Rest	810	842
Total	**15,375**	**15,502**

(1) Restated under IFRS 5 (Note 3.3 and 9).

As a result of the application of IFRS 5, which has entailed the classification of the gas distribution businesses in Italy and Colombia, the electricity distribution business in Moldova and the generation business in Kenya as discontinued operations (Note 3.3 and 9), the calculation of the average number of employees in the current period and in the comparative figures for the previous year has not taken into account the average number of employees in companies classified as discontinued operations, which amounts to 1,393 persons (1,735 persons at 31 December 2016). Neither did this calculation consider the number of employees of those companies at the year end, amounting to 1,396 persons at 31 December 2017 (1,727 persons at 31 December 2016).

In addition, the calculation of the average number of employees did not take into account the average number of employees of equity-consolidated companies, which amounts to 835 persons (920 persons at 31 December 2016). Neither did this calculation consider the number of employees of those companies at the year end, amounting to 819 persons at 31 December 2017 (848 persons at 31 December 2016).

At the end of 2016, the number of Electricaribe employees that were not taken on as a result of the loss of control (Note 8) was 1,478 persons.

Note 26. Other operating expenses

The breakdown of this heading for 2017 and 2016 is as follows:

	2017	2016(1)
Taxes	451	465
Operation and maintenance	364	353
Advertising and other commercial services	297	326
Professional services and insurance	181	191
Concession construction or improvements services (IFRIC 12) (Note 24)	146	114
Supplies	93	99
Services to customers	82	78
Operating leases (2)	65	54
Other	305	311
Total	**1,984**	**1,991**

(1) The consolidated income statement for 2016 has been restated reclassifying to discontinued operations under IFRS 5 (Notes 3.3 and 9).
(2) Note 35 details uncancellable minimum payments under operating leases.

Note 27. Profit/(loss) on disposals of fixed assets

In 2017 mainly includes a gain before tax of Euros 18 million for the sale of several buildings in Madrid (Note 6).

In 2016, this heading included the capital gain of Euros 51 million from the sale of four buildings in Madrid for Euros 206 million (Note 6).

Note 28. Other results

In 2016, this item related to the pre-tax gain of Euros 128 million from the sale of the interest in GNL Quintero, S.A. (Chile) for Euros 182 million (Note 7).

It also included the transfer of accumulated translation differences in equity due to the shareholding in Electricaribe generated up to the date of loss of control (Note 8) with a negative impact of Euros 38 million.

Note 29. Net financial income

The breakdown of this heading for 2017 and 2016 is as follows:

	2017	2016(1)
Dividends	14	11
Interest income	19	28
Other	78	85
Total financial income	**111**	**124**
Cost of borrowings	(630)	(763)
Interest expenses pension plans	(14)	(32)
Other financial expense	(164)	(142)
Total financial expense	**(808)**	**(937)**
Variations in the fair value of derivate financial instruments (Note 17)	(2)	(2)
Net exchange differences	-	-
Net financial income	**(699)**	**(815)**

(1) The consolidated income statement for 2016 has been restated reclassifying to discontinued operations under IFRS 5 (Notes 3.3 and 9).

Note 30. Cash generated from operating activities and other details of the cash flows

The breakdown of cash generated from operations in 2017 and 2016 is as follows:

	2017	2016
Profit before tax	**1,427**	**1,851**
Adjustments to net income:	**2. 546**	**2,727**
Depreciation, amortisation and impairment expenses *(Note 5 and 6)*	1,694	1,759
Other adjustments to net income:	852	968
Net financial income *(Note 9 and 30)*	697	825
Profit of entities recorded by equity method *(Note 7 and 9)*	(14)	98
Transfer of deferred income *(Note 14)*	(42)	(43)
Other results *(Note 28)*	-	(122)
Net variation in Provisions	8	(76)
Pre-tax profit/(loss) from discontinued activities net of gains/impairments *(Note 9)*	203	286
Changes in working capital (excluding the effects of adjustments in consolidation scope and exchange differences):	**(155)**	**5**
Inventories	(15)	135
Trade and other receivables	(176)	(316)
Trade and other payables	36	186
Other cash flows from operating activities:	**(1,050)**	**(1,208)**
Interest paid	(686)	(793)
Interest collected	26	31
Dividends received	48	79
Income tax paid	(438)	(525)
CASH FLOWS GENERATED FROM OPERATING ACTIVITIES	**2,768**	**3,375**

Investments in Group companies, associates and business units at 31 December 2017 and 2016 breakdown is as follows:

	2017	2016
Gas Natural Chile, S.A. (Note 9)	-	306
Vayu (Note 31)	-	22
Capital increase Nueva Generadora del Sur, S.A.(Note 7)	14	-
Other	-	3
Total	**14**	**331**

Proceeds due to disinvestments in Group companies, associates and business units at 31 December 2017 and 2016 breakdown is as follows:

	2017	2016
Gasco, S.A. (Note 9)	-	220
GNL Quintero, S.A. (Note 7)	-	182
Gas Natural, S.A. ESP (Note 9)	134	-
Other	2	3
Total	**136**	**405**

Payments for equity instruments at 31 December 2017 and 2016 breakdown is as follows:

	2017	2016
Gas Natural SDG, S.A. treasury shares (Note 13)	14	(13)
CGE treasury shares (Note 13)	(9)	(8)
Non-controlling interest in Gas Galicia acquisition (Note13)	-	(6)
Total	**5**	**(27)**

The movement in borrowings in 2017 and 2016 is as follows, presenting separately the changes that generate cash flows from those that do not have been the following:

		Generates cash flows		Do not generate cash flows		
	At 1.1.2017	Increase	Decrease	Currency translation differences	Transfers and other (1)	At 31.12.2017
Issuing of debentures and other negotiable obligations	**11,661**	6,694	(5,802)	(37)	(279)	**12,214**
Borrowings from financial institutions	**5,693**	2.292	(1,466)	(240)	(151)	**6,218**
Derivative financial instruments	**80**	-	-	(2)	(20)	**49**
Other financial liabilities	**168**	331	(414)	(2)	(4)	**68**
Total	**17,602**	**9,317**	**(7,682)**	**(324)**	**(454)**	**18,549**

(1) Mainly includes the transfers to “Non-current assets held for sale” to the date on which this classification applies (Note 9).

		Generates cash flows		Do not generate cash flows		
	At 1.1.2016	Increase	Decrease	Currency translation differences	Transfers and other (1)	At 31.12.2016
Issuing of debentures and other negotiable obligations	**12,323**	5,125	(5,841)	43	11	**11,661**
Borrowings from financial institutions	**5,543**	2,379	(1,838)	225	(616)	**5,693**
Derivative financial instruments	**179**	-	-	(2)	(97)	**80**
Other financial liabilities	**203**	322	(390)	(2)	**35**	**168**
Total	**18,248**	**7,826**	**(8,069)**	**264**	**(667)**	**17,602**

(1) It mainly includes the derecognition of the Electricaribe balances due to the deconsolidation of the holding following the loss of control (Note 8).

In the section “Other changes in cash and cash equivalents” are included cash variations due to changes in the consolidation scope and transfers to “Non-current assets held for sale”.

Note 31. Business combinations

2017

No significant business combinations took place in 2017.

2016

Vayu Limited

On 29 July 2016 Gas Natural Fenosa completed the purchase of 100% of the Irish gas and electricity supply company Vayu Limited (Vayu). The total cost of the business combination amounted to Euros 32 million. Goodwill was calculated at Euros 16 million as the difference between the acquisition cost and interest in the fair value of the identifiable assets and liabilities existing at the transaction date.
The net assets acquired at 31 July 2016 and goodwill break down as follows:

Acquisition cost	32
Fair value of the net assets	16
Goodwill (Note 5)	**16**

	Fair value	Carrying amount
Intangible assets (Note 5)	14	-
Other current assets	12	12
Cash and cash equivalents	10	10
TOTAL ASSETS	**36**	**22**
Deferred tax liabilities (Note 21)	2	-
Other current liabilities	18	18
TOTAL LIABILITIES	**20**	**18**
Net assets acquired	**16**	**4**
Fair value of the net assets acquired	**16**	
Acquisition price	32	
Cash and cash equivalents in subsidiary acquired	10	
Net acquisition cost	**22**	

If the operation had taken place on 1 January 2016, the impact of the operation on revenue and consolidated profit would not have been significant.

During the process for the assignment of the purchase price, assets were identified subject to restatement on the basis of the balance sheet of Vayu Limited at 31 July 2016. Vayu Limited 's net assets were basically measured using the following methodology:

- The business was valued following the revenue approach and in particular, through the discounted cash flow method, based on Level 3 inputs as the data were not observable on the market.

- The main parameters used in the valuation were a discount rate of 12.1% and a growth rate of 0%.

- The most sensitive assumptions included in the projections and which were based on sector forecasts and the analysis of historical information related to the evolution of electricity and gas margins.

As a result of the assignment process, an intangible asset restatement was recognised with respect to the value of the gas and electricity customer portfolio and the value of energy acquisition agreements. The deferred tax liabilities relating to the revaluations were also recognised.

No contingent liabilities were recognised at the date of the acquisition and therefore no provisions were recognised other than those figuring in the carrying value.

The provisional goodwill resulting from this business combination was attributed to the high profitability of the business acquired, the benefits and synergies that are expected to arise as a result of the combination and the existence of organised human capital in Vayu with considerable experience in the energy markets.

Ibereólica Cabo Leones II S.A.

On 15 December 2015 an agreement was reached for the acquisition of 51% of Ibereólica Cabo Leones II S.A by Gas Natural Fenosa through its subsidiary Global Power Generation Chile S.p.A. The business combination was recognised for accounting purposes in 2016, since it was in this financial year that the key information was obtained for such recognition and the twelve-month period from the acquisition established by IFRS 3 was completed.

Cabo Leones II was a 204 MW wind project which, in the energy auctions of 2016, was awarded a power supply contract with the Chile distribution system for 555 Gwh per year from 2020.

Through this acquisition, Gas Natural Fenosa carried out its commitment to enter the Chilean generation market,

The total cost of the business combination amounted to Euros 11 million. Goodwill was calculated at Euros 3 million as the difference between the acquisition cost and interest in the fair value of the identifiable assets and liabilities existing at the transaction date.

The net assets acquired at 01 January 2016 and goodwill break down as follows:

Acquisition cost	11
Fair value of the net assets	8
Goodwill (Note 5)	**3**

	Fair value	Carrying amount
Intangible assets (Note 5)	23	1
TOTAL ASSETS	**23**	**1**
Deferred tax liability *(Note 21)*	6	-
Trade and other payables	1	1
TOTAL LIABILITIES	**7**	**1**
Net assets acquired	**16**	**-**
Non-controlling interests (Note 13)	**8**	
Fair value of the net assets acquired	**8**	

Acquisition price	11
Cash and cash equivalents in subsidiary acquired	-
Net acquisition cost	**11**

In the purchase price allocation process, the assets were identified that could be revalued based on the balance sheet of Ibereólica Cabo Leones II S.A. at 1 January 2016, relating to intangible assets represented by the value of the authorisations necessary to operate the facility. The deferred tax liabilities relating to the revaluations were also recognised.

These net assets of Ibereólica Cabo Leones II S.A. were basically measured using the following methodology:

- The business was measured following the revenue approach and in particular, through the discounted cash flow method, based on Level 3 inputs as the data were not observable on the market.

- The main parameters used in the measurement were a discount rate of 9.2% and a growth rate of 0%.

- The most sensitive assumptions used in the projections, which were based on sectoral forecasts and the analysis of historical data, were the evolution of energy prices in the Chilean market and the estimated wind hours during the useful life of the facility.

Other acquisitions

In December 2016, Gas Natural Fenosa acquired, through GPG, 100% of Inca de Varas I, S.A. and Inca de Varas II, S.A. for an initial amount of Euros 1 million, basically relating to intangible assets. These companies were initiating the development of a photovoltaic solar generation facility in Chile with a capacity of 120 MW.

In addition, in December 2016 Gas Natural Fenosa acquired, through GPG, 85% of Sobral I Solar Energia SPE Ltda. and Sertao I Solar Energia SPE Ltda. for an overall amount of Euros 1 million, mainly relating to intangible assets. These companies are basically commencing the development of two photovoltaic solar generation facilities in Brazil with a joint capacity of 60 MW.

If these operations had taken place on 1 January 2016, the impact of the operations on revenue and consolidated profit would not have been significant.

The accounting recognition of all business combinations described in this Note has been definitively determined in 2017 without any changes with respect to the 2016 provisional accounting treatment.

Note 32. Service concession arrangements

Gas Natural Fenosa manages a number of concessions containing provisions for the construction, operation and maintenance of facilities, as well as connection and power supply obligations during the concession period, in accordance with applicable regulations (Note 2). There follow details of the concession period and the period remaining to the expiration of concessions that are not indefinite:

Company	Activity	Country	Concession period	Initial remaining period
Gas Natural BAN, S.A.	Gas distribution	Argentina	35 (extendable 10)	10
Energía San Juan S.A.	Electricity distribution (CGE)	Argentina	60	39
Companhia Distribuidora de Gás do Río de Janeiro, S.A, Ceg Rio, S.A. and Gas Natural Sao Paulo Sul, S.A.	Gas distribution	Brazil	30 (extendable 20/30)	10-13
Unión Fenosa Generadora La Joya, S.A. and Unión Fenosa Generadora Torito, S.A.	Electricity generation	Costa Rica	20	5-13
Gas Natural Fenosa Generación S.L.U., S.A. and Gas Natural Fenosa Renovables, S.L.	Hydraulic power generation	Spain	14-65	5-46
Gas Natural México S.A. de C.V. and Comercializadora Metrogas S.A. de C.V.	Gas distribution	Mexico	30 (extendable 15)	10-21
Europe Maghreb Pipeline Ltd	Gas transportation	Morocco	25 (extendable)	4
Empresa Distribuidora de Electricidad Metro Oeste, S.A. and Empresa Distribuidora de Electricidad Chiriqui, S.A.	Electricity distribution	Panama	15	11
Gas Natural Perú, S.A.	Gas distribution	Peru	20-year extendable	17

As indicated in Note 3.4.3.b, Gas Natural Fenosa applies IFRIC 12 “Service concession arrangements”, the intangible asset model being applicable basically to the gas distribution activities in Argentina, Brazil and Peru, and to the electricity distribution activity in Argentina, while the financial asset model applies to the electricity generation business in Costa Rica.

The hydraulic power plant concessions in Spain (Note 3.4.4.b) fall out with the scope of IFRIC 12, due among other reasons to the fact that power selling prices are set in the market. The other international concessions fall out with the scope of IFRIC 12 because the grantor does not control a significant residual interest in the infrastructure at the concession end date and simultaneously determines the service price. Concession assets are still recognised in “Property, plant and equipment”.

Note 33. Information on transactions with related parties

Related parties are as follows:

- Significant shareholders of Gas Natural Fenosa, 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 Gas Natural Fenosa are Fundación Bancaria Caixa d'Estalvis i Pensions de Barcelona ("la Caixa"), Repsol, S.A. (Repsol) and Global Infrastructure Partners III (GIP) and subsidiaries.

- Directors and executives of the company, and their immediate families. The term "director" means a member of the Board of Directors; "executive" means a member of the Management Committee of Gas Natural Fenosa and the Internal Audit Director. Operations with directors and executives are disclosed in Note 34.

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

The aggregates for operations with significant shareholders are as follows, in thousand euro:

	2017				2016			
	Significant shareholders			Group companies	Significant shareholders			Group companies
Expense and Income (thousand euros)	**"la Caixa"**	**Repsol**	**GIP**		**"la Caixa"**	**Repsol**	**GIP (*)**	
Financial expenses	1,509	-	-	55	2,799	-	-	100
Leases	-	-	-	5	-	-	-	5
Receipt of services	11,955	14,045	-	10,426	15,160	8,853	-	25,954
Purchases of goods (2)	-	345,504	-	330,014	-	236,845	-	300,478
Other expenses (1)	35,265	-	-	-	24,541	-	-	-
Total expenses	**48,729**	**359,549**	**-**	**340,500**	**42,500**	**245,698**	**-**	**326,537**
Financial income	653	-	-	154	247	-	-	415
Leases	-	-	-	-	-	-	-	-
Provision of services	559	38,629	-	21,430	462	1,363	-	22,079
Sales of goods (finished or in progress) (2)	22,971	817,607	-	44,812	25,909	694,196	-	44,240
Other income	-	-	-	2,296	-	-	-	2,007
Total income	**24,183**	**856,236**	**-**	**68,692**	**26,618**	**695,559**	**-**	**68,741**

	2017				2016			
	Significant shareholders			Group companies	Significant shareholders			Group companies
Other transactions (in thousand Euros)	**"la Caixa"**	**Repsol**	**GIP**		**"la Caixa"**	**Repsol**	**GIP (*)**	
Acquisition of property, plant and equipment, intangible assets or other assets (3)	-	10,879	-	-	-	424,651	-	-
Financing agreements, loans and capital contributions(lender) (4)	1,323,987	-	-	3,436	513,062	-	-	11,211
Sale of property, plant and equipment, intangibles or other assets (5)	362,465	-	-	-	274,528	-	-	-
Financing agreements: loans and capital contributions (borrower) (6)	119,541	-	-	-	123,316	-	-	-
Warranties and guarantees received	160,000	-	-	-	100,000	-	-	-
Dividends and other profits distributed	244,558	200,859	200,138	-	424,923	367,291	66,045	-
Other operations (7)	1,030,014	-	-	-	480,720	-	-	-

Trade debtors and creditors (thousand euros)	2017				2016			
	Significant shareholders			Group companies	Significant shareholders			Group companies
	"la Caixa"	Repsol	GIP		"la Caixa"	Repsol	GIP (*)	
Trade and other receivables	481	68,970	-	17,286	-	77,381	-	8,099
Trade and other payables	-	42,755	-	31,219	-	20,828	-	30,351

(*) Since 21 September 2016.

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

(2) Basically includes sales and procurements of energy. In the case of group companies, it basically includes the operations with Unión Fenosa Gas.

(3) Basically includes the purchase of LPG supply points under the agreement with Repsol Butano dated 30 September 2015, that are located in the area of influence of its existing distribution zones and which is completed as the relevant administrative authorisations are obtained.

(4) Includes cash and cash equivalents.

(5) Includes basically the assignment of debt claims (factoring without recourse) with "la Caixa" each of the years.

(6) At 31 December 2017, credit lines contracted with "la Caixa" amounted to Euros 569,000 thousand (Euros 569,000 thousand at 31 December 2016), of which no amounts having been utilised. "La Caixa" also has shares of other loans totalling Euros 119,541 thousand. (Euros 123,316 thousand at 31 December 2016).

(7) At 31 December 2017, the item "Other transactions" with "la Caixa" includes Euros 915,920 thousand in respect of foreign exchange hedges and Euros 114,094 thousand in respect of interest rate hedges (Euros 348,962 thousand and Euros 131,758 thousand at 31 December 2016).

Note 34. Information on members of the Board of Directors and senior management personnel

Remuneration of the members of the Board of Directors

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

The amount accrued by the members the Board of Directors of Gas Natural SDG, S.A., for belonging to the Board of Directors, Executive Committee (EC), Audit Committee (CA) and Appointments and Remuneration Committee (ARM), totalled Euros 4,668 thousand (Euros 4,573 thousand in 2016), broken down in euros as follows:

	Office	Board	EC	AC	ARC	Total
Mr. Isidro Fainé Casas	Chairman	550,000	550,000	-	-	1,100,000
Mr. Josu Jon Imaz San Miguel	First Deputy Chairman	126,500	126,500	-	-	253,000
Mr. William Alan Woodburn	Second Deputy Chairman	126,500	126,500	-	25,000	278,000
Mr . Rafael Villaseca Marco	Chief Executive Officer	126,500	126,500	-	-	253,000
Mr . Ramón Adell Ramón	Director	126,500	126,500	40,000	-	293,000
Mr . Enrique Alcántara-García Irazoqui	Director	126,500	-	40,000	-	166,500
Mr . Xabier Añoveros Trías de Bes	Director	126,500	-	40,000	-	166,500
Mr . Marcelino Armenter Vidal	Director	126,500	126,500	-	-	253,000
Mr . Mario Armero Montes	Director	126,500	-	-	-	126,500
Mr . Francisco Belil Creixell	Director	126,500	126,500	-	25,000	278,000
Ms. Benita María Ferrero-Waldner	Director	126,500	126,500	-	-	253,000
Mr . Alejandro García-Bragado Dalmau	Director	126,500	-	-	25,000	151,500
Ms. Cristina Garmendia Mendizábal	Director	126,500	-	40,000	25,000	191,500
Ms. Helena Herrero Starkie	Director	126,500	-	40,000	-	166,500
Mr . Miguel Martínez San Martín	Director	126,500	126,500	-	25,000	278,000
Mr. Rajaram Rao	Director	126,500	126,500	40,000	-	293,000
Mr. Luis Suárez de Lezo Mantilla	Director	126,500	-	40,000	-	166,500
		2,574,000	**1,688,500**	**280,000**	**125,000**	**4,667,500**

As the remuneration for belonging to the Board of Directors and the various Board Committees has remained unchanged, the increase is due solely to the higher number of Committee members as a result of changes in the company's corporate governance following the alteration in September 2016 of the company's shareholder structure. In this respect, the Executive Committee has increased by 2 members, the Audit Committee has increased by 4 members and the Appointments and Remuneration committee has increased by 2 members.

In 2017, as in 2016, no amounts were received for other items.

In 2017, the Chief Executive Officer did not receive any amount as a Board member of the investee companies (Euros 37 thousand in 2016). These amounts are deducted from the CEO's annual variable remuneration.

The amounts accrued to the Chief Executive Officer for executive functions in respect of fixed remuneration, annual variable remuneration, multi-year variable remuneration and other items totalled Euros 1,285 thousand, Euros 1,131 thousand, Euros 757 thousand and Euros 16 thousand, respectively, in 2017 (Euros 1,212 thousand, Euros 1,002 thousand, Euros 813 thousand and Euros18 thousand in 2016).

Contributions to pension plans and group insurance policies, together with life insurance premiums paid, totalled Euros 321 thousand in 2017 (Euros 318 thousand in 2016). Funds accumulated due to these contributions amount to Euros 3,648 thousand at 31 December 2017 (Euros 3,241 thousand at 31 December 2016).

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

The members of the Board of Directors are covered with the same liability policy that insures all managers and directors of Gas Natural Fenosa. The premium paid in 2017 by Gas Natural SDG, S.A. for the entire policy amounted to Euros 109 thousand (Euros 101 thousand in 2016).

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

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

The CEO's contract provides for an indemnity of three yearly payments of his full emoluments at the date of the contractual amendment for certain termination events: by decision of the company, excepting a serious and culpable breach of his professional obligations giving rise to serious damage to the interests of Gas Natural SDG, S.A.; by decision of the CEO; or due to the completion of the contract. In addition, as consideration for a post-contractual no-competition agreement with a duration of one year, an indemnity equivalent to one year's full remuneration is provided for.

The contract provides for the obligation on the Company's part to arrange third party liability insurance.

Transactions with Directors

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

The Directors of Gas Natural SDG, SA have not reported to the Board of Directors any conflict of interests that has to be informed.

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

During the years 2017 and 2016, 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.

Management Committee remuneration

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

During 2017 a total of 11 persons formed part of the Management Committee, of which one is a woman. One person joined the committee in April.

Amounts accrued to executives in respect of fixed remuneration, annual variable remuneration, multi-year variable remuneration and other items totalled Euros 5,507 thousand, Euros 2,595 thousand, Euros 1,641 thousand and Euros 108 thousand, respectively, in 2017 (Euros 4,827 thousand, Euros 2,553 thousand, Euros 1,852 thousand and Euros 120 thousand, respectively, in 2016).

Contributions to pension plans and group insurance policies, together with life insurance premiums paid, totalled Euros 2,564 thousand in 2017 (Euros 2,389 thousand in 2016). Funds accumulated due to these contributions amount to Euros 26,367 thousand at 31 December 2017 (Euros 22,121 thousand at 31 December 2016).

The executives have received no remuneration in respect of profit sharing or bonuses and no loans have been granted to them. The management personnel does not have advance payments (Euros 175 thousand at 31 December 2016). At 31 December 2017, Gas Natural Fenosa has granted guarantees on credits to management personnel for an amount of Euros 754 thousand. As of December 31, 2016 there were no guarantees granted. No indemnities were received during 2017 or 2016.

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

Note 35. Contingent liabilities and assets, guarantees and commitments

The companies in the Gas Natural Fenosa Group are involved in certain judicial and extrajudicial disputes within the ordinary course of their activities. At the date of preparation of these consolidated annual accounts, the main litigation or arbitration in which Gas Natural Fenosa companies are involved are the following:

Contingent liabilities and assets

Claims for PIS and COFINS taxes in Brazil

In September 2005, the Río de Janeiro Tax Administration rendered ineffective the recognition that it had previously issued, in April 2003, for the offset of receivables in respect of PIS and COFINS sales taxes paid by Companhia Distribuidora de Gás do Rio de Janeiro - CEG, in which Gas Natural Fenosa holds an interest of 54.2%. The administrative court confirmed that ruling in March 2007 and the company filed an appeal at a contentious-administrative court (Justicia Federal do Rio de Janeiro). Subsequently, notification of a public civil action against CEG relating to the same events was received on 26 January 2009. The total amount of tax payable in dispute, including interest, amounted to BRL 386 million (Euros 97 million). In November 2015, the above-mentioned first-instance court issued a judgement partially allowing CEG's appeal and reducing the total amount to BRL 260 million (Euros 66 million). This reduction in the amount of the contingency will not be final until the possible appeals have been lodged, which could take another four years according to a preliminary estimate. Gas Natural Fenosa has appealed against the judgment and considers, together with the company's legal advisors that even the reduced amount is unfounded.

Qatar Gas arbitration

In May 2015, Gas Natural Fenosa 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. Gas Natural Fenosa has requested a price reduction and the supplier has requested an increase. The award has been notified on 3 February 2018 and contains various pronouncements that require negotiations between the parties, although from its analysis it turns out that the effects, positive or negative, if they occur, would not significantly affect the financial statements.

Claim against Metrogas, S.A.

Transportadora de Gas del Norte S.A. lodged various complaints against Metrogas, S.A., a Chilean company 54.2% owned by Gas Natural Fenosa, before the civil and commercial courts of first instance in Argentina for supposed breach of contract in the transport of Argentinian gas to Chile during the Argentina gas crisis. In April 2017, Metrogas, S.A. received a judicial notice declaring a joinder of claims, meaning that the total amount stands at USD 227 million (Euros 189 million). The procedures are at the evidence stage.

Environmental incentive to coal plants in Spain

In 2007, the Spanish authorities introduced an environmental incentive to support the installation of new sulphur oxide filters in existing coal plants. To date, Gas Natural Fenosa has received Euros 63 million for this incentive. In November 2017, the European Commission opened an investigation to determine whether this incentive complied with the European Union's state aid rules.

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 Gas Natural Fenosa, 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, who requested the contract to be invalid, and against the Arab Republic of Egypt. With respect to the gas supply, 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 and before the CIADI have yet to be delivered.

Gas Natural Fenosa considers that no significant liabilities will be derived from the risks described in the relevant section of this Note.

Guarantees

As at 31 December 2017 and 2016 guarantees provided by Gas natural Fenosa were as follows:

- Guarantees provided to third parties basically related to investment commitments, constructions and distribution network expansion, bidding and tenders and contracts for their activities amounting to Euros 1,251 million (Euros 1,332 million at 31 December 2016)
- Guarantees related to economic obligations derived from its participation and operation in the Spanish gas system (MIBGAS) and the Spanish electricity system (MEFF and OMIE) totalling Euros598 million (Euros 481 million at 31 December 2016).
- Financial guarantees corresponding to the guarantee of compliance with the loan obligations received by investees amounting Euros 100 million (Euros 126 million at 31 December 2016).
- Debt issue guarantees made by the group companies, Gas Natural Capital Markets, S.A., Gas Natural Finance, B.V., Unión Fenosa Preferentes, S.A.U. and Gas Natural mexico S.A. de CV for an amount of Euros 12.879 million (Euros 11.982 million at 31 December 2016).
- Guarantees for gas supply and transport contracts obligations as well as charter contracts for gas tankers of the group companies Gas Natural Aprovisionamientos, S.A. and Gas Natural Europe, S.A.S.

- Irrevocable guarantee by Gas Natural SDG, S.A. of all the liabilities and commitments of Vayu Ltd and its subsidiaries in Ireland at 31 December 2017 pursuant to Section 357 of the 2014 Companies Act of Ireland in order to file the consolidated financial statements of Gas Natural Fenosa instead of its separate financial statements, on the basis of the exemption allowed under Section 1 (b) of said Act.

Given that the aforementioned guarantees are basically granted in order to guarantee compliance with contractual obligations or investment commitments, the events that would lead to its execution, and therefore the disbursement in cash, would be breaches by Gas Natural Fenosa of its obligations in relation to the ordinary course of its activity, which is considered to have a probability of remote occurrence. Gas Natural Fenosa estimates that the liabilities not foreseen at 31 December 2017, if any, that could arise from guarantees furnished, would not be significant.

Contractual commitments

The following tables present the contractual commitments for purchases and sales at 31 December 2017:

	At 31 December 2017						
Acquisition	**Total**	**2018**	**2019**	**2020**	**2021**	**2022**	**and later years**
Energy purchases (1)	71,707	6,647	6,165	6,188	5,894	4,449	42,364
Energy transmission (2)	3,423	462	478	503	523	140	1,317
Investment (3)	726	600	84	39	1	1	1
Operating leases (4)	266	92	45	38	17	16	58
Nuclear fuel purchases	35	17	18	-	-	-	-
Total contractual obligations	**76,157**	**7,818**	**6,790**	**6,768**	**6,435**	**4,606**	**43,740**

		At 31 December 2017					
Sale	**Total**	**2018**	**2019**	**2020**	**2021**	**2022**	**and later years**
Energy sales (5)	15,140	3,154	1,966	1,601	1,083	857	6,479
Provision of capacity assignment services (6)	3,366	233	248	293	263	268	2,061
Total contractual obligations	**18,506**	**3,387**	**2,214**	**1,894**	**1,346**	**1,125**	**8,540**

1) Basically reflects the long-term commitments for natural gas purchases amounted to Euros 71,108 million under gas supply contracts with take or pay clauses negotiated and held for “own use” (Note 3.4.7.3). Normally, these contracts are for 20-25 years, a minimum amount of gas to be purchased and revision mechanisms for prices indexed to international natural gas prices and regulated prices of natural gas in the countries of origin. The commitments according to these contracts have been calculated on the basis of natural gas prices at 31 December 2017.

   This also includes long-term commitments to buy electricity, calculated based on prices at 31 December 2017.

2) Reflects the long-term commitments (20 to 25 years) for gas transport and electricity transmission calculated on the basis of prices at 31 December 2017. It also reflects operating costs associated with charter contracts for gas tankers under finance leases, including the six operational tankers (Note 18) and the two tankers under construction (Note 6), which are expected to become operational in 2018.

3) Basically reflects the investment commitments for the construction of two gas tankers expected to enter services in 2018 (Note 6), the construction of new power generation facilities and the development of the gas and electricity distribution network.

4) It mainly reflects the commitments for operating leases on ships which mature in 2020 and commitments under property leases.

   It includes the rent of the “Torre del Gas” building owned by Torre Marenostrum, S.L., for which Gas Natural Fenosa has an operating lease without a purchase option until the year 2019 with option to extend at market value for successive periods of three years, on a discretionary basis for Gas Natural Fenosa and an obligatory basis for Torre Marenostrum S.L.

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

5) Basically reflects long-term commitments to sell natural gas under gas sale contracts, containing take-or-pay clauses, negotiated and held for "own use" (Note 3.4.7.3). The commitments have been calculated based on natural gas prices at 31 December 2017.

6) Reflects service provision commitments under power generation capacity assignment contracts in Mexico (Note 3.4.19). The commitments made in these contracts have been calculated based on prices at 31 December 2017.

Note 36. Auditors' fees

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

	Thousand Euro					
	2017			2016(1)		
	PwC Auditores, S.L.	Other network PwC	Total	PwC Auditores, S.L.	Other network PwC	Total
Auditing services	2,249	1,271	**3,520**	1,905	1,512	3,417
Assurance services and services related to the audit (2)	383	230	**613**	572	256	828
Other services (2)	146	1,059	**1,205**	137	96	233
Total fees	**2,778**	**2,560**	**5,338**	**2,614**	**1,864**	**4,478**

(1) The consolidated income statement for 2016 has been restated reclassifying to discontinued operations under IFRS 5 (Notes 3.3 and 9).

(2) In PwC Audirores, S.L. includes in this heading the verification reports of non-financial information, comfort letters and guidance on the issue of sustainability.

Additionally, other audit firms have rendered the following services to Group companies:

	Thousand Euro	
	2017	2016(1)
Auditing services	1,468	2,257
Assurance services and services related to the audit	-	-
Other services	662	336
Total fees	**2,130**	**2,593**

(1) The consolidated income statement for 2016 has been restated to discontinued operations under IFRS 5 (Notes 3.3 and 9).

The calculation of auditor fees for the current and period and in the comparative analysis with the previous year does not take into account the fees relating to companies that have been reclassified to discontinued operations, amounting to Euros 624 million with respect to the fees accrued by companies operating under the PwC brand and Euros 61 thousand accrued by other audit firms (Euros 489 thousand and Euros 50 thousand at 31 December 2016, respectively).

Note 37. Environment

Environmental actions

The Environmental Strategy is based on four environmental pillars that are defined according to the key vectors of the company's environmental management system:

- Climate and Air: Reducing emissions through our operations and promoting the use of sustainable energy.
- Water: Promoting the efficient and responsible use of water.
- Natural Capital: Minimising the impacts on ecosystems and promoting natural capital.
- Circular Economy: Optimising resource consumption and enhancing resource recirculation.

This is achieved through environmental management of Gas Natural Fenosa based on the ISO 14001 model, the correct functioning of which is verified periodically, providing the tools required to assure environmental management. In this context, in 2017 the adaptation to the 2015 reference framework was completed and the certification of environmental management was extended to electricity and gas distribution companies in Chile.

With respect to air and the climate, Gas Natural Fenosa bases its strategy on five lines of action: the reduction of emissions in its operations through low-carbon energy and renewable energy sources, the reduction of emissions through energy efficiency, the development of sustainable products and services, the integration of the climate variable into internal management and the calculation of impact and performance. During 2017, there has been an increase in direct CO_2 emissions compared with 2016 as a direct result of a significant reduction in non-emission generation in Spain due to adverse weather conditions, which has led to an increase in thermal energy production and therefore an increase in CO_2 emissions. As a result, the specific emission per unit of energy generated has also increased compared with 2016.

With regard to water management, in 2017 actions were carried out focusing on optimising consumption and reducing waste discharges, promoting sustainable use in stakeholders, inclusion in decision-making and determining impact and performance. In spite of this, in 2017 there was an increase in water use, primarily due to the increased demand in the activity of coal-fired and combined cycle power plants

In 2017, Gas Natural Fenosa has conducted multiple actions in the natural capital and biodiversity area, all of which are aligned with the reduction in and compensation for its impacts, the enhancement of the value of the natural surroundings and the determination of its impact on natural capital.

Within the axis of the circular economy, actions have been carried out associated with the optimisation of raw materials consumption, reduction of waste generation, contribution to the development of regulations and the determination of impact and performance.

All these environmental activities undertaken in 2017 amounted to Euros 96 million (Euros 90 million in 2016), of which Euros 17 million related to environmental investments and Euros 79 million relate to environmental management expenditure on the environmental management of the facilities, excluding that derived from the coal market. These actions include those relating to the improvement of security at nuclear power plants, the improvement of combustion systems in thermal power stations to reduce NOx emissions, the improvement of hydro generation facilities and the launch of new photovoltaic energy products in the energy solutions segment.

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

Issuances

In 2017, total consolidated CO_2 emissions from Gas Natural Fenosa' coal thermal and combined cycle plants subject to regulations governing the greenhouse gas emission trade regime totalled 11.2 million tonnes of CO_2 (10.4 million tonnes of CO_2 in 2016).

Gas Natural Fenosa devises a strategy each year for managing its CO_2 emission allowance coverage portfolio, acquiring them through its active participation both in both the primary and secondary markets. In addition, it has a committed investment of approximately Euros 1 million in primary projects and carbon funds, for the provision of emission credits.

Note 38. Events after the balance sheet date

On 16 January 2018 Gas Natural Fenosa, through its Euro Medium Term Notes (EMTN) programme, carried out a bond issue amounting to Euros 850 million, maturing in January 2028 with an annual coupon of 1.5%.%. The revenues obtained from this issue have been used in a buy-back of bonds maturing between 2019 and 2023 amounting to Euros 916 million, which was completed on 23 January 2018.

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APPENDIX I Gas Natural Fenosa companies

1. Subsidiaries

Company	Country	Activity	Method of Consolidation (1)	Total % interest % Controlling interest (2)	% Equity interest
Gas Natural BAN, S.A.	Argentina	Gas distribution	F.C.	70.0	70.0
Ceg Río, S.A.	Brazil	Gas distribution	F.C.	59.6	59.6
Companhia Distribuidora de Gás do Río de Janeiro, S.A.	Brazil	Gas distribution	F.C.	54.2	54.2
Gas Natural Sao Paulo Sul, S.A.	Brazil	Gas distribution	F.C.	100.0	100.0
Gas Natural Redes GLP, S.A.	Spain	Gas distribution	F.C.	100.0	100.0
Gas Natural Transporte SDG, S.L.	Spain	Gas distribution	F.C.	100.0	100.0
Holding de Negocios de Gas, S.A.U.	Spain	Gas distribution	F.C.	100.0	100.0
Nedgia Andalucía, S.A.	Spain	Gas distribution	F.C.	100.0	100.0
Nedgia Aragón, S.A.	Spain	Gas distribution	F.C.	100.0	100.0
Nedgia Balears, S.A.	Spain	Gas distribution	F.C.	100.0	100.0
Nedgia Castilla La-Mancha, S.A.	Spain	Gas distribution	F.C.	95.0	95.0
Nedgia Castilla y León, S.A.	Spain	Gas distribution	F.C.	90.1	90.1
Nedgia Catalunya, S.A.	Spain	Gas distribution	F.C.	100.0	100.0
Nedgia Cegas, S.A.	Spain	Gas distribution	F.C.	99.7	99.7
Nedgia Galicia, S.A.	Spain	Gas distribution	F.C.	68.5	68.5
Nedgia Madrid, S.A.	Spain	Gas distribution	F.C.	100.0	100.0
Nedgia Navarra, S.A.	Spain	Gas distribution	F.C.	100.0	100.0
Nedgia Redes Distribución Gas, S.A.	Spain	Gas distribution	F.C.	100.0	100.0
Nedgia Rioja, S.A.	Spain	Gas distribution	F.C.	87.5	87.5
Nedgia, S.P.A. (4)	Italy	Gas distribution	F.C.	100.0	100.0
Comercializadora Metrogas, S.A. de CV (3)	Mexico	Gas distribution	F.C.	100.0	85.0
Gas Natural México, S.A. de CV (3)	Mexico	Gas distribution	F.C.	85.0	85.0
Gas Natural Fenosa Perú, S.A.	Peru	Gas distribution	F.C.	100.0	100.0
Unión Fenosa Distribución, S.A.	Spain	Electricity distribution	F.C.	100.0	100.0
Gas Natural Fenosa Furnizare Energie, S.R.L. (4)	Moldova	Electricity distribution	F.C.	100.0	100.0
Red Unión Fenosa, S.A. (4)	Moldova	Electricity distribution	F.C.	100.0	100.0
Empresa de Distribución Electrica Chiriqui, S.A.	Panama	Electricity distribution	F.C.	51.0	51.0
Empresa de Distribución Electrica Metro Oeste, S.A.	Panama	Electricity distribution	F.C.	51.0	51.0
Gas Natural Almacenamientos Andalucía, S.A.	Spain	Gas infrastructures	F.C.	100.0	100.0
Gas Natural Exploración, S.L.	Spain	Gas infrastructures	F.C.	100.0	100.0
Palencia 3 Investigación Desarrollo y Explotación, S.L.	Spain	Gas infrastructures	F.C.	63.9	63.9
Petroleum Oil & Gas España, S.A.	Spain	Gas infrastructures	F.C.	100.0	100.0
Gas Natural Rigassificazione Italia, S.P.A.	Italy	Services	F.C.	100.0	100.0
Metragaz, S.A.	Morocco	Gas infrastructures	F.C.	76.7	76.7
Europe Maghreb Pipeline, Ltd.	United Kingdom	Gas infrastructures	F.C.	77.2	77.2
Natural Energy, S.A.	Argentina	Gas commercialisation	F.C.	100.0	100.0
Gas Natural Serviços, S.A.	Brazil	Gas commercialisation	F.C.	100.0	100.0
Serviconfort Colombia, S.A.S. (4)	Colombia	Gas commercialisation	F.C.	100.0	100.0
Gas Natural Servicios, S.A. de C.V. (3)	Mexico	Gas commercialisation	F.C.	100.0	85.0
Gas Natural Aprovisionamientos SDG, S.A.	Spain	Gas commercialisation	F.C.	100.0	100.0

Company	Country	Activity	Method of Consolidation (1)	Total % interest % Controlling interest (2)	% Equity interest
Gas Natural Fenosa LNG, S.L.	Spain	Gas commercialisation	F.C.	100.0	100.0
Sagane, S.A.	Spain	Gas commercialisation	F.C.	100.0	100.0
Gas Natural Europe, S.A.S.	France	Gas commercialisation	F.C.	100.0	100.0
Gas Natural Fenosa LNG GOM Limited	Ireland	Gas commercialisation	F.C.	100.0	100.0
Gas Natural Fenosa LNG International Ltd	Ireland	Gas commercialisation	F.C.	100.0	100.0
Gas Natural Fenosa LNG Marketing Ltd	Ireland	Gas commercialisation	F.C.	100.0	100.0
Gas Natural Fenosa LNG Singapore Pte. Ltd	Singapore	Gas commercialisation	F.C.	100.0	100.0
Gas Natural Vendita Italia, S.P.A. (4)	Italy	Gas commercialisation	F.C.	100.0	100.0
Gas Natural Puerto Rico, Inc	Puerto Rico	Gas commercialisation	F.C.	100.0	100.0
La Energía, S.A.	Spain	Gas commercialisation	F.C.	100.0	100.0
Gas Natural Comercializadora, S.A.	Spain	Gas and electricity commercialisation	F.C.	100.0	100.0
Gas Natural S.U.R. SDG, S.A.	Spain	Gas and electricity commercialisation	F.C.	100.0	100.0
Gas Natural Servicios SDG, S.A.	Spain	Gas and electricity commercialisation	F.C.	100.0	100.0
Mataró Energía Sostenible, S.A.	Spain	Gas and electricity commercialisation	F.C.	51.1	51.1
Vayu Energy, Ltd	Ireland	Gas and electricity commercialisation	F.C.	100.0	100.0
Vayu Ltd	Ireland	Gas and electricity commercialisation	F.C.	100.0	100.0
Vayu Energy, Ltd (UK)	United Kingdom	Gas and electricity commercialisation	F.C.	100.0	100.0
Berrybank Development Pty, Ltd	Australia	Electricity generation	F.C.	100.0	74.0
Crookwell Development Pty, Ltd	Australia	Electricity generation	F.C.	100.0	74.0
Ryan Corner Development Pty, Ltd	Australia	Electricity generation	F.C.	100.0	74.0
Sertao i Solar Energía, SPE, Ltda	Brazil	Electricity generation	F.C.	85.0	63.8
Sobral i Solar Energía, SPE, Ltda	Brazil	Electricity generation	F.C.	85.0	63.8
GPG Solar Chile 2017 SpA	Chile	Electricity generation	F.C.	100.0	75.0
Iberéolica Cabo Leones II, S.A.	Chile	Electricity generation	F.C.	51.0	38.3
Inca de Varas I	Chile	Electricity generation	F.C.	100.0	75.0
Inca de Varas II	Chile	Electricity generation	F.C.	100.0	75.0
Parque Eólico Vientos del Pacífico, S.p.A	Chile	Electricity generation	F.C.	100.0	75.0
Hidroeléctrica Rio San Juan S.A.S. ESP	Colombia	Electricity generation	F.C.	100.0	75.0
Almar Ccs, S.A.	Costa Rica	Electricity generation	F.C.	100.0	75.0
P.H. La Perla, S.A.	Costa Rica	Electricity generation	F.C.	100.0	100.0
Unión Fenosa Generadora La Joya, S.A.	Costa Rica	Electricity generation	F.C.	65.0	48.8
Unión Fenosa Generadora Torito, S.A.	Costa Rica	Electricity generation	F.C.	65.0	48.8
Boreas Eólica 2, S.A.	Spain	Electricity generation	F.C.	89.6	89.6
Corporación Eólica de Zaragoza, S.L	Spain	Electricity generation	F.C.	68.0	68.0
Energías Ambientales de Somozas, S.A.	Spain	Electricity generation	F.C.	97.0	97.0
Energías Especiales Alcoholeras, S.A., En Liquidación	Spain	Electricity generation	F.C.	82.3	82.3
Explotaciones Eólicas Sierra de Utrera, S.L.	Spain	Electricity generation	F.C.	75.0	75.0
Fenosa Wind, S.L.U.	Spain	Electricity generation	F.C.	100.0	100.0
Fenosa, S.L.U.	Spain	Electricity generation	F.C.	100.0	100.0
Gas Natural Fenosa Generación, S.L.U.	Spain	Electricity generation	F.C.	100.0	100.0
Gas Natural Fenosa Renovables Ruralia, S.L.U.	Spain	Electricity generation	F.C.	75.0	75.0
Gas Natural Fenosa Renovables, S.L.U.	Spain	Electricity generation	F.C.	100.0	100.0

Company	Country	Activity	Method of Consolidation (1)	Total % interest % Controlling interest (2)	% Equity interest
Gas Natural Wind 4, S.L.U.	Spain	Electricity generation	F.C.	100.0	100.0
Global Power Generation, S.A.	Spain	Electricity generation	F.C.	75.0	75.0
J.G.C. Cogeneración Daimiel, S.L.	Spain	Electricity generation	F.C.	97.6	97.6
P.E. El Hierro, S.L.	Spain	Electricity generation	F.C.	95.0	95.0
P.E. Montamarta, S.L.	Spain	Electricity generation	F.C.	95.0	95.0
P.E. Nerea, S.L.	Spain	Electricity generation	F.C.	95.0	95.0
P.E. Peñarroldana, S.L.	Spain	Electricity generation	F.C.	95.0	95.0
Sociedad de Tratamiento Hornillos, S.L., en liquidación	Spain	Electricity generation	F.C.	94.4	94.4
Sociedad de Tratamiento La Andaya, S.L., en liquidación	Spain	Electricity generation	F.C.	60.0	60.0
Sociedad Parque Eólico Mouriños, S.L.U.	Spain	Electricity generation	F.C.	100.0	100.0
Societat Eòlica de l´Enderrocada, S.A.	Spain	Electricity generation	F.C.	80.0	80.0
Tratamiento Cinca Medio, S.L. en liquidación	Spain	Electricity generation	F.C.	80.0	80.0
Tratamiento de Almazán, S.L., en liquidación	Spain	Electricity generation	F.C.	90.0	90.0
Iberáfrica Power Ltd. (4)	Kenya	Electricity generation	F.C.	100.0	75.0
El Gritón Solar S.A. de C.V.	Mexico	Electricity generation	F.C.	80.0	60.0
Fuerza y Energía Bii Hioxo, S.A. de C.V.	Mexico	Electricity generation	F.C.	100.0	75.0
Fuerza y Energía de Hermosillo, S.A. de C.V.	Mexico	Electricity generation	F.C.	100.0	75.0
Fuerza y Energía de Naco Nogales, S.A. de C.V.	Mexico	Electricity generation	F.C.	100.0	75.0
Fuerza y Energía de Norte Durango, S.A de C.V	Mexico	Electricity generation	F.C.	100.0	75.0
Fuerza y Energía de Tuxpan, S.A. de C.V.	Mexico	Electricity generation	F.C.	100.0	75.0
Energía y Servicios de Panamá, S.A.	Panama	Electricity generation	F.C.	51.0	38.3
Generadora Palamara La Vega, S.A.	Dominican Rep.	Electricity generation	F.C.	100.0	75.0
Lignitos de Meirama, S.A.	Spain	Mining	F.C.	100.0	100.0
Kangra Coal (Proprietary), Ltd.	South Africa	Mining	F.C.	70.0	70.0
Welgedacht Exploration Company, Ltd	South Africa	Mining	F.C.	100.0	70.0
Gas Natural Informática, S.A.	Spain	IT services	F.C.	100.0	100.0
United Saudi Spanish Power and Gas Services, LLC	Saudi Arabia	Engineering services	F.C.	100.0	78.8
Gas Natural Fenosa Engineering Brasil , S.A.	Brazil	Engineering services	F.C.	100.0	100.0
Gas Natural Fenosa Engineering, S.A.S.	Colombia	Engineering services	F.C.	100.0	100.0
Gas Natural Fenosa Ingeniería y Desarrollo de Gen., S.A.S.	Colombia	Engineering services	F.C.	100.0	75.0
Gas Natural Fenosa Ingeniería y Desarrollo de Gen., S.A.	Costa Rica	Engineering services	F.C.	100.0	75.0
Operación y Mantenimiento Energy Costa Rica, S.A.	Costa Rica	Engineering services	F.C.	100.0	75.0
Soluziona Technical Services, Llc. En Liquidación	Egypt	Engineering services	F.C.	100.0	100.0
Gas Natural Fenosa Engineering, S.L.	Spain	Engineering services	F.C.	100.0	100.0
Gas Natural Fenosa Ingeniería y Desarrollo de Gen., S.L.	Spain	Engineering services	F.C.	100.0	75.0
Operación y Mantenimiento Energy, S.A.	Spain	Engineering services	F.C.	100.0	75.0
Proyectos Balmes México, S.A. de C.V.	Mexico	Engineering services	F.C.	100.0	75.0
Gas Natural Fenosa Ingeniería y Desarrollo de Gen., S.A.	Guatemala	Engineering services	F.C.	100.0	75.0
Spanish Israeli Operation and Maintenance Company, Ltd.	Israel	Engineering services	F.C.	100.0	100.0
Gas Natural Fenosa Ingenieria México, S.A. de C.V.	Mexico	Engineering services	F.C.	100.0	100.0
Gas Natural Fenosa Ingenieria y Desarrollo de Gen. México, S.A. de C.V.	Mexico	Engineering services	F.C.	100.0	75.0
GPG Energía México, S.A. de C.V.	Mexico	Electricity generation	F.C.	100.0	75.0
Unión Fenosa Operación México S.A. de C.V.	Mexico	Engineering services	F.C.	100.0	75.0

Company	Country	Activity	Method of Consolidation (1)	Total % interest % Controlling interest (2)	% Equity interest
Gas Natural Fenosa Engineering Panamá, S.A.	Panama	Engineering services	F.C.	100.0	100.0
Gas Natural Fenosa Technology INC	Puerto Rico	Engineering services	F.C.	100.0	75.0
Operations & Maintenance Energy Uganda Ltd	Uganda	Engineering services	F.C.	100.0	75.0
Natural Re, S.A.	Luxembourg	Insurance	F.C.	100.0	100.0
Gas Natural Capital Markets, S.A.	Spain	Financial services	F.C.	100.0	100.0
Unión Fenosa Financiación, S.A.	Spain	Financial services	F.C.	100.0	100.0
Unión Fenosa Preferentes, S.A.U.	Spain	Financial services	F.C.	100.0	100.0
Gas Natural Fenosa Finance B.V.	Netherlands	Financial services	F.C.	100.0	100.0
Clover Financial and Treasury Services, DAC.	Ireland	Financial services	F.C.	100.0	100.0
Natural Servicios, S.A.	Argentina	Services	F.C.	100.0	100.0
Gas Natural do Brasil, S.A.	Brazil	Services	F.C.	100.0	100.0
Gas Natural Servicios Económicos, S.A.S.	Colombia	Services	F.C.	100.0	100.0
Gas Natural Servicios Integrales, S.A.S.	Colombia	Services	F.C.	100.0	100.0
Compañía Española de Industrias Electroquímicas, S.A.	Spain	Services	F.C.	98.5	98.5
General de Edificios y Solares, S.L.	Spain	Services	F.C.	100.0	100.0
Gas Natural Italia S.P.A. (4)	Italy	Services	F.C.	100.0	100.0
Administración y Servicios ECAP, S.A. de C.V.	Mexico	Services	F.C.	100.0	100.0
Administradora de Servicios de Energía México, S.A. de CV (3)	Mexico	Services	F.C.	100.0	85.0
Energía y Confort Administración de Personal, S.A. de C.V. (3)	Mexico	Services	F.C.	100.0	85.0
Sistemas de Administración y Servicios, S.A. de C.V. (3)	Mexico	Services	F.C.	85.0	85.0
Gas Natural Fenosa Servicios Panamá, S.A.	Panama	Services	F.C.	100.0	100.0
Inversiones Hermill, S.A.	Dominican Rep.	Services	F.C.	100.0	100.0
Gas Natural SDG Argentina, S.A.	Argentina	Holding company	F.C.	100.0	100.0
Invergás, S.A.	Argentina	Holding company	F.C.	100.0	100.0
Global Power Generation Australia Pty, Ltd.	Australia	Holding company	F.C.	98.7	74.0
Global Power Generation Chile, S.p.A.	Chile	Holding company	F.C.	100.0	75.0
Gas Natural Distribución Latinoamerica, S.A.	Spain	Holding company	F.C.	100.0	100.0
Gas Natural Fenosa Electricidad Colombia, S.L.	Spain	Holding company	F.C.	100.0	100.0
Gas Natural Fenosa Internacional, S.A.	Spain	Holding company	F.C.	100.0	100.0
Nedgia, S.A.	Spain	Holding company	F.C.	100.0	100.0
La Propagadora del Gas Latam, S.L.U.	Spain	Holding company	F.C.	100.0	100.0
La Propagadora del Gas, S.A.	Spain	Holding company	F.C.	100.0	100.0
Unión Fenosa Minería, S.A.	Spain	Holding company	F.C.	100.0	100.0
Gas Natural Fenosa Minería, B.V.	Netherlands	Holding company	F.C.	100.0	100.0
GPG México Wind, B.V.	Netherlands	Holding company	F.C.	100.0	75.0
GPG México, B.V.	Netherlands	Holding company	F.C.	100.0	75.0
Buenergía Gas & Power, Ltd.	Cayman Islands	Holding company	F.C.	95.0	71.3
First Independent Power (Kenya), Ltd. (4)	Kenya	Holding company	F.C.	100.0	75.0
Unión Fenosa México, S.A. de C.V.	Mexico	Holding company	F.C.	100.0	75.0
Distribuidora Eléctrica de Caribe, S.A.	Panama	Holding company	F.C.	100.0	100.0
Generación Eléctrica del Caribe , S.A.	Panama	Holding company	F.C.	100.0	75.0
Unión Fenosa South Africa Coal (Proprietary), Ltd	South Africa	Holding company	F.C.	100.0	100.0
CGE Group:					

Company	Country	Activity	Method of Consolidation (1)	Total % interest % Controlling interest (2)	% Equity interest
Compañía General de Electricidad, S.A.	Chile	Electricity distribution	F.C.	97.2	97.0
Agua Negra S.A.	Argentina	Electricity distribution	F.C.	100.0	97.0
Energía San Juan S.A.	Argentina	Electricity distribution	F.C.	100.0	97.0
Los Andes Huarpes S.A.	Argentina	Electricity distribution	F.C.	98.0	97.0
CGE Argentina S.A.	Chile	Electricity distribution	F.C.	100.0	97.0
CGE Magallanes S.A.	Chile	Electricity distribution	F.C.	99.9	96.9
Empresa de Transmisión Eléctrica Transemel S.A.	Chile	Electricity distribution	F.C.	100.0	94.6
Empresa Eléctrica de Antofagasta S.A.	Chile	Electricity distribution	F.C.	92.7	87.9
Empresa Eléctrica de Arica S.A.	Chile	Electricity distribution	F.C.	94.2	88.6
Empresa Eléctrica de Iquique S.A.	Chile	Electricity distribution	F.C.	88.6	85.9
Empresa Eléctrica de Magallanes S.A.	Chile	Electricity distribution	F.C.	55.2	53.5
Comercial & Logística General S.A.	Chile	Services	F.C.	100.0	97.0
Energy Sur Ingeniería, S.A.	Chile	Services	F.C.	55.0	53.4
Inversiones y Gestión S.A.	Chile	Services	F.C.	100.0	97.0
Novanet S.A.	Chile	Services	F.C.	100.0	97.0
Sociedad de Computación Binaria S.A.	Chile	Services	F.C.	100.0	97.0
Transformadores Tusan S.A.	Chile	Services	F.C.	100.0	97.0
TV Red S.A.	Chile	Services	F.C.	90.0	48.2
CGE Gas Natural, S.A.	Chile	Holding company	F.C.	97.4	92.1
Aprovisionadora Global de Energía, S.A.	Chile	Gas distribution	F.C.	60.2	55.4
Gas Sur S.A.	Chile	Gas distribution	F.C.	100.0	92.1
Innergy Holdings S.A.	Chile	Gas distribution	F.C.	60.0	55.3
Innergy Soluciones Energéticas S.A.	Chile	Gas distribution	F.C.	100.0	55.3
Innergy Transportes S.A.	Chile	Gas distribution	F.C.	100.0	55.3
Metrogas S.A.	Chile	Gas distribution	F.C.	60.2	55.4
Gasoducto del Pacífico (Argentina) S.A.	Argentina	Gas infrastructures	F.C.	56.7	52.2
Gasoducto del Pacífico S.A.	Chile	Gas infrastructures	F.C.	60.0	55.3
Gasoducto del Pacífico (Cayman) Ltd. en liquidación	Cayman Islands	Gas infrastructures	F.C.	56.7	52.2
Centrogas S.A.	Chile	Services	F.C.	100.0	55.4
Empresa Chilena de Gas Natural S.A.	Chile	Services	F.C.	100.0	55.4
Financiamiento Doméstico S.A.	Chile	Services	F.C.	99.9	55.3
GN Holding Argentina Comercializadora, S.A.	Argentina	Holding company	F.C.	100.0	92.1
GN Holding Argentina, S.A.	Chile	Holding company	F.C.	100.0	92.1
Sociedad Inversiones Atlántico S.A.	Chile	Holding company	F.C.	100.0	92.1
CGE Servicios, S.A.	Chile	Services	F.C.	100.0	100.0

(1) Consolidation method: F.C. Full Consolidation, P.C. Proportionate Consolidation, E.M. Equity Method
(2) Parent company's interest in the subsidiary.
(3) The shareholding percentage relating to legally owned shares and to the share buy-back commitment at the percentages stated in Note 18, which are also allocated to the Parent company.
(4) Companies registered as held for sale

2. Joint ventures

Company	Country	Activity	Method of Consolidation (1)	Total % interest % Controlling interest (2)	% Equity interest
Grupo UF Gas:					
Unión Fenosa Gas, S.A.	Spain	Gas marketing	E.M.	50.0	50.0
Segas Services, S.A.E.	Egypt	Gas infrastructures	E.M.	100.0	40.7
Spanish Egyptian Gas Company S.A.E.	Egypt	Gas infrastructures	E.M.	80.0	40.0
Nueva Electricidad del Gas, S.A.U, En Liquidación	Spain	Gas infrastructures	E.M.	100.0	50.0
Unión Fenosa Gas Exploración y Producción, S.A.U.	Spain	Gas infrastructures	E.M.	100.0	50.0
Unión Fenosa Gas Comercializadora, S.A.	Spain	Gas marketing	E.M.	100.0	50.0
Unión Fenosa Gas Infraestructures B.V.	Netherlands	Holding company	E.M.	100.0	50.0
Gas Natural Vehicular del Norte Asociación en Participación (3)	Mexico	Gas distribution	E.M.	51.3	43.6
Eléctrica Conquense, S.A.	Spain	Electricity distribution	E.M.	46.4	46.4
Eléctrica Conquense de Distribución, S.A.	Spain	Electricity distribution	E.M.	100.0	46.4
CH4 Energía S.A. de C.V. (3)	Mexico	Gas marketing	E.M.	50.0	42.5
ENER RENOVA, S.A.	Chile	Electricity generation	E.M.	40.0	40.0
Cogeneración del Noroeste, S.L.	Spain	Electricity generation	E.M.	40.0	40.0
Desarrollo de Energías Renovables de la Rioja, S.A.	Spain	Electricity generation	E.M.	36.3	36.3
Desarrollo de Energías Renovables de Navarra, S.A.	Spain	Electricity generation	E.M.	50.0	50.0
ENER Renova España, S.L.	Spain	Electricity generation	E.M.	40.0	40.0
Energías Eólicas de Fuerteventura, S.L.	Spain	Electricity generation	E.M.	50.0	50.0
Infraestructuras Eléctricas La Mudarra, S.L	Spain	Electricity generation	E.M.	39.6	36.6
Molinos de la Rioja, S.A.	Spain	Electricity generation	E.M.	33.3	33.3
Molinos del Cidacos, S.A.	Spain	Electricity generation	E.M.	50.0	50.0
Montouto 2000, S.A.	Spain	Electricity generation	E.M.	49.0	49.0
Nueva Generadora del Sur, S.A.	Spain	Electricity generation	E.M.	50.0	50.0
P.E. Cinseiro, S.L.	Spain	Electricity generation	E.M.	50.0	50.0
Sociedad Gestora de Parques Eólicos Andalucía, S.A.	Spain	Electricity generation	E.M.	21.0	21.0
Toledo PV, A.E.I.E	Spain	Electricity generation	E.M.	33.3	33.3
Ghesa Ingeniería y Tecnología, S.A.	Spain	Engineering services	E.M.	41.2	41.2
EcoEléctrica Holding, LLC.	Puerto Rico	Holding company	E.M.	50.0	35.6
EcoEléctrica, L.P.	Puerto Rico	Electricity generation	E.M.	100.0	35.6
EcoEléctrica LLC	Puerto Rico	Holding company	E.M.	100.0	35.6
CGE Group:					
Gascart S.A.	Argentina	Gas distribution	E.M.	50.0	46.0
Gasnor S.A.	Argentina	Gas distribution	E.M.	97.4	46.0
Gasmarket S.A.	Argentina	Gas distribution	E.M.	50.0	46.0
Empresa de Distribución Eléctrica de Tucumán S.A.	Argentina	Electricity distribution	E.M.	80.5	48.5
Compañía Eléctrica de Inversiones S.A.	Argentina	Electricity distribution	E.M.	90.0	48.5
Empresa Jujeña de Energía S.A.	Argentina	Electricity distribution	E.M.	90.0	43.7
Empresa Jujeña de Sistemas Energéticos Dispersos S.A.	Argentina	Electricity distribution	E.M.	90.0	43.7
Norelec S.A.	Argentina	Electricity distribution	E.M.	50.0	48.5
Dimater, S.A.	Argentina	Electricity distribution	E.M.	100.0	48.5

Company	Country	Activity	Method of Consolidation (1)	Total % interest % Controlling interest (2)	% Equity interest
Empresa de Construcción y Servicios , S.A.	Argentina	Electricity distribution	E.M.	100.0	48.5
Noanet, S.A.	Argentina	Electricity distribution	E.M.	100.0	48.5
Gasoductos GasAndes, S.A. (Argentina)	Argentina	Gas infrastructures	E.M.	47.0	26.0
Andes Operaciones y Servicios S.A.	Chile	Gas infrastructures	E.M.	50.0	27.7
Gas Natural Producción, S.A.	Chile	Gas infrastructures	E.M.	36.2	33.3
Gasoductos GasAndes, S.A. (Chile)	Chile	Gas infrastructures	E.M.	47.0	26.0
GNL Chile S.A.	Chile	Gas infrastructures	E.M.	33.3	18.5

(1) Consolidation method: F.C. Full Consolidation, P.C. Proportionate Consolidation, E.M. Equity Method
(2) Parent company's interest in the subsidiary.
(3) The shareholding percentage relating to legally owned shares and to the share buy-back commitment at the percentages stated in Note 18, which are also allocated to the Parent company.

3. Jointly-controlled assets and operations

Company	Country	Activity	Method of Consolidation (1)	Total % interest: % Controlling interest (2)	Total % interest: % Equity interest
Cilento Reti Gas, S.R.L. (3)	Italy	Gas distribution	P.C.	60.0	60.0
Bezana / Beguenzo	Spain	Gas infrastructures	P.C.	55.6	55.6
Boquerón	Spain	Gas infrastructures	P.C.	4.5	4.5
Casablanca	Spain	Gas infrastructures	P.C.	9.5	9.5
Chipirón	Spain	Gas infrastructures	P.C.	2.0	2.0
Gas Natural West África, S.L.	Spain	Gas infrastructures	P.C.	40.0	40.0
Montanazo	Spain	Gas infrastructures	P.C.	17.7	17.7
Rodaballo	Spain	Gas infrastructures	P.C.	4.0	4.0
Tánger Larache	Morocco	Gas infrastructures	P.C.	24.0	24.0
Central Térmica de Anllares, A.I.E.	Spain	Electricity generation	P.C.	66.7	66.7
Centrales Nucleares Almaraz-Trillo, A.I.E	Spain	Electricity generation	P.C.	19.1	19.1
Comunidad de bienes Central Nuclear de Almaraz (Grupo I y II)	Spain	Electricity generation	P.C.	11.3	11.3
Comunidad de bienes Central Nuclear de Trillo (Grupo I)	Spain	Electricity generation	P.C.	34.5	34.5
Comunidad de bienes Central Térmica de Aceca	Spain	Electricity generation	P.C.	50.0	50.0
Comunidad de bienes Central Térmica de Anllares	Spain	Electricity generation	P.C.	66.7	66.7
Eólica Tramuntana 21, S.L.	Spain	Electricity generation	P.C.	60.0	60.0
Eólica Tramuntana 22, S.L.	Spain	Electricity generation	P.C.	60.0	60.0
Eólica Tramuntana 23, S.L.	Spain	Electricity generation	P.C.	60.0	60.0
Eólica Tramuntana, S.L.	Spain	Electricity generation	P.C.	60.0	60.0
UTE ESE Clece - Gas Natural	Spain	Services	P.C.	50.0	50.0

(1) Consolidation method: F.C. Full Consolidation, P.C. Proportionate Consolidation, E.M. Equity Method
(2) Parent company’s interest in the subsidiary
(3) Companies registered as held for sale

4. Associates

Company	Country	Activity	Method of Consolidation (1)	Total % interest: % Controlling interest (2)	% Equity interest
Gas Natural Cundiboyacense, S.A. ESP (3)	Colombia	Gas distribution	E.M.	77.5	32.4
Gas Natural del Cesar, S.A. ESP (3)	Colombia	Gas distribution	E.M.	62.2	15.4
Gas Natural del Oriente, S.A. ESP (3)	Colombia	Gas distribution	E.M.	54.5	22.8
Gas Natural, S.A. ESP (3)	Colombia	Gas distribution	E.M.	41.9	41.9
Qalhat LNG S.A.O.C.	Oman	Gas infrastructures	E.M.	7.4	3.7
Sistemas Energéticos La Muela, S.A.	Spain	Electricity generation	E.M.	20.0	20.0
Sistemas Energéticos Mas Garullo, S.A.	Spain	Electricity generation	E.M.	18.0	18.0
Sociedade Galega do Medio Ambiente, S.A.	Spain	Electricity generation	E.M.	49.0	49.0
Bluemobility System, S.L. En Liquidación	Spain	Services	E.M.	20.0	20.0
CER's Commercial Corp	Panama	Services	E.M.	25.0	18.8
Gas Natural Servicios, S.A.S.	Colombia	Services	E.M.	100.0	41.9
Kromschroeder, S.A.	Spain	Services	E.M.	44.5	44.5
Inimo Ingeniería, S.L.	Spain	Services	E.M.	100.0	44.5
Torre Marenostrum, S.L.	Spain	Services	E.M.	45.0	45.0

(1) Consolidation method: F.C. Full Consolidation, P.C. Proportionate Consolidation, E.M. Equity Method
(2) Parent company’s interest in the subsidiary
(3) Companies registered as held for sale

APPENDIX II Variations in consolidation scope

The main consolidation scope changes during 2017 were as follows:

Company name	Operation category	Effective date of operation	Voting rights acquired /eliminated (%)	Voting rights after the operation (%)	Consolidation method after the operation
Línea Trasmisión Cabo Leones, S.A.	Disposal	1 January	50.0	-	-
Proyectos Balmes México, S.A. DE C.V.	Incorporation	1 January	100.0	100.0	Full
Gas Natural Fenosa LNG Singapore PTE. LTD.	Incorporation	1 January	100.0	100.0	Full
Vayu Energy, B.V.	Liquidation	28 February	100.0	-	-
Arte Contemporáneo y Energía, A.I.E.	Liquidation	26 April	100.0	-	-
Lanzagorta y Palmes 2, S.L.	Acquisition	7 June	100.0	100.0	Full
Compañía General de Electricidad, S.A.	Capital increase	1 July	0.3	96.9	Full
Compañía General de Electricidad, S.A.	Amortization own shares	30 November	0.1	97.0	Full
CGE Gas Natural, S.A.	Capital increase	1 July	5.7	91.7	Full
CGE Gas Natural, S.A.	Amortization own shares	11 December	0.4	92.1	Full
Global Power Generation Australia Pty, Ltd.	Acquisition	5 July	1.7	98.7	Full
Parque Eólico Vientos del Pacífico, S.p.A	Acquisition	7 July	100.0	100.0	Full
GPG Solar Chile 2017 SpA	Acquisition	21 August	100.0	100.0	Full
Agua Negra S.A.	Capital increase	25 September	3.1	100.0	Full
Energía San Juan S.A.	Capital increase	25 September	3.1	100.0	Full
Los Andes Huarpes S.A.	Capital increase	25 September	3.5	100.0	Full
El Gritón Solar S.A. de C.V.	Acquisition	26 October	80.0	80.0	Full
Gas Natural Fenosa Renovables Ruralia, S.L.U.	Acquisition	20 November	24.0	75.0	Full
Operación y Mantenimiento Energy Mexico, S.A. de C.V. En Liquidación	Liquidation	6 December	100.0	-	-
Infraestructuras Eléctricas La Mudarra, S.L.	Acquisition	13 December	2.8	36.6	Equity
Castrios, S.A.	Disposal	14 November	33.3	-	-
Inmobiliaria Parque Nuevo S.A.	Liquidation	10 November	50.0	-	-
Gas Natural, S.A. ESP	Disposal	22 December	17.2	41.9	Equity
Inimo Ingeniería, S.L.	Acquisition	27 December	100.0	100.0	Equity

The main changes in the consolidation scope in 2016 were as follows:

Company name	Operation category	Effective date of operation	Voting rights acquired /eliminated (%)	Voting rights after the operation (%)	Consolidation method after the operation
Renovables Aragón, S.L.U	Acquisition	1 March	100.0	100.0	Full
Alas Capital Gas Natural, S.A.	Disposal	11 March	40.0	-	-
Gas Natural Chile, S.A.	Incorporation	30 March	56.6	56.6	Full
Sociedad Inversiones Atlántico, S.A.	Incorporation	31 March	55.1	55.1	Full
Energías Especiales de Extremadura, S.L.	Liquidation	25 April	99.0	-	-
Regasificadora del Noroeste, S.A.	Disposal	28 April	11.6	-	-
Leo-Ras, S.L.	Acquisition	15 May	100.0	100.0	Full
Aprovisionadora Global de Energía, S.A.	Incorporation	1 June	36.9	36.9	Full
Unión Fenosa Financial Services USA, Llc	Liquidation	29 June	100.0	-	-
Union Fenosa Wind Australia Pty, Ltd.	Acquisition	20 July	0.2	96.7	Full
Gas Natural Redes GLP, S.A.	Incorporation	21 July	100.0	100.0	Full
Enervent, S.A.	Disposal	28 July	26.0	-	-
Infraestructuras de Gas, S.A.	Disposal	29 July	85.0	-	
Planta de Regasificación de Sagunto, S.A.	Disposal	31 July	50.0	-	-
Vayu Ltd	Acquisition	2 August	100.0	100.0	Full
Vayu Energy, Ltd	Acquisition	2 August	100.0	100.0	Full
Vayu Energy, Ltd (UK)	Acquisition	2 August	100.0	100.0	Full
Vayu Energy B.V.	Acquisition	2 August	100.0	100.0	Full
LNG GOM Limited	Acquisition	2 August	100.0	100.0	Full
LNG International Resources Ltd	Acquisition	2 August	100.0	100.0	Full
LNG Marketing Ltd	Acquisition	2 August	100.0	100.0	Full
Gas Natural Wind 6, S.L.	Liquidation	2 August	60.0	-	-
Gas Natural Chile, S.A.	Acquisition	8 August	37.9	94.5	Full
Gasco S.A.	Disposal	8 August	55.1	-	-
Gasco GLP S.A.	Disposal	8 August	55.1	-	-
Gasmar S.A.	Disposal	8 August	35.2	-	-
Hualpén Gas S.A.	Disposal	8 August	17.6	-	-
Autogasco S.A.	Disposal	8 August	55.1	-	-
Transportes e Inversiones Magallanes S.A.	Disposal	8 August	46.9	-	-
Automotive Gas Systems S.A.	Disposal	8 August	55.1	-	-
Inversiones Invergas S.A.	Disposal	8 August	55.1	-	-
Inversiones Atlántico S.A.	Disposal	8 August	55.1	-	-
Campanario Generación S.A.	Disposal	8 August	11.0	-	-
Inversiones GLP S.A.S. E.S.P.	Disposal	8 August	38.6	-	-
JGB Inversiones S.A.S. E.S.P.	Disposal	8 August	38.6	-	-
Unigas Colombia S.A. E.S.P.	Disposal	8 August	27.0	-	-
Montagas S.A. E.S.P.	Disposal	8 August	12.9	-	-
Energas S.A. E.S.P.	Disposal	8 August	10.9	-	-
Tecnet, S.A.	Disposal	9 August	100.0	-	-
Infraestructuras Eléctricas La Mudarra, S.L.	Incorporation	31 August	39.6	39.6	Equity
CGE Gas Natural, S.A.	Incorporation	14 October	100.0	100.0	Full
GNL Quintero, S.A.	Disposal	8 November	20.0	-	-
Union Fenosa Wind Australia Pty, Ltd.	Acquisition	15 December	0.2	97.0	Full
Hormigones del Norte, S.A.	Disposal	16 December	100.0	-	-
Sobral i Solar Energía SPE, Ltda	Acquisition	19 December	85.0	85.0	Full
Sertao i Solar Energía SPE, Ltda	Acquisition	19 December	85.0	85.0	Full
Inca de Varas I	Acquisition	20 December	100.0	100.0	Full
Inca de Varas II	Acquisition	20 December	100.0	100.0	Full
Gasifica, S.A.	Liquidation	27 December	100.0	-	-
Gas Galicia SDG, S.A.	Acquisition	29 December	6.9	68.5	Full
Electrificadora del Caribe S.A, E.S.P.	Loss of control	31 December	85.4	-	-
Energía Empresarial de la Costa, S.A., E.S.P.	Loss of control	31 December	85.4	-	-
Energía Social de la Costa S.A. E.S.P.	Loss of control	31 December	85.4	-	-

APPENDIX III Gas Natural tax group companies

The companies belonging to the Gas Natural tax group are as follows:

Gas Natural SDG, S.A.	La Energía, S.A.
Boreas Eólica 2, S.A.	La Propagadora del Gas Latam, S.L.U.
Compañía Española de Industrias Electroquímicas, S.A.	La Propagadora del Gas, S.A.
Energías Ambientales de Somozas, S.A.	Lignitos de Meirama, S.A.
Energías Especiales Alcoholeras, S.A.	Nedgia, S.A.
Europe Mahgreb Pipeline Limited	Nedgia Andalucía, S.A.
Explotaciones Eólicas Sierra de Utrera, S.L.	Nedgia Aragón, S.A.
Fenosa Wind, S.L.	Nedgia Balears, S.A.
Fenosa, S.L.U.	Nedgia Castilla-La Mancha, S.A.
Gas Natural Almacenamientos Andalucía, S.A.	Nedgia Castilla y León, S.A.
Gas Natural Aprovisionamientos SDG, S.A.	Nedgia Catalunya, S.A.
Gas Natural Capital Markets, S.A.	Nedgia Cegas, S.A.
Gas Natural Comercializadora, S.A.	Nedgia Madrid, S.A.
Gas Natural Distribución Latinoamérica, S.A.	Nedgia Navarra, S.A.
Gas Natural Exploración, S.L.	Nedgia Redes Distribución de Gas, S.A.
Gas Natural Fenosa Electricidad Colombia, S.L.	Nedgia Rioja, S.A.
Gas Natural Fenosa Engineering, S.L.	Operación y Mantenimiento Energy, S.A.
Gas Natural Fenosa Generación, S.L.U.	Parque Eólico el Hierro, S.L.
Gas Natural Fenosa Ingeniería y Desarrollo de Generación, S.L.U.	Parque Eólico Montamarta, S.L.
Gas Natural Fenosa Internacional, S.A.	Parque Eólico Nerea, S.L.
Gas Natural Fenosa LNG, S.L.	Parque Eólico Peñarroldana, S.L.
Gas Natural Fenosa Renovables, S.L.U.	Petroleum, Oil & Gas España, S.A.
Gas Natural Informática, S.A.	Sagane, S.A.
Gas Natural Redes GLP, S.A.	Sociedad de Tratamiento Hornillos, S.L.
Gas Natural S.U.R. SDG, S.A.	Sociedad Parque Eólico Mouriños, S.L.U.
Gas Natural Servicios SDG, S.A.	Societat Eòlica de l'Enderrocada, S.A.
Gas Natural Transporte SDG, S.L.	Tratamiento Cinca Medio, S.L.
Gas Natural Wind 4, S.L.U.	Tratamiento de Almazán, S.L.
General de Edificios y Solares, S.L.	Unión Fenosa Distribución, S.A.
Global Power Generation, S.A.	Unión Fenosa Financiación, S.A.
Holding de Negocios de Gas, S.A.U.	Unión Fenosa Minería, S.A.
JGC Cogeneración Daimiel, S.L.	Unión Fenosa Preferentes, S.A.U.

CONSOLIDATED DIRECTORS' REPORT

Consolidated Directors' Report for the year ended 31 December 2017

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1. Highlights and main aggregates

1.1. 2017 Highlights

January to March

- Gas Natural Fenosa issues Euros 1,000 million in notes with a 1.375% annual coupon, maturing in 10 years.
- Continues to be a member of the *FTSE4Good* sustainability index, for the fifteenth consecutive year.
- The company is ranked *Gold Class* in the 2017 *RobecoSam* sustainability index.
- Gas Natural Fenosa earmarks Euros 4.5 million to tackle vulnerability in vulnerable clients.
- Once again, the company is certified as one of Spain's Top Employers based on its employees' work conditions.
- Gas Natural Fenosa issues Euros 1,000 million in notes with a 1.125% annual coupon, maturing in 7 years.

April to June

- Gas Natural Fenosa Renovables will invest Euros 700 million after being awarded 667 MW of wind capacity in an auction held by the Spanish government.
- Gas Natural Fenosa takes part in the European Make Power Clean initiative to foster a cleaner electricity market in Europe.
- The Integrated Control Centre (ICC) for the company's hydroelectric plants is opened in Ourense.

July to September

- Gas Natural Fenosa is granted a Euros 450 million loan from the European Investment Bank (EIB) to finance wind farms and electricity distribution in Spain. It also signs a Euros 200 million loan agreement with Instituto de Crédito Oficial (ICO) to help fund its investment plan through 2020.
- Gas Natural Fenosa signs its first "sustainable loan", for Euros 330 million, with ING.
- The company is awarded 250 MW of photovoltaic capacity in the new renewables auction which will result in Euros 165 million investments.
- Gas Natural Fenosa signs an agreement to sell a non-controlling 20% stake in its gas distribution business in Spain for Euros 1,500 million.
- Gas Natural Fenosa is one of the winners in DuPont's International Safety and Sustainability Awards.
- Gas Natural Fenosa is leader in the gas utilities sector of the Dow Jones Sustainability Index.
- *Actualidad Económica* ranks Gas Natural Fenosa among top five best companies to work for.
- Gas Natural Fenosa, through its subsidiary GPG, launches commercial operations at its first photovoltaic power plant in Brazil (68MW).

October to December

- Gas Natural Fenosa agrees to sell its companies and assets in Italy to 2i Rete Gas and Edison.
- Gas Natural Distribución to become Nedgia in compliance with the principle of unbundling under European Directive 2009/73/EC (gas).
- Gas Natural Fenosa launches its first green bonds in a Euros 800 million issue to finance renewable projects with a 0.875% annual coupon.
- Gas Natural Fenosa agrees to sell its stake in gas distribution in Colombia to Canadian fund Brookfield.
- The company teams up with Norwegian tech firm Connect LNG to develop DirectLink LNG, the world's first floating LNG ship-to-shore transfer system.
- The company is again included in the Euronext Vigeo Europe 120 and Euronext Vigeo Eurozone 120 indices.

Financial performance (Euros million)

Notes to financial information

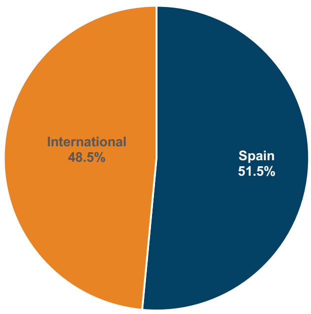
– Gas Natural Fenosa's financial disclosures contain magnitudes and metrics drafted in accordance with International Financial Reporting Standards (IFRS) and others that are based on the Group's disclosure model, referred to as Alternative Performance Metrics (APM), which are viewed as adjusted figures 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 2016 have been re-stated due to the discontinuation of the following operations: gas distribution in Italy and Colombia, electricity distribution in Moldova, gas supply in Italy and electricity generation in Kenya in application of IFRS 5.

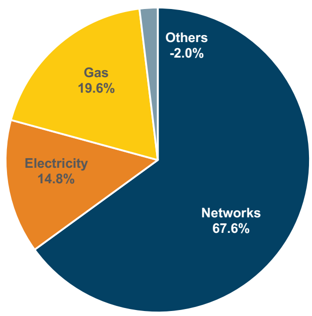
Main financial aggregates

	2017	2016	%
Revenue	23,306	21,908	6.4
EBITDA	3,915	4,664	(16.1)
Income attributable to equity holders of the parent	1,360	1,347	1.0
Net capital expenditure	1,597	2,225	(28.2)
Net borrowings (at 31/12)	15,i22	15,423	(1.7)

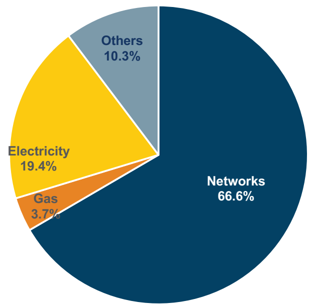
EBITDA by geography in 2017 (%)



EBITDA by business in 2017 (%)



Capital expenditure by business in 2017 (%)



Main financial ratios

	2017	2016
Leverage	45.3%	44.8%
EBITDA/Cost of net financial debt	6.4x	6.3x
Net financial debt/EBITDA	3.9x	3.3x
ROA (return on assets)	2.9%	2.9%

Main stock market ratios and shareholder remuneration

	2017	2016
Average no. of shares ('000) [1]	1,000,478	1,000,468
Share price at 31/12 (Euros)	19.25	17.91
Market capitalisation at 31/12 (Euros million)	19,263	17,922
Earnings per share (Euros)[1]	1.36	1.35
Payout (%)	73.6	74.3
Total dividend [2]	1,001	1,001
Dividend per share	1.00	1.00
Price-earnings ratio (P/E)	14.2	13.3
EV/EBITDA	8.8	7.1

[1] Calculated considering the weighted average number of shares during the year
[2] Based on the total equivalent amount used to pay dividends. In 2017, this included a supplementary dividend amounting to Euros 671 million, pending approval by shareholders at the General Meeting.

1.2. Operational performance

Distribution	2017	2016
Gas distribution (GWh)	460,014	426,510
Electricity distribution (GWh)	53,670	65,586
Gas distribution connections ('000)	10,491	10,224
Electricity connection points ('000)	7,447	7,324
Gas distribution network (km)	116,181	113,083
Length of electricity transmission and distribution network (km)	214,399	215,894

Gas	2017	2016
Gas supply in Spain (GWh)	176,053	178,916
Gas supply in rest of world (GWh)	183,978	146,541
Total gas supply (GWh)	**360,031**	**325,457**

Electricity	2017	2016
Installed capacity in Spain (MW)	12,716	12,716
Installed capacity in rest of world (MW)	2,732	2,590
Total installed capacity (MW)	**15,448**	**15,306**
Net production in Spain (GWh)	27,953	28,504
Net production in rest of world (GWh)	18,436	17,857
Total net production (GWh)	**46,389**	**46,361**

1.3. Environmental and social performance

Environment	2017	2016
Emission factor (t CO2/GWh)	431	411
GHG emissions [1]	20.5	19,5
Emissions-free installed capacity (%)	22.4	22.1
Emissions-free net production (%)	9.7	16.4

Interest in people	2017	2016
No. of employees [2]	15,375	15,502
Training hours per employee	38.4	51.0
Men/women (%)	71/29	71/29

Health and safety	2017	2016
No. of accidents leading to days lost	45	65
Frequency	1.3	1.72

Commitment to society and integrity	2017	2016
Economic value distributed (Euros million)	22,402	21,478
No. of notifications received by the Ethics Committee	141	178

[1] GHG: greenhouse gases, measured as CO_2 equivalent (scope 1).

[2] Does not include the number of employees at discontinued operations (1,396 persons in 2017 and 1,727 persons in 2016)

2. Business model and value creation

2.1. Business model

Gas Natural Fenosa 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.

Gas Natural Fenosa'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	

Gas Natural Fenosa'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:

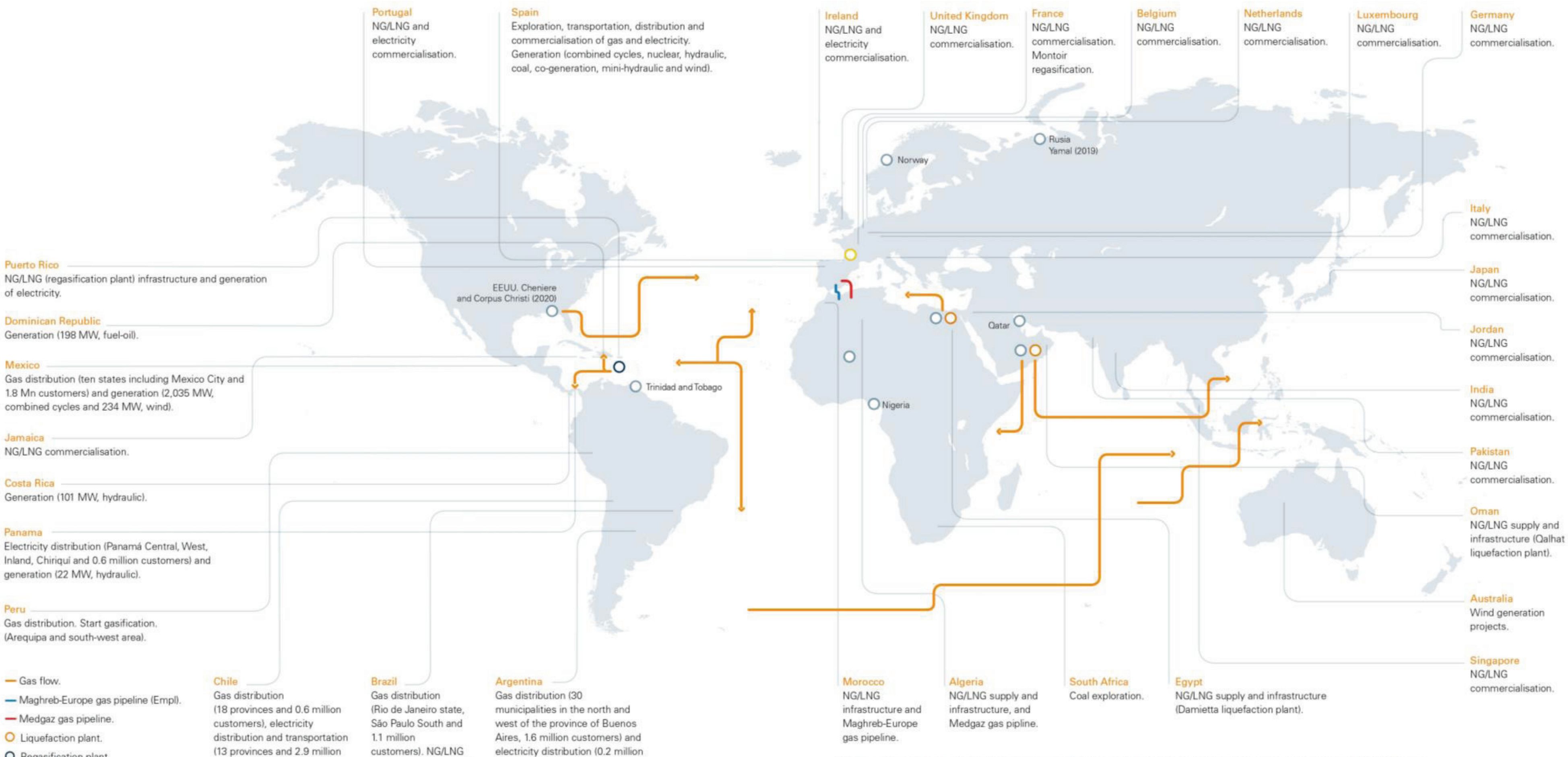
Networks – Gas distribution	41% of EBITDA: Spain and Latin America
Networks – Electricity distribution	26% of EBITDA: Spain and Latin America
Gas	20% of EBITDA: Infrastructure and supply
Electricity	15% of EBITDA: Spain and International

Note: -2% other activities

Gas Natural Fenosa has a differentiated business model, with 85% of EBITDA from regulated or quasi-regulated activities and 49% from international projects.

Throughout the value chain, Gas Natural Fenosa'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.

Worldwide presence



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 and electricity generation in Kenia business because they have been reclassified to discontinued operations.

2.2. Business lines

Leadership in the gas business

	Networks	Gas		
	Gas distribution	**Infrastructures**	**Procurement**	**Supply**
	10.5 million distribution connections 116,181 km of network	Six LNG carriers Two transportation pipelines, Maghreb-Europe (EMPL) and Medgaz	~ 30 bcm supply portfolio	360 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 5.1 million customers. Presence in Argentina, Brazil, Chile, Mexico and Peru and in six of the ten largest Latin American cities.	- Six LNG carriers (0.9 Mm3) - 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 Gas Natural Fenosa a global operator with a strong international profile. Gas Natural Fenosa 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. 40% market share in Spain. Competitive supply to combined cycle plants (CCGT).
Our strength	Gas Natural Fenosa 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.	Gas Natural Fenosa 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.	Gas Natural Fenosa 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. Gas Natural Fenosa 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**
	7.4 million supply connections 214,399 km of network	15.5 GW of power generation capacity	35.2 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 (3.7 million customers).	**Spain** Capacity of 12.8 GW, with a significant presence in five technologies: 7 GW CCGT, 2 GW hydroelectric, 2.1 GW coal, 1.1 GW renewable and 0.6 GW nuclear power. Gas Natural Fenosa has a market share of 17.1% in non-renewable generation and 2.1% in renewable generation. **International** Capacity of 2.7 GW: 2.1 GW CCGT (Mexico), 0.2 GW oil-fired (Dominican Republic), 0.1 GW hydroelectric power (Costa Rica and Panama) and 0.3 GW renewables (Mexico and Brazil).	Leader in the mainstream consumer and residential segments, with a total market share of 14.1% in Spain. One of the main traders in the Spanish market. A dual supply and a broad range of value-added services.
Our strength	Gas Natural Fenosa is a leader in the markets where it operates. Gas Natural Fenosa 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.

2.3. 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.

Gas Natural Fenosa 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.

Our capital	Our commitments	Our results	Our stakeholders
Financial Operating cash flow: Euros 2,923 million Net financial debt: Euros 15,154 million Equity: Euros 18,305 million	Commitment to results	**Financial** Payout: 73.6% Ebitda: Euros 3,915 million Net profit: Euro 1.360 million	Shareholders
Manufacturing Gas and electricity distribution networks Procurement contracts and infrastructure Generating capacity	Service excellence Responsible supply chain	**Manufacturing** Gas distribution:460,014 GWh Electricity distribution: 53,670 GWh Gas supply: 360,031 GWh Net production: 46,389 GWh	Customers
Human Employees and subcontractors Corporate University	Interest in people Health and safety	**Human** Trained workforce (%): 93.7 Voluntary rotation: 2.9 Accident frequency rate: 1.3	Employees
Environmental	Responsible environmental management	**Environmental** Direct GHG emissions: 20.5 CO2 emissions/generation: 431	Society
Social Regulation Relationship with local communities	Social commitment Integrity and transparency	**Social** Economic value distributed: Euros 22,402 million Social investment: Euros 12.9 million	

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.

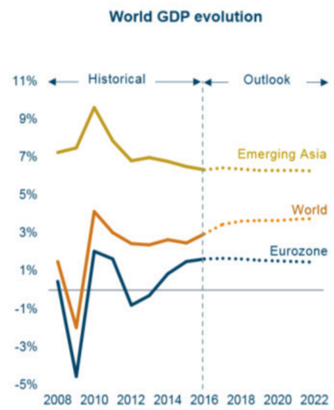
3. Market context, risks and opportunities

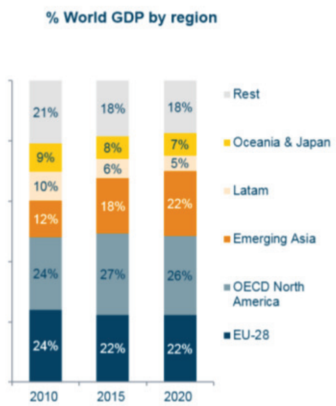
3.1. Market context

3.1.1. Moderate economic growth

Two-speed global economic growth is a reality:

- **Developed economies are slowing down:** The Eurozone is expected to see continued economic recovery. The Spanish economy is gaining traction in a more favourable external context. Although economic growth in Spain is currently above the EU average, it will tend to converge after 2020.
- **Uneven growth in emerging economies:** The epicentre of global economic growth continues to shift towards Asia, although doubts about China have undermined the region's strength somewhat. Latin America has put the deceleration of the last few years behind it, but must now implement changes in its production models to gain competitiveness in relation to Asia and continue to grow. Moreover, some of the larger emerging economies (like Brazil, India and Russia) are growing below their potential due to low commodity prices, the difficulties in accelerating investment in this context.



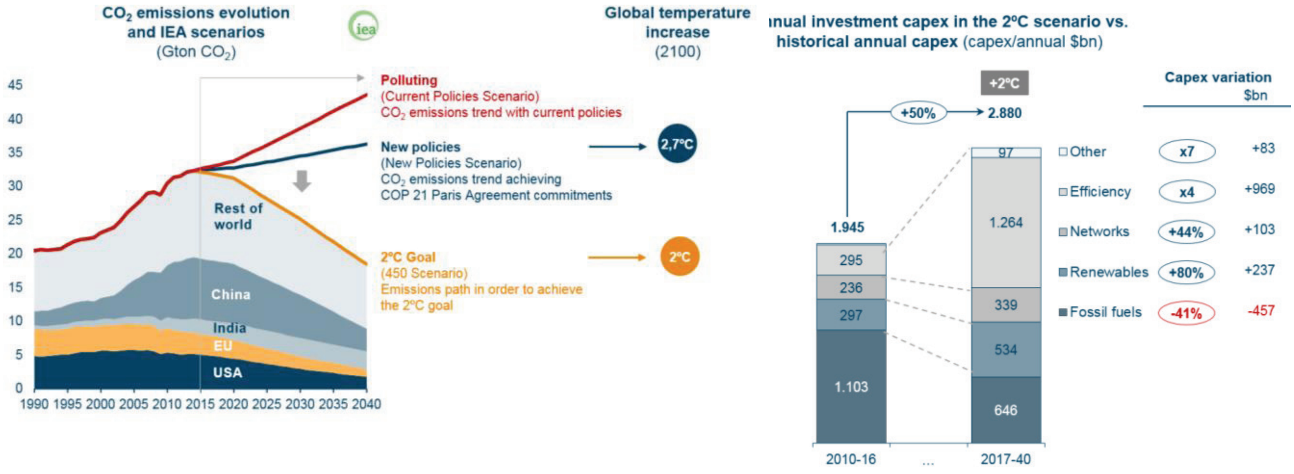


Source: IMF and Caixabank Research

3.1.2. Growth in demand for energy is shaped by environmental policies and the uncertainty about commodity prices

Impact of climate policies on demand

The Paris Agreement (Conference of parties COP '21) seeks to minimise the impact of climate change, implying a reduction in emissions that is only possible if there is a long-term transformation in energy. This energy transformation may be an opportunity, since it will require increased investment, but it would reshape the appeal of businesses and investments alike.



Source: IEA World Energy Outlook 2017

Demand for energy by region

From a regional standpoint, developed countries will see greater decoupling between energy demand and economic performance, while energy growth will centre on developing countries.

Environmental goals and industrial offshoring make developed economies less energy-intensive (flat or decreasing demand for energy).

Growth in energy consumption continues to shift towards developing countries:

- More urbanisation, industrialisation and growth of the middle class all increase per capita energy consumption in those regions.
- Renewable generation is now a competitive alternative without government assistance in many developing economies, limiting the scope for growth in thermal generation in countries where coal predominates.

Future fuel mix

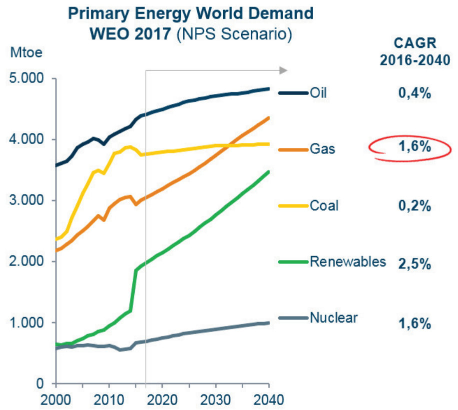
Although there is no single path to achieving climate goals, the most ambitious scenarios represent significant challenges for fossil fuels.

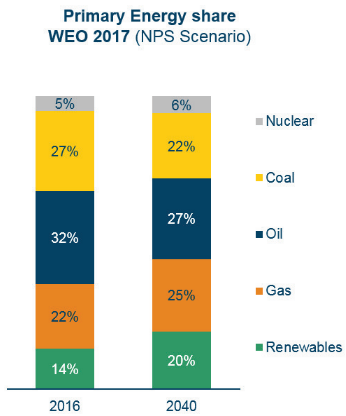
Thanks to the lower investment costs, renewables are consolidating their leadership and will be the fastest-growing primary energy source in the medium and long term.

Natural gas will continue to be the fastest-growing fossil fuel in any of the decarbonisation scenarios, replacing coal in many consumer segments.

Both oil and, in particular, coal, would suffer the most in a transition towards the 2ºC target. However, oil will remain the largest single energy source by volume as there are no clear alternatives for many of its final uses (e.g. transport and petrochemicals).

In final energy consumption, electricity will grow at twice the pace of any other fuel. On the one hand, economic development in emerging countries requires greater use of electricity (motors, cooling systems, information technologies, etc.). And, on the other hand, greater electrification in households and transport, coupled with digitalisation, will contribute to this growth of electricity as a final energy.





Source: IEA World Energy Outlook 2017 (sustainable development scenario)

<u>Energy prices</u>

The end of the commodity supercycle , along with the revolution in shale gas and tight oil, have led to surplus energy production capacity, increasing the uncertainty regarding energy commodity prices:

- increasing the volatility of energy prices
- limiting investment in infrastructure that could trigger price tensions in the future

Furthermore, greater penetration of renewable generation at zero marginal cost will impact prices in wholesale electricity markets. Hence, in the next few years, new market mechanisms will have to be set up to generate price incentives for both new and existing capacity.

3.1.3. Technological advances affect a number of phases of the energy value chain, impacting its business models in some cases.

- Technology applied to hydrocarbon exploration and production (deepwater, horizontal drilling, fracking, etc.) allow vast reserves to be harnessed for production at competitive prices, potentially reactivating demand in some segments and regions.
- Floating storage and regasification units (FSRUs) offer considerable potential for gas, by developing markets very quickly (< 1 year)—these markets being precisely those that have contributed most to growth in demand for LNG in the last few years.
- Lower costs in renewable generation consolidate the latter's position as the main target for new investment in electric power generation worldwide.
- Distributed solar power generation still requires subsidies, but it is an increasingly attractive solution in certain regions, reconfiguring the traditional centralised generation model.
- The development of batteries, as i) a generation asset, ii) network backup or iii) storage at the point of consumption are, for now, a technology in the pilot phase which is set to be further developed in the next few years.
- The development of electric vehicles requires subsidies for introduction on a mass scale, but the reduction in costs and emissions caps in some cities may trigger widespread penetration in less than a decade, boosting electricity consumption and changing the electricity load curve.
- Digitalisation in the energy sector, such as the development of applications and services that transform the relationship with customers due to greater connectivity, will enable demand management to be optimised (smart devices) and the portfolio of products and services to be expanded.

3.2. Risks

3.2.1.Risk management model

Gas Natural Fenosa'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.

Gas Natural Fenosa 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.

Corporate governance

Preventive risk management, which includes issues beyond the mere economic sphere of the company's activities, is a core feature of Gas Natural Fenosa's corporate governance. Within the framework of its risk management and control policy, the company analyses and approves its risk profile each year and establishes the necessary measures to mitigate risks. Additionally, Audit Committee monitors the operation of risk management and control systems.

Risk management

Gas Natural Fenosa constantly analyses its overall risk profile by identifying, characterising and measuring the risks with the greatest potential impact on the company's financial statements. In this way, it determines the maximum accepted level of risk exposure and the admissible limits. These limits are assigned to each risk category as well as in overall terms; the result is the target overall risk profile.

Internal audit and Compliance

The Internal Audit units are responsible for performing the assurance and control function. To this end, the Internal Audit function has a risk-based approach, which provides independent assurance not linked to management about the effectiveness of the internal control system and of risk measurement and management in all areas of the group.

Risk management bodies

Guaranteeing the predictability and sustainability of the company's operational and financial performance is a key aspects of risk management at Gas Natural Fenosa, 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.

Risk Committee

Entrusted with determining and reviewing the company's target risk profile. It also exercises oversight to ensure that the entire organisation understands and accepts its responsibility for identifying, assessing and managing the main risks.

Risk 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.

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.

Other corporate areas

In charge of tracking and managing certain risks which are specific in nature or need to be managed in a specific way. Notable examples are the Environment and Quality Assurance Unit, which handles environmental and climate change risk, and the Reputation and Sustainability Unit, which manages reputational risk. Both operate in coordination with the Risk Units.

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, procurement costs or 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 in the company and in improving management of exposure, all of which have an essential impact on the reinsurance market's perception of Gas Natural Fenosa's operational excellence.

3.2.2. Main risks

Risk type		Description	Management	Metric	Trend
Market risks					
Commodity prices	Gas	Volatility in the international markets that determine 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.
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 rates		Volatility in funding rates.	Financial hedges. Diversification of funding sources.	Stochastic	↓ Increase financial strength in a context of agile deleveraging.
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	←→ Spain is expected to recover slowly, in line with the process of macroeconomic normalisation.
Operational risks					
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.
Volume	of gas	Mismatch between gas supply and demand.	Optimisation of contracts and assets worldwide.	Stochastic	←→ Temporarily slack demand in Spain.
	of electricity	Reduction of the available thermal gap. Uncertainty about volume of hydroelectric output.	Optimisation of the balance between supply and generation.	Stochastic	↑ Slack demand in Spain, impacting the thermal gap due to renewables' growing share.
Operational: insurable risks		Accidents, damage and non-availability of Gas Natural Fenosa assets.	Continuous improvement plans. Optimisation of total cost of risk and of hedges.	Stochastic	↓ Development of specific oversight units.
Operational: image and reputation		Impaired perception of Gas Natural Fenosa by stakeholders.	Identification and tracking of potential reputational events. Transparency.	Scenarios.	←→ Stabilisation of RepTrak index score.
Operational: environment		Harm to the natural and/or social environment. Development of 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.	Scenarios/ Stochastic.	↑ Uncertainty about policy developments to encourage energy efficiency.

Risk type	Description	Management	Metric	Trend
Operational: geopolitical exposure	Company-owned assets or supply contracts in geographical areas whose political equilibrium is delicate.	Diversification by country and region. Specific insurance policies.	Scenarios/ Stochastic.	⇄ Stagnation of the situation in the Middle East/North Africa.

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 price, credit and liquidity risk) are detailed in Note 17 to the Consolidated Annual Accounts.

3.3. Opportunities

Gas Natural Fenosa's main opportunities are as follows:

- **Generation mix:** Gas Natural Fenosa'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. Specifically, because of its LNG carrier fleet, Gas Natural Fenosa is one of the world's leading LNG operators and a key player in the Atlantic and Mediterranean.

- **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.

- **International generation**: Increase the renewable energy generating capacity at an international level given the cost-competitiveness of renewable energies and Gas Natural Fenosa's presence in growth markets.

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

4. Corporate governance

Attached as an annex and forming an integral part of this Directors' Report is the Annual Report on Corporate Governance 2017, as required by article 526 of the Capital Companies Act.

4.1. Corporate Governance Model

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

The corporate governance terms of reference mainly comprise:

- Articles of Association (updated in 2017)
- Regulations of the Board of Directors and its committees (updated in 2016)
- Regulations of the General Meeting of Shareholders (updated in 2015)
- Internal Code of Conduct in connection with the Securities Markets
- Human Rights Policy
- Code of Ethics (updated in 2015)

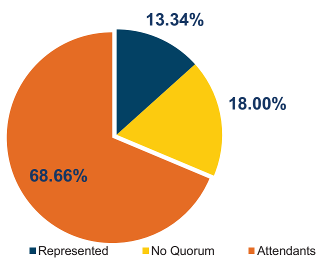
On 21 September 2016, the shareholders of Gas Natural Fenosa, Criteria Caixa, S.A.U. (Criteria) and Repsol, S.A. (Repsol) announced the sale to GIP III Canary 1 S.à.r.l. (GIP) of 20 % (10% each by Criteria and Repsol) of Gas Natural SDG, S.A., as established in the sale agreement signed on 12 September 2016. As a result of that sale in 2016, the composition of Gas Natural Fenosa's Board of Directors and committees was modified and a condition was introduced into the Regulation of the Board of Directors that a majority of two-thirds of directors would be required to approve certain reserved matters. During 2017 the General Meeting approved by co-optation the following Directors:

- Mr.D. Alejandro García-Bragado (Proprietary Criteria)
- Mr. Marcelino Armenter (Proprietary Criteria)
- Mr. William Woodburn (Proprietary GIP)
- Mr. Rajaram Rao (Proprietary GIP)
- Mr. Mario Armero (Proprietary GIP)
- Ms. Helena Herrero (Independent)

4.2. Shareholders' Meeting

Shareholders who, either individually or collectively with others, hold 100 shares may attend the meeting provided that they are shareholders of record at least five days in advance.

Attendance at the 2017 Shareholders' Meeting (%): 82,00%



4.3. Board of Directors

Gas Natural Fenosa structures the functioning of its highest management body, the Board of Directors, a through its functioning in Plenary and in Commissions, in response to the requirements of the Capital Companies Law. Therefore, the Board of Directors of Gas Natural Fenosa has an Audit Committee and the Appointments and Remuneration Committee, which exercise the functions entrusted to them by the Law.

Additionally, the Board of Directors has an Executive Comitee, which deals with resolving the most operational matters over which the Board has competence.

During 2017, the Board of Directors debated, took cognizance and made decisions about the following matters, among others, within the scope of its powers:

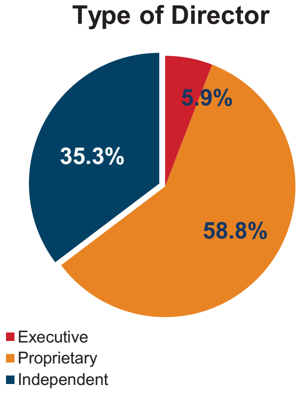
- Monthly, half-year and annual monitoring and supervision of business development.
- Approval of accounts and other actions required by accounting regulations and/or stock market.
- Strategic discussion aimed at preparing the new Strategic Plan 2018-2020.
- Budget, financing plan, investment plan and other actions in terms of activity programming and financial discipline.
- Efficiency plan.
- Company's registered offices transfer.
- Examination of the main risks of the Company and its control systems.
- Corporate operations, among which are the divestments made in Italy, Colombia and in the gas distribution business in Spain.
- Actions in matters of corporate governance: in addition to the usual (Annual Corporate Governance Report, Annual Remuneration Report, etc), this year there has been external advice in the process of evaluating the functioning of the Board of Directors and its Committees, in accordance with the best corporate governance practices.
- General Meeting, including proposal for appointment of new directors and proposal for dividend distribution.
- Social Corporate Responsability.

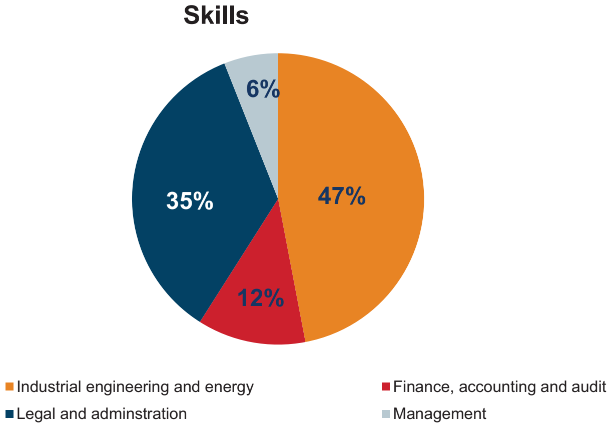
Composition of the Board of Directors and its committees (at 31 December 2017)

Board of Directors		Executive Committee	Audit Committee	Appointments and Remuneration Committee	Category of director	Seniority on Board
Chairman	Mr. Isidro Fainé Casas	Chairman			Proprietary	18/05/2015
First Deputy Chairman	Mr. Josu Jon Imaz San Miguel	Board member			Proprietary	21/09/2016
Second Deputy Chairman	Mr. William Alan Woodburn	Board member		Board member	Proprietary	30/09/2016
Managing Director	Mr. Rafael Villaseca Marco	Board member			Executive Director	28/01/2005
Director	Mr. Ramón Adell Ramón	Board member	Chairman		Independent	18/06/2010
Director	Mr. Enrique Alcántara-García Irazoqui		Board member		Proprietary	27/06/1991
Director	Mr. Xabier Añoveros Trías de Bes		Board member		Independent	20/04/2012
Director	Mr. Marcelino Armenter Vidal	Board member			Proprietary	21/09/2016
Director	Mr. Mario Armero Montes				Proprietary	21/09/2016
Director	Mr. Francisco Belil Creixell	Board member		Chairman	Independent	14/05/2015
Director	Ms. Benita María Ferrero-Waldner	Board member			Independent	14/05/2015
Director	Mr. Alejandro García-Bragado Dalmau			Board member	Proprietary	21/09/2016
Director	Ms. Cristina Garmendia Mendizábal		Board member	Board member	Independent	14/05/2015
Director	Ms. Helena Herrero Starkie		Board member		Independent	04/05/2016
Director	Mr. Miguel Martínez San Martín	Board member		Board member	Proprietary	14/05/2015
Director	Mr. Rajaram Rao	Board member	Board member		Proprietary	21/09/2016
Director	Mr. Luis Suárez de Lezo Mantilla		Board member		Proprietary	26/02/2010
Non-director Secretary	Mr. Manuel García Cobaleda	Non-director Secretary	Non-director Secretary	Non-director Secretary	N/A	29/10/2010

There were no director removals or appointments in 2017.

Board of Directors profile (%)





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
2017	15	3	10	5
2016	15	6	7	8

4.4. Management Committee

In terms of management structure dependent on the Managing Director there is a Management Committee composed of:

Mr. Rafael Villaseca Marco: Managing Director
Mr. Carlos J. Álvarez Fernández: Chief Financial Officer
Mr. Sergio Aranda Moreno: General Manager – Latin America
Mr. Antonio Basolas Tena: General Manager - Strategy and Development
Mr. José Mª Egea Krauel: General Manager - Energy Planning
Mr. Manuel Fernández Álvarez: General Manager - Wholesale Energy Business
Mr. Antonio Gallart Gabás: Chairman of Compañía General de Electricidad, S.A.
Mr. Manuel García Cobaleda: General Counsel and Secretary of the Board of Directors
Mr. Jordi García Tabernero: General Manager - Communication and Institutional Relations
Mr. Daniel López Jordà: General Manager - Retail Energy Business
Mr. Antoni Peris Mingot: General Manager - Regulated Business
Ms. Rosa María Sanz García: General Manager - People and Resources

4.5. 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 2017.

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.

Based on a favourable report from the Appointments and Remuneration Committee, the Board of Directors resolved to maintain in 2017, without any changes, the remuneration for membership of the Board of Directors and Executive Committee (in force since 2007) and for membership of the Appointments and Remuneration Committee and the Audit Committee (in force since 2015).

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

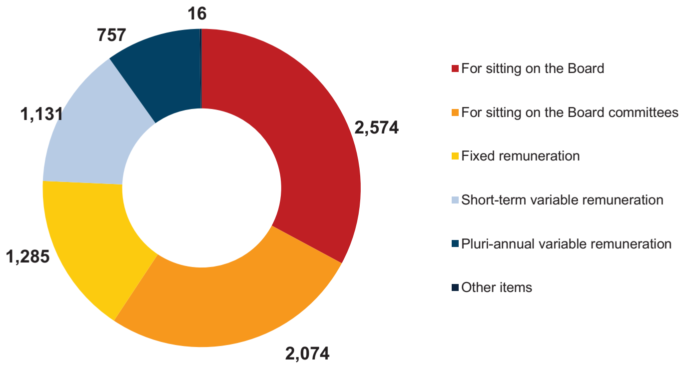
Chairman of the Board of Directors	550.000
Director	126.500
Chairman of the Executive Committee	550.000
Member of the Executive Committee	126.500
Member of the Appointments and Remuneration Committee	25.000
Member of the Audit Committee	40.000

The CEO's remuneration for his executive functions is based on the following:

Item	Objective	Criteria
Fixed remuneration	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.	Calculated on the basis of attainment of the objectives for the year: economic (EBITDA, net profit, working capital/revenues), efficiency (achievement of synergies), business growth (net increase in no. of gas connection points and sales of LNG in other countries) and quality, security and safety (accident rate, environmental ratios and customer satisfaction).
Multi-year variable remuneration	Strengthen the commitment to achieving the goals set out in the strategic plans.	It is calculated by applying the degree of attainment of the economic goals related to optimisation and financial discipline (EBITDA, net debt/EBITDA, market capitalisation and enterprise value/EBITDA), each weighted 25%. The 2015-2017, 2016-2018 and 2017-2019 remuneration programmes are currently in force.
Other items	Safeguard the company's benefits.	Health and life insurance. Energy rebate.

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

Total remuneration earned by the Board of Directors in 2017, by type (Euros thousand)

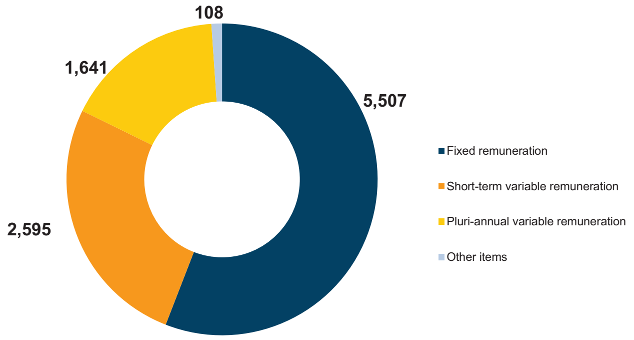


Management Committee

The general remuneration policy for members of the Management Committee is determined 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 CEO's executive functions, although it has specific individual objectives in addition to the group objectives.

Total remuneration earned by the Management Committee and head of Internal Audit[1] in 2017, by type (Euros thousand)



[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.

5. Profit of the year

5.1. Commitment to results

What resources are relevant to this commitment?
Financial
Human
Social

How do we measure our performance?
EBITDA
Net profit
Investments
Indebtedness
Pay-out

What this means for Gas Natural Fenosa

In a challenging environment, Gas Natural Fenosa' acts with the goal to maintain a solid financial and business profile. Gas Natural Fenosa'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 Gas Natural Fenosa.

5.1.1. Analysis of consolidated results

Net sales

	2017	% s/total	2016	% s/total	% 2017/2016
Gas distribution	5,005	21.5	4,000	18.3	25.1
Spain	1,270	5.4	1,198	5.5	6.0
Latin America	3,735	16.1	2,802	12.8	33.3
Electricity Distribution	4,166	17.9	5,506	25.1	(24.3)
Spain	861	3.7	833	3.8	3.4
Latin America	3,305	14.2	4,673	21.3	(29.3)
Gas	10,451	44.8	8,943	40.8	16.9
Infrastructure	317	1.4	324	1.5	(2.2)
Supply	10,134	43.4	8,619	39.3	17.6
Electricity	6,265	26.9	6,017	27.5	4.1
Spain	5,375	23.1	5,279	24.1	1.8
International	890	3.8	738	3.4	20.6
Rest	437	1.9	364	1.7	20.1
Consolidation adjustments	(3,018)	(13.0)	(2,922)	(13.4)	3.3
Total	**23,306**	**100.0**	**21,908**	**100.0**	**6.4**

Net sales totalled Euros 23,306 million in 2017, a 6.4% increase with respect to 2016, due basically to higher volumes and sale prices in the gas business compared with the previous year, to higher pool prices (offset by lower electricity sale volumes), and to the currency effect.

EBITDA

	2017	**% s/total**	**2016**	**% s/total**	**% 2017/2016**
Gas distribution	1,614	41.2	1,506	32.3	7.2
Spain	906	23.1	889	19.1	1.9
Latin America	708	18.1	617	13.2	14.7
Electricity Distribution	1,032	26.4	1,292	27.7	(20.1)
Spain	598	15.3	603	12.9	(0.8)
Latin America	434	11.1	689	14.8	(37.0)
Gas	766	19.6	824	17.7	(7.0)
Infrastructure	296	7.6	300	6.4	(1.3)
Supply	470	12.0	524	11.3	(10.3)
Electricity	578	14.8	954	20.4	(39.4)
Spain	302	7.8	715	15.3	(57.8)
International	276	7.0	239	5.1	15.5
Rest	(75)	(2.0)	88	1.9	(185.2)
Total	**3,915**	**100.0**	**4,664**	**100.0**	**(16.1)**

Consolidated EBITDA declined by Euros 749 million (16.1%) in 2017 to Euros 3,915 million, after restatement to reflect cessation of the gas distribution business in Italy and Colombia, the electricity distribution business in Moldova, the gas supply business in Italy and the electricity generation business in Kenya. Nevertheless, the 2017 figures do not include the figures for Electricaribe, and they do include a one-time Euros 110 million increase in personnel expenses basically because of launching the new 2018-2020 efficiency plan; consequently, in like-for-like terms, the reduction was just 8.8%.

Foreign currency fluctuations in consolidation had a negative impact on EBITDA in 2017 amounting to Euros 15 million with respect to 2016, mainly due to depreciation of the US dollar, Argentinian peso and Mexican peso.

EBITDA from Gas Natural Fenosa's international activities declined by 4.8% to account for 48.5% of the consolidated total, compared with 42.8% last year. EBITDA from operations in Spain fell by 24.5% and declined as a share of the consolidated total to 51.5%.

In other activities in 2016, the company recognised a Euros 51 million gross capital gain (Euros 35 million net of taxes) for the sale of four buildings in Madrid for the amount of Euros 206 million while in 2017 only capital gain have been recorded for 23 million euros.

Operating income

	2017	% s/total	2016	% s/total	% 2017/2016
Gas distribution	1,122	53.2	1,048	37.9	7.1
Spain	599	28.4	596	21.5	0.5
Latin America	523	24.8	452	16.4	15.7
Electricity Distribution	611	28.9	693	25.1	(11.8)
Spain	365	17.3	381	13.8	(4.2)
Latin America	246	11.6	312	11.3	(21.2)
Gas	596	28.2	670	24.2	(11.0)
Infrastructure	243	11.5	242	8.8	0.4
Supply	353	16.7	428	15.4	(17.5)
Electricity	(16)	(0.8)	269	9.8	(105.9)
Spain	(171)	(8.1)	154	5.6	(211.0)
International	155	7.3	115	4.2	34.8
Rest	(201)	(9.5)	84	3.0	(339.3)
Total	**2,112**	**100.0**	**2,764**	**100.0**	**(23.6)**

Depreciation and amortisation charges and impairment losses in 2017 amounted to Euros 1,648 million, a 3.5% decrease year-on-year, mainly due to extending the useful lives of the combined cycle plants from 25 to 35 years.

Provisions for bad debts amounted to Euros 155 million, compared with Euros 315 million the previous year; this reduction is due basically to deconsolidating Electricaribe.

Operating profit declined by Euros 652 million (-23.6%) in 2017 to Euros 2,112 million, after restatement to reflect cessation of the gas distribution business in Italy and Colombia, the electricity distribution business in Moldova, the gas supply business in Italy and the electricity generation business in Kenya (-19.3% in like-for-like terms, excluding Electricaribe and the cost of the efficiency plan).

As a result of natural disasters (forest fires, and wind and snow storms) in Chile and Moldova, the effects of hurricane Maria in Puerto Rico and the earthquake in Mexico, Euros 20 million were recognised for the loss of earnings, an amount of Euros 25 million was recognised under "Other operating expenses" for the expenses and indemnities incurred as a result of those disasters, and an amount of Euros 8 million under "Depreciation, amortisation and impairment expenses" for the impairment of property, plant and equipment that were affected.

Financial result

The financial result amounted to Euros -699 million in 2017, 14.2% less than the 2016 figure (Euros -815 million).

The breakdown of the financial result is as follows:

	2017	2016	%
Cost of net interest-bearing debt	(611)	(735)	(16,9)
Other financial expenses/revenues	(103)	(96)	7,3
Financial income- Costa Rica[1]	15	16	6,2
Financial result	**(699)**	**(815)**	**(14,2)**

[1] The Costa Rica generation concessions are accounted for as finance leases in accordance with IFRIC 12.

The cost of net interest-bearing debt in 2017 was Euros 611 million, i.e. lower than in 2016 due to deconsolidating Electricaribe and to the lower coupons on new debt issued to refinance maturing debt, call bonds or restructure bank loans.

The average cost of gross financial debt was 3.5%, and 79% of the debt is at fixed rates.

Income from discontinued operations

In 2017, income from discontinued operations amounted to Euros 460 million (Euros 193 million in 2016), corresponding to the gas distribution business in Italy (Euros 30 million) and Colombia (Euros 430 million), the electricity distribution business in Moldova (Euros 12 million), the gas supply business in Italy (Euros 7 million) and the electricity generation business in Kenya (Euros -19 million). Additionally, the figures for 2016 included the net profit of the LPG business in Chile (Euros 44 million) up to its disposal in August 2016. Income from discontinued operations attributable to the controlling company amounted to Euros 428 million in 2017 (Euros 132 million in 2016).

Gas distribution in Italy

The Italian gas distribution business contributed Euros 30 million in net profit in 2017 (Euros 25 million in 2016).

The main aggregates of the regulated gas business in Italy are as follows:

	2017	2016	%
Gsa sales - TPA (GWh)	3,950	3,578	10.4
Distribution network (km)	7,327	7,265	0.9
Connection points (‘000) (at 31/12)	461	460	0.2

A total of 3,950 GWh of gas were distributed, a 10.4% increase with respect to 2016, due to favourable weather conditions.

The distribution grid stood at 7,327 km at 31 December 2017, having expanded by 20 km in the last three months.

Gas Natural Fenosa has 460,665 gas distribution connection points in Italy, a slight increase with respect to the previous year.

Gas distribution in Colombia

The Colombian gas distribution business contributed Euros 430 million in net profit in 2017 (Euros 87 million in 2016). Income attributable to the controlling company amounted to Euros 393 million in 2017 (Euros 48 million in 2016), including Euros 350 million in capital gains on the disposal.

The main aggregates of the gas distribution business in Colombia are as follows:

	2017	2016	%
Gas sales - TPA (GWh)	27,082	28,177	-3.9
Distribution network (km)	22,344	21,839	2.3
Connection points (‘000) (at 31/12)	2,976	2,862	4.0

Gas and TPA sales declined by 3.9% year-on-year, due to the atypical sales volume in the secondary market (in which surplus gas remaining after covering generic demand from the customer portfolio is sold) in the early months of 2016 and to the low volume registered in 2017.

Residential-commercial customer numbers increased by 114,084 net in 2017, which represented a 3.2% decrease year-on-year, basically as a result of the new building segment, where the market contracted due to a deceleration in the sale of completed buildings.

Electricity distribution in Moldova

The electricity distribution business in Moldova contributed Euros 12 million in net profit in 2017 (Euros 30 million in 2016).

The main aggregates of the electricity distribution business in Moldova are as follows:

	2017	2016	%
Electricity sales - TPA (GWh)	2,702	2,672	1.1
Connection points ('000) (at 31/12)	889	878	1.3

Gas supply in Italy

The Italian gas supply business contributed Euros 7 million in net profit in 2017 (Euros 6 million in 2016).

The main aggregates in the gas supply business are as follows:

	2017	2016	%
Gas supply in Italy (GWh)	10,631	9,853	7.9
Wholesale	7,309	6,819	7.2
Residential	3,322	3,034	9.5

Electricity generation in Kenya

The electricity generation business in Kenya contributed a net loss of Euros -19 million in 2017 (vs. a profit of Euros 1 million in 2016), including a Euros 24 million impairment of the investment to fair value less costs to sell. Income attributable to the controlling company amounted to Euros -14 million (Euros 1 million in 2016).

The main aggregates of the electricity generation business in Kenya are as follows:

	2017	2016	%
Electricity generated (GWh)	267	191	39.8
Installed capacity (MW)	106	112	-5.4
Availability factor (%)	95.3	95.8	-0.5 p.p.

Equity-accounted affiliates

Equity-accounted affiliates contributed Euros 14 million in earnings in 2017 (Euros -98 million in 2016) due to the positive contribution by Ecoeléctrica in Puerto Rico and by other holdings (Chile and renewables), which was partly offset by the negative result contributed by the Union Fenosa Gas subgroup. In 2016, the holding in Union Fenosa Gas was impaired by Euros 94 million.

Income tax

The effective tax rate in 2017 was 13.3%, compared with 18.0% in 2016.

On 30 November 2017, following the process of business reorganisation and structure simplification in Chile, subsidiaries CGE Distribución, S.A., Compañía Nacional de Fuerza Eléctrica, S.A. and Empresa

Eléctrica Atacama, S.A. were merged into their parent company, Compañía General de Electricidad, S.A. The resulting goodwill was allocated to the tax value of the non-monetary assets received from the merged company (power transmission networks), which is equivalent to the carrying amount on the transaction date, resulting in a reduction of Euros 117 million in deferred tax liabilities and a contra-item under "Income tax" in the consolidated income statement.

In 2016, subsidiary Transnet was merged into its parent company, Compañía General de Electricidad, S.A., resulting in a Euros 128 million reduction in deferred tax liabilities with a contra-item under "Income tax" in the consolidated income statement. This was offset by the impact of the tax reform in Colombia, which resulted in a Euros 21 million increase in expenses under "Income tax" in the consolidated income statement.

But for these one-time impacts, the effective tax rate as of 31 December 2017 would have been 21.5% (23.8% in 2016).

Non-controlling interest

The main items in this account are the non-controlling interests in EMPL, international electricity (GPG), the gas distribution companies in Chile, Brazil and Mexico, and the electricity distribution companies in Chile and Panama, as well as accrued interest on perpetual subordinated notes.

Profit attributed to non-controlling interests amounted to Euros 337 million in 2017, i.e. 7.4% less than the previous year's figure of Euros 364 million.

Net profit

Net income in 2017 amounted to Euros 1,360 million, a 1.0% increase with respect to 2016.

5.1.2. Consolidated balance sheet

Investments

The breakdown of net investments by type is as follows:

	2017	2016	%
Capital expenditure and intangible assets	1,782	2,517	(29.2)
Financial investments	44	384	(88.5)
Total gross investments	**1,826**	**2,901**	**(37.1)**
Disposals and others	-229	-676	(66.1)
Total net investments	**1,597**	**2,225**	**(28.2)**

Investments in property, plant and equipment and intangible assets amounted to Euros 1,782 million in 2017, a 29.2% decrease with respect to 2016, due to recognition in 2016 of Euros 425 million for the acquisition of two new gas carriers under finance lease and the acquisition of new LPG connection points for Euros 426 million.

The breakdown of investments in property, plant and equipment and intangible assets is as follows:

	2017	% 2017	2016	% 2016	% 2017/2016
Gas distribution	584	32.8	968	38.5	(39.7)
Spain	212	11.9	693	27.6	(69.4)
Latin America	372	20.9	275	10.9	35.3
Electricity Distribution	602	33.8	653	25.9	(7.8)
Spain	252	14.1	265	10.5	(4.9)
Latin America	350	19.7	388	15.4	(9.8)
Gas	66	3.7	471	18.7	-
Infrastructure	18	1.0	13	0.5	38.5
Supply	48	2.7	458	18.2	-
Electricity	346	19.4	189	7.5	83.1
Spain	178	10.0	105	4.2	69.5
International	168	9.4	84	3.3	100.0
Rest	184	10.3	236	9.4	(22.0)
Total	**1,782**	**100.0**	**2,517**	**100.0**	**(29.2)**

The electricity distribution business accounts for 33.8% of total consolidated capital expenditure, having registered a 7.8% decrease with respect to 2016. The electricity distribution business in Latin America accounted for 19.7% of total consolidated capital expenditure, having declined by 9.8%.

Gas distribution represents 32.8% of total consolidated capital expenditure, having declined by 39.7% with respect to 2016 because of the 69.4% reduction in investment in Spain, which in 2016 included part of the investment to acquire new LPG connection points. This decrease offset the 35.3% increase in the gas distribution business in Latin America, which accounted for 20.9% of the consolidated total, while capital expenditure (both maintenance and growth) increased in all countries.

Capital expenditure outside Spain increased by 13.9% to account for 54.0% of the total (vs. 33.6% in 2016).

Investment in Spain declined by 50.9%, and its share declined to 46.0% of the total, compared with 66.4% in 2016, due to the acquisition in September 2016 of a gas carrier under a finance lease.

Excluding that effect, capital expenditure in Spain would have amounted to 60.0% of the total in 2016.

Equity and shareholder remuneration

At 31 December 2017, Gas Natural Fenosa's shareholders' equity totalled Euros 18,305 million. Of that total, Euros 14,734 million is attributable to Gas Natural Fenosa.

At 31 December 2017, the total number of ordinary shares was 1,000,689,341, represented by book entries, with a par value of one euro each. All of the outstanding shares are fully paid-up and have the same political and economic rights.

At 31 December 2017, based on publicly available information, the main shareholders of Gas Natural Fenosa were as follows:

	Interest in share capital %
Fundación Bancaria Caixa d'Estalvis i Pensions de Barcelona,“la Caixa” (1)	24.4
Repsol, S.A.	20.1
Global Infrastructure Partners III (2)	20.0
Sonatrach	4.0

(1) Through Criteria Caixa S.A.U.

(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.

The distribution of 2016 income proposed to the Shareholders' Meeting on 20 April 2017 entailed allocating Euros 1,001 million to dividends, the same amount as in 2016. That represents a dividend of Euros 1 per share and a pay-out of 74.3%, i.e. a dividend yield of 5.6% based on the share price on 31 December 2016 (Euros 17.91).

The distribution of 2017 income that the Board of Directors will propose to the Shareholders' Meeting for approval entails allocating Euros 1,001 million to dividends, the same amount as in the previous year. That represents a dividend of Euros 1 per share and a pay-out of 73.6%, i.e. a dividend yield of 5.2% based on the share price on 31 December 2017 (Euros 19.25).

The interim dividend for 2017, amounting to Euros 0.330 per share, was paid entirely in cash on 27 September 2017.

For additional information, see Note 13 to the Consolidated Financial Statements.

Debt and finances

Net interest-bearing debt (Euros million)

	31.12.17	31.12.16	%
Net interest-bearing debt	15,154	15,423	(1.7)

As of 31 December 2017, net interest-bearing debt amounted to Euros 15,154 million and leverage stood at 45.3% (Euros 15,423 million and 44.8%, respectively, as of 31 December 2016).

The net debt/EBITDA ratio was 3.9 and EBITDA/cost of net interest-bearing debt was 6.4 at 31 December 2017.

Net interest-bearing debt is calculated as follows:

	31.12.17	31.12.16
Non-current financial liabilities	15,916	15,003
Current financial liabilities	2,543	2,599
Cash and cash equivalents	(3,225)	(2,067)
Derivatives	(80)	(112)
Net interest-bearing debt	**15,154**	**15,423**

Maturity of net debt (Euros million)

	2018	2019	2020	2021	2022	Post 2023
Maturity of net debt	850	762	2,443	2,029	1,617	7,453

The table shows Gas Natural Fenosa's net debt maturity calendar as of 31 December 2017.

A total of 89.4% of the net interest-bearing debt matures in or after 2020. The average term of the debt is 5.8 years.

Of the net interest-bearing debt, 5.6% is short term and 94.4% is long term.

Main financial transactions

In April 2017, Gas Natural Fenosa issued Euros 1,000 million in notes under its EMTN programme with a 1.125% coupon, maturing in 7 years. The proceeds were used to redeem Euros 1,000 million of bonds maturing in 2018, 2020 and 2021. Additionally, on 29 September 2017, under the EMTN programme, Gas Natural Fenosa made a private placement of a Euros 300 million 12-year bond with a 1.875% coupon, and in November 2017 it issued an 8-year Euros 800 million green bond with a 0.875% coupon.

In January 2018, Gas Natural Fenosa 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.

The breakdown of net interest-bearing debt by currency at 31 December 2017, in absolute and relative terms, is as follows:

(Euros million)	31.12.2017	%
EUR	12,267	81.0
CLP	1,677	11.1
US$	614	4.1
MXN	295	1.9
BRL	292	1.9
Other	9	-
Net interest-bearing debt	**15,154**	**100.0**

Credit rating

The table shows the credit rating of Gas Natural Fenosa's long-term and short-term debt:

Agency	Short term	Long term
Fitch	F2	BBB+
Moody's	P-2	Baa2
Standard & Poor's	A-2	BBB

Liquidity and capital

At 31 December 2017, cash and cash equivalents together with available bank finance totalled over Euros 10,550 million, providing the company with sufficient liquidity to cover its debt maturities for more than 24 months, with the following breakdown:

Liquidity sources	Limit	Drawn	Undrawn
Committed credit lines	7,215	(254)	6,961
Uncommitted credit lines	539	(217)	322
Undrawn loans	42	-	42
Cash and cash equivalents	-	-	3,225
Total	**7,796**	**(471)**	**10,550**

Additionally, at 31 December 2017, the company had Euros 6,254 million available in the form of shelf registrations for financial instruments, including Euros 3,795 million in the Euro Medium Term Notes (EMTN) programme, Euros 1,000 million in the Euro Commercial Paper (ECP) programme, and a combined Euros 1,459 million in the stock market certificates programmes on the Mexico Stock Exchange, the commercial paper programme on the Panama Exchange, the marketable bonds programme in Argentina and the bond lines in Chile.

The breakdown of working capital at 31 December is as follows:

(Euros million)	2017	2016
Current operating assets[1]	5,536	5,595
Current operating liabilities[2]	(4,069)	(4,276)
	1,467	**1,319**

[1] Includes inventories, trade receivables and other receivables.

[2] Includes trade payables, other payables and other current liabilities, not including dividends payable.

Gas Natural Fenosa takes an average of 25 days to pay suppliers.

Analysis of contractual obligations and off-balance sheet transactions

The breakdown of contractual obligations, off-balance sheet transactions and contingent liabilities of Gas Natural Fenosa is set out in note 35 to the consolidated financial statements.

5.1.3. Analysis of results by segment

Gas distribution

5.1.3.1. Gas distribution in Spain

This business in Spain includes gas distribution, third-party access (TPA), the activities that are charged for outside the regulated distribution remuneration (meter rental, customer connections, etc.), and the piped liquefied petroleum gas (LPG) business.

Results

	2017	2016	%
Net sales	1,270	1,198	6.0
Purchases	(67)	(33)	103.0
Net personnel expenses	(76)	(68)	11.8
Other revenues and expenses	(221)	(208)	6.3
EBITDA	**906**	**889**	**1.9**
Depreciation, amortisation and impairment expenses	(299)	(291)	2.7
Change in operating provisions	(8)	(2)	300.0
Operating income	**599**	**596**	**0.5**

Net sales in the gas distribution business totalled Euros 1,270 million, Euros 72 million more than in 2016, due basically to the LPG business, which completed the acquisition of supply connections in the fourth quarter of 2016. Revenues in the regulatory inspection business increased in 2017 because of the schedule, since 2016 was a trough year with a lower number of inspections as a result of the change in the obligatory inspection frequency from every 4 to every 5 years.

Procurements were affected by higher LPG activity and a larger volume of regulatory inspections.

The implementation in 2017 of the group's 2018-2020 efficiency plan had a negative impact on personnel expenses in the amount of Euros -8 million.

These factors, coupled with the positive impact of efficiency measures on operating expenses, resulted in a 1.9% increase in EBITDA. Excluding the impact of the 2018-2020 efficiency plan, EBITDA would have increased by 2.8%.

Main aggregates

The main aggregates in gas distribution in Spain were as follows:

	2017	2016	%
Gas sales – TPA (GWh)	195,586	184,619	5.9
LPG sales (tn)	134,194	57,175	-
Distribution network (Km)	53,369	51,956	2.7
Change in connection points (‘000)	58	47	23.4
Connection points (‘000) (at 31/12)	5,371	5,313	1.1

Regulated gas sales increased by 5.9% (+10,967 GWh).

Residential demand was slightly higher than the previous year, +1.8% (+768 GWh) due to favourable weather conditions in December.

Demand growth was concentrated in the industrial market. Demand under 60 bars increased by 3.8% (+3,488 GWh). Demand for transportation and industrial consumption over 60 bars increased by 13.3% (+6,710 GWh).

The growth in LPG sales was due to the acquisition of supply connections in the fourth quarter of 2016.

The distribution network expanded by 1,413 km in 2017.

In connection with the addition of connection points, as part of the efficiency measures, the growth model was adapted to reduce unit capture costs, with the result that there was a delay in bringing residential connections into service; nonetheless, this was offset in remuneration terms by the larger number of new large accounts that were connected.

5.1.3.2. Gas distribution in Latin America

This division involves regulated gas distribution in Argentina, Brazil, Chile, Mexico and Peru. In Chile, it also includes the gas procurement and supply business.

Results

	2017	2016	%
Net sales	3,735	2,802	33.3
Purchases	(2,615)	(1,840)	42.1
Net personnel expenses	(119)	(105)	13.3
Other revenues and expenses	(293)	(240)	22.1
EBITDA	**708**	**617**	**14.7**
Depreciation, amortisation and impairment expenses	(159)	(146)	8.9
Change in operating provisions	(26)	(19)	36.8
Operating income	**523**	**452**	**15.7**

Revenues increased by 33.3% to Euros 3,735 million, due to appreciation by the main Latin American currencies.

EBITDA in Latin America, by country

	2017	2016	Variation	Currency translation	Adjusted variation
Argentina	48	44	9.1%	-8	27.3%
Brazil	283	240	17.9%	11	13.3%
Chile	206	174	18.4%	-	18.4%
Mexico	175	162	8.0%	-7	12.3%
Peru	-4	-3	-33.3%	-	-33.3%
Total	**708**	**617**	**14.7%**	**-4**	**15.4%**

The figure shows gas distribution EBITDA in Latin America, by country, and the variation with respect to 2016.

EBITDA amounted to Euros 708 million, an increase of 14.7% with respect to the previous year, impacted by currency performance. Excluding the effect of currency fluctuations, EBITDA would have increased by 15.4%.

Brazil contributed 40.0% of total EBITDA. Adjusting for the aforementioned currency effect, EBITDA increased by 13.3%. Dispatching for thermal power plants and TPA was higher (+34.7%) than in 2016, while gas sales in the residential-commercial market were down 4.5% year-on-year. In contrast, the change in trend in the industrial sector with respect to 2016 persisted, with 6.5% growth; additionally, sales of automotive natural gas increased by 11.0% year-on-year as it proved more competitive than liquid fuels.

Mexico accounted for 24.7% of total EBITDA in this business. Adjusting for the exchange rate effect, Mexico's EBITDA increased by 12.3%, and the sales margin increased by 19.3% due to tariff updates and growth in all markets.

Chile contributed Euros 206 million in EBITDA (+18.4% at constant exchange rates), i.e. 29.1% of total EBITDA from Latin America, due basically to higher sales to the residential-commercial segment. Gas distribution contributed Euros 134 million of that EBITDA figure, and gas procurement and supply contributed Euros 72 million.

EBITDA in Argentina amounted to Euros 48 million, higher than in the same period of 2016, following the entry into force on 1 April 2017 of a new tariff table for all markets, even though the new tariff will be implemented in three stages. Sales rose by 0.8% overall, considering that it was a particularly warm winter.

EBITDA in gas distribution in Latin America includes Euros 6 million from energy services (Euros 3 million in 2016).

Main aggregates

The main aggregates of the gas distribution business in Latin America are as follows:

	2017	2016	%
Gas activity sales (GWh):	264,428	241,891	9.3
Gas sales	141,762	131,361	7.9
TPA	122,666	110,530	11.0
Distribution network(Km)	62,812	61,127	2.8
Change in connection points (‘000)	209	208	0.5
Connection points (‘000) (at 31/12)	5,120	4,911	4.3

The main physical aggregates by country as of 31 December 2017 are as follows:

	Argentina	Brazil	Chile Distribution	Chile Procurement and supply*	Mexico	Peru	Total
Gas activity sales (GWh)	72,084	89,079	10,933	34,714	57,617	1	264,428
Change vs. 2016 (%)	0.8	23.7	6.5	4.3	12.5	-	9.3
Distribution network (km)	25,865	7,536	7,211	-	21,940	260	62,812
Change vs. 31/12/2016 (km)	202	90	245	-	888	260	1,685
Connection points ('000) (at 31/12)	1,651	1,090	602	-	1,773	4	5,120
Change vs. 31/12/2016 ('000)	19	53	18	-	115	4	209

* Does not include sales to group distributors for 10,614 GWh (9,992 GWh in 2016).

There were a total of 5.120 million gas distribution customers at 31 December 2017. Customer numbers increased by 209 thousand year-on-year, notably in Mexico.

Sales in the gas activity in Latin America, which includes both gas sales and TPA (third-party access) services, totalled 264,428 GWh, i.e. higher than in 2016, particularly due to higher sales in Mexico and Brazil.

The gas distribution grid expanded by 1,685 km (+2.8%) in the last 12 months, to 62,812 km at 31 December 2017. This expansion was driven mainly by Mexico (which added 888 km) and Peru (260 km).

Highlights in the region during the year:

- In Argentina, after a year of intense negotiations, the new tariffs arising from the Integral Tariff Review (RTI) were applied on 1 April 2017. The tariff tables were approved on 31 March 2017 by ENARGAS Resolution 4.354, which announced the RTI outcome for Gas Natural BAN.

  The outcome of the Integral Tariff Review process includes a major capital expenditure plan that is already under way and entails a significant change in the scale of this business.

  The new tariff will be phased in over three stages, with inflation adjustments every six months. The first stage commenced on 1 April 2017; the second began on 1 December 2017 and includes the first inflation adjustment; the third stage, which will also include an inflation adjustment, will commence in April 2018.

- In Brazil, new residential-commercial customer additions declined by 4.9% year-on-year due to a large number of additions of new buildings in 2016 on the occasion of the Olympic Games. Sales increased by 23.7% due to higher sales in the power generation and TPA market (+34.7%) as a result of higher thermal plant utilisation; sales of automotive natural gas expanded by 11.0% as this fuel was more competitive than liquid fuels and also because of the increase in vehicle conversions in the period; sales to the industrial market grew by 6.5% against the backdrop of a macroeconomic recovery. In contrast, sales in the residential and commercial market declined by 4.5%, mainly as a result of lower consumption by large retailers.

  Continuing with its expansion plan, which commenced in 2016, the company invested in compressed natural gas fuelling stations to bring this fuel to more towns in the State of Rio. It had added five municipalities by 2017 year-end: Angra dos Reis, Mangaratiba, Saquarema, Maricá and Cachoeiras de Macacu, serving 2,300 residential and commercial customers. It is expected to extend services to Araruama and Itaperuna in 2018, the goal being to double customer numbers in the next two years, and to begin supplying industries and CNG fuelling stations.

- Mexico continued to implement the growth acceleration plan, having increased customer numbers by 2.5% and made progress in all segments in the first half of the year. Gas sales increased by 12.5%, mainly in the TPA market, while the industrial market expanded by 1.5% and the residential-commercial market by 1.6%.

As part of the ongoing energy reform, in December 2016 the company was granted a concession to distribute gas in the Mexico Valley area (Cuautitlán-Texcoco-Hidalgo). This area adjoins Mexico City and will enable gas to be distributed in a market close to the existing grid. Commercialisation commenced this year and customer numbers are expected to reach 125,000 within five years.

Continuing with the expansion process, applications have been filed for permits to distribute in the Tabasco, Campeche, Mérida and Península (Quintana Roo) zones, comprising 28 municipalities with a total population of 5.3 million people and 1.5 million homes; 154,000 customers are expected to be signed in the first five years. To date, permits have been obtained for Tabasco, Campeche and Mérida.

- The number of supply connections in Chile increased by 18 thousand, including 3.2% growth in the residential-commercial segment with respect to 2016. As for gas sales and TPA, the strongest growth was observed in the residential-commercial (11.4%) and industrial (4.4%) segments, while there was a year-on-year decline in sales for power generation (23.3%) and TPA (2.6%).

  The new Gas Law, promulgated in February 2017, filled a legal vacuum by reducing the uncertainties surrounding investment, thereby allowing the distribution business to expand and providing for an increase in natural gas use in Chile, which was one of the main objectives of Chile's Energy Agenda and Energy Policy, both drawn up following work directed by the Ministry of Energy.

  In this context of legal certainty, an expansion plan has been stepped up since February 2017, with a substantial increase in investment in established territories, where the goal is to increase saturation, and in connecting more regions to the gas grid.

- Commercial operations commenced in Peru in November after Shell had commissioned the gas terminal; the company ended the year with 4,216 residential and commercial customer there.

Electricity Distribution

5.1.3.3. Electricity distribution in Spain

The electricity distribution business in Spain includes regulated distribution of electricity and network services for customers, basically connections and hook-ups, metering and other actions associated with third-party access to Gas Natural Fenosa's distribution network.

Results

	2017	2016	%
Net sales	861	833	3.4
Purchases	-	-	-
Net personnel expenses	(116)	(85)	36.5
Other revenues and expenses	(147)	(145)	1.4
EBITDA	**598**	**603**	**(0.8)**
Depreciation, amortisation and impairment expenses	(233)	(222)	5.0
Change in operating provisions	-	-	-
Operating income	**365**	**381**	**(4.2)**

The Ministerial Order on electricity tolls for 2017 (ETU/1976/2016) establishes that, until the approval of the remuneration for transmission and distribution for 2017 under the provisions of Royal Decree 1047/2013, of 27 December, and Royal Decree 1048/2013, of 27 December, the remuneration established in Order IET/981/2016 and Order IET/980/2016, which established the remuneration for electricity transmission and distribution companies for 2016, will be paid pro rata.

Net revenues amounted to Euros 861 million, i.e. 3.4% more than in the same period of 2016, due to application of the aforementioned Ministerial Orders and to the accrual of investments that were brought into operation, considering also the adjustment to the finance percentage of the base, as published in the draft ministerial order covering the remuneration for distribution.

EBITDA amounted to Euros 598 million in 2017, a 0.8% decline year-on-year due to the negative impact of personnel expenses caused by implementation of the group's efficiency plans. The implementation in 2017 of the group's 2018-2020 efficiency plan had a negative impact on personnel expenses in the amount of Euros -32 million. Excluding that effect, EBITDA grew 4.5%.

Main aggregates

	2017	2016	%
Electricity sales - TPA (GWh)	32,039	32,025	-
Connections (‘000) (at 31/12)	3,721	3,702	0.5
ICEIT (minutes)	47	43	9.3

Domestic demand amounted to 249,498 GWh in 2017, a 1.1% increase, according to figures from Red Eléctrica de Spain (REE).

The number of supply points increased by 18,602 net in year-on-year terms in 2017.

. The ICEIT figure for 2017 was 46.5 minutes, the wildfires in Galicia in October and the storms in December (an application for classification as force majeure has been filed) having discounted the impact of the storms in Galicia in February on the grounds of force majeure.

As of 31 December 2017, smart meters accounted for 96% of the total, and 94% of meter readings were being performed on a remote basis. The plan is to achieve 100% smart meters and remote readings in the residential market by 31 December 2018, as required by law. Nevertheless, in accordance with Order ETU 1282/2017, from 1 January 2019, electricity distribution companies are allowed to have up to 2% of their meters without upgrading provided that this is due to causes not attributable to the companies themselves, which must be duly supported and accepted by the National Markets and Competition Commission.

5.1.3.4. <u>Electricity distribution in Latin America</u>

This division involves regulated electricity distribution in Argentina, Chile and Panama, and electricity transmission in Chile.

In 2016, this area also included electricity distribution in Colombia.

Results

	2017	2016	%
Net sales	3,305	4,673	(29.3)
Purchases	(2,486)	(3,408)	(27.1)
Net personnel expenses	(151)	(216)	(30.1)
Other revenues and expenses	(234)	(360)	(35.0)
EBITDA	**434**	**689**	**(37.0)**
Depreciation, amortisation and impairment expenses	(138)	(162)	(14.8)
Change in operating provisions	(50)	(215)	(76.7)
Operating income	**246**	**312**	**(21.2)**

EBITDA in electricity distribution in Latin America totalled Euros 434 million. Excluding Colombia's contribution to EBITDA in 2016, EBITDA in this business would have been in line with the previous year (-0.5%). The currency effect was not material in the full year as the various currency movements offset each other.

The implementation in 2017 of the group's 2018-2020 efficiency plan had a negative impact on personnel expenses in the amount of Euros -7 million. Excluding that effect and the impact of Electricaribe, EBITDA would have increased by 1.1%.

EBITDA in Panama amounted to Euros 106 million in 2017, an 8.5% decline at constant exchange rates. This reduction was mainly due to extraordinary items such as refunds to customers of revenues corresponding to the tariff for the period 2002-2006, and higher revenues received in the first half of 2016 as a result of recognition, by the regulator, of extraordinary generation costs corresponding to the year 2015. Excluding the one-time effects, EBITDA would have increased by 2.1%.

EBITDA in Chile and Argentina (CGE) amounted to Euros 328 million, a Euros 7 million increase at constant exchange rates.

Main aggregates

	2017	**2016***	**%**
Electricity activity sales (GWh):	21,631	33,561	(35.5)
Electricity sales	19,755	31,441	(37.2)
TPA	1,876	2,120	(11.5)
Connection points ('000) (at 31/12)	3,726	3,622	2.9

* Colombia figures are as of 30/11/2016 since the December figures are not available.

Electricity sales amounted to 21,631 GWh, a 35.5% decline, basically due to deconsolidating Electricaribe (Colombia), which provided 12,306 GWh in sales. But for that effect, sales would have risen by 1.8%.

The main physical aggregates by country as of 31 December 2017 are as follows:

	Argentina	**Chile**	**Panamá**	**Total**
Electricity activity sales (GWh):	1,951	14,573	5,107	21,631
Change vs. 2016 (%)	0.3	1.8	2.3	(35.5)
				-
Connection points ('000) (at 31/12)	228	2,857	641	3,726
Change vs. 31/12/2016, ('000)	7	71	26	104

Sales in Panama increased by +2.3% year-on-year. Demand growth slowed in the early months of 2017 due to temperatures being lower than in the previous two years.

The increase in sales and in connection points (excluding the impact of deconsolidating Electricaribe) reflects sustained growth in the electricity distribution business in Latin America.

<u>Electricity transmission in Chile</u>

	2017	**2016**	**%**
Electricity transmitted (GWh)	14,403	14,484	(0.6)
Transmission network (Km at 31/12)	3,528	3,528	-

Power transmission in Chile decreased by 0.6% year-on-year, mainly due to lower activity in the first half which failed to be offset by the growth in the second half. The transmission grid is 3,528 km long, the same as one year earlier.

Gas

5.1.3.5. Infrastructure

This area includes operating the Maghreb-Europe gas pipeline as well as gas exploration, production, storage and regasification.

Results

	2017	2016	%
Net sales	317	324	(2.2)
Purchases	(1)	(4)	(75.0)
Net personnel expenses	(5)	(5)	-
Other revenues and expenses	(15)	(15)	-
EBITDA	**296**	**300**	**(1.3)**
Depreciation, amortisation and impairment expenses	(53)	(58)	(8.6)
Change in operating provisions	-	-	-
Operating income	**243**	**242**	**0.4**

Net sales in the infrastructure business totalled Euros 317 million in 2017, a 2.2% decline year-on-year.

EBITDA declined by 1.3% year-on-year to Euros 296 million due to the negative impact of the USD exchange rate. But for that effect, EBITDA would have been in line with the previous year.

Main aggregates

The main aggregates in international gas transportation are as follows:

	2017	2016	%
Gas transportation-EMPL (GWh):	100,371	111,720	(10.2)
Portugal-Morocco	38,787	41,295	(6.1)
Spain (Gas Natural Fenosa)	61,584	70,425	(12.6)

The gas transportation activity conducted in Morocco through companies EMPL and Metragaz represented a total volume of 100,371 GWh, 10.2% less than in 2016. Of that figure, 61,584 GWh were shipped for Gas Natural Fenosa through Sagane and 38,787 GWh for Portugal and Morocco.

Gas Natural Fenosa owns 14.9% of Medgaz, the company that owns and operates the Algeria-Europe subsea gas pipeline connecting Beni Saf with the Almería coast in Spain (capacity: 8 bcm/year). That capacity is associated with a new supply contract amounting to 0.8 bcm/year. A total of 7,589 GWh were shipped via the Medgaz pipeline for Gas Natural Fenosa in 2017.

The company currently has 916 GWh of company-owned gas storage capacity. A number of works (pipeline replacement and initial well drilling) have been completed on one of the projects to increase storage capacity, as part of the exploration, production and storage projects that Gas Natural Fenosa plans for the Guadalquivir Valley in the coming years. The other four projects are at various stages of the permit process.

5.1.3.6. Supply

This business includes wholesale gas procurement and supply both in the Spanish liberalised market and in other countries, maritime shipping, retail supply of gas and other related products and services in the liberalised market in Spain, and supply of gas at the last-resort tariff (TUR) in Spain.

The figures for the gas supply business in 2017 and 2016 were restated due to discontinuation of the Italian business; consequently, sales to the Group's supply company in Italy are shown under the International LNG business, while sales to end customers in Italy are detailed in section 2.2.6. Income from discontinued operations.

Results

	2017	2016	%
Net sales	10,134	8,619	17.6
Purchases	(9,366)	(7,813)	19.9
Net personnel expenses	(76)	(65)	16.9
Other revenues and expenses	(222)	(217)	2.3
EBITDA	**470**	**524**	**(10.3)**
Depreciation, amortisation and impairment expenses	(80)	(60)	33.3
Change in operating provisions	(37)	(36)	2.8
Operating income	**353**	**428**	**(17.5)**

Net sales amounted to Euros 10,134 million, a 17.6% increase with respect to last year. EBITDA amounted to Euros 470 million, a 10.3% decrease with respect to the previous year, due to greater competitive pressure on margins in the industrial market in Spain and to the decline in the volume of sales to the retail market (-6.2%).

The implementation in 2017 of the group's 2018-2020 efficiency plan had a negative impact on personnel expenses in the amount of Euros -2 million. Excluding that effect, EBITDA fell by 9.9%.

EBITDA in the supply business includes Euros 118 million from energy services (Euros 106 million in 2016).

Market situation

Demand for gas in Spain amounted to 349,223 GWh in 2017 (320,027 GWh in 2016): 52,082 GWh for the residential market (51,880 GWh in 2016), 221,787 GWh for the industrial market and for third-party supply (208,671 GWh in 2016) and 75,354 GWh for the electricity market (59,476 GWh in 2016).

The main gas price indices performed as follows:

	2017	2016	%
Brent (USD/bbl)	54.3	43.7	24.2
Henry Hub (USD/MMBtu)	3.1	2.4	29.2
NBP (USD/MMBtu)	5.8	4.7	23.4
TTF (EUR/MWh)	17.0	13.9	22.3

Main aggregates

The main aggregates in the supply activity are as follows:

	2017	2016	%
Gas supply (GWh):	360,031	325,457	10.6
Spain:	176,053	178,916	(1.6)
Gas Natural Fenosa supply	139,304	140,877	(1.1)
Residential	25,381	27,053	(6.2)
Industrial	93,135	96,421	(3.4)
Electricity	20,788	17,403	19.5
Supply to third parties	36,749	38,039	(3.4)
International:	183,978	146,541	25.5
Wholesale Europe supply	61,891	67,283	(8.0)
International LNG	122,087	79,258	54.0
Energy services contracts (‘000) (at 31/12)	2,873	2,853	0.7
Market share of gas contracts Spain	39.9%	44.0%	(9.3)
Gas carrier fleet capacity (m3)	940,440	1,387,344	(32.2)

Gas supply

Wholesale supply by Gas Natural Fenosa totalled 334,650 GWh, a 12.1% increase, basically due to the international business (+25.5%).

Gas Natural Fenosa supplied 150,672 GWh of gas to end customers in Spain, i.e. 0.8% less than in the previous year.

International gas supply amounted to 183,978 GWh in 2017, a 25.5% increase year-on-year, driven particularly by international LNG supply.

In the organised market in gas through MIBGAS, the Spanish Cabinet decided to require the Gas Natural Fenosa Group to act as a market maker in day-ahead (DA) and month-ahead (MA) products in order to enhance liquidity in those markets.

In the fourth quarter of 2017, Gas Natural Fenosa participated in the auction for new short-term underground storage capacity for the period from November to December 2017. Gas Natural Fenosa was awarded 1.0 TWh of capacity, i.e. 37% of the total capacity that was adjudicated.

Gas Natural Fenosa has a strong position in natural gas supply in Europe, with a presence in France, Belgium, Ireland, Luxembourg, Portugal, the Netherlands and Germany.

Sales in France in 2017 amounted to 37.6 TWh, to customers in numerous segments such as industry, local government and the public sector. Sales in Belgium, Luxembourg, the Netherlands and Germany in the same period amounted to 17.2 TWh.

Gas Natural Fenosa is also active in the wholesale market in Ireland, where it sold 1.6 TWh in 2017.

Gas Natural Fenosa is the second-largest operator in Portugal, where its market share is approximately 12%, slightly lower than in the preceding quarter due to fierce competition; it is the leading foreign player in the Portuguese market, having sold 5.5 TWh in 2017.

The company continues to diversify into international markets, having sold gas in the Americas and Asia. This strengthens the company's presence in the main international LNG markets, providing it with a medium-term position in growing countries and new markets.

In line with its firm commitment to innovation, Gas Natural Fenosa has developed a unique system for transporting LNG. This patented system consists of a floating platform with a coupling system that is compatible with all gas carriers. Called DirectLink, it makes it possible to supply LNG in remote or inaccessible locations where it was not previously feasible to use natural gas for economic or financial reasons.

Shipping fleet capacity declined due to conclusion of the operating leases on three tankers and to delays in the delivery of two new tankers under finance lease, which had been expected in 2017.

In the retail market, Gas Natural Fenosa focuses on meeting its customers' energy needs. With a range of quality products and services, it has 11.7 million active gas, electricity and maintenance contracts.

Gas Natural Fenosa provides a comprehensive service by integrating the supply of both energies (gas and electricity) with maintenance services to achieve efficiencies and enhance customer satisfaction; it supplies both energies to over 1.5 million homes, a large percentage of which have a maintenance contract in place.

With a strong focus on continued growth in the retail business, the company sells products and services throughout Spain, having signed 1,512 thousand new contracts in 2017.

In the residential market, Gas Natural Fenosa updates its product portfolio in order to offer electricity and natural gas tariffs that fit each customer's profile. New products meet customer needs in terms of usage, how they wish to pay, when they use energy and whether they are interested in consuming renewable energy.

In the SME market, Gas Natural Fenosa makes customised price offers in this segment. It also expands, updates and pursues flexibility in its product portfolio in order to match customer profiles as closely as possible through products indexed to electricity market prices, fixed-price products for business, and eco-type products.

In the SME segment, Gas Natural Fenosa tries to distinguish itself from competitors by offering its Energy Saving Service, which provides customers with recommendations on how to save by optimising their contractual power and conditions. We also enhance end-to-end management of our portfolio by personalised attention via a range of channels, including face-to-face customer care backed by agents from our Energy Class and Generalist platforms, depending on the customer's volume. Additionally, the portfolio of gas and electricity maintenance services for SMEs continues to expand, having attained 32,300 contracts.

The offering of services for residential and SME customers has enabled the company to increase the number of active contracts to 2.8 million, managed through the group's own operating platform with 117 associated firms connected via an online system. As a result of this performance, the portfolio of energy and services contracts in the retail segment increased in value.

Gas Natural Fenosa remains committed to innovation by adding new functionalities in all digital channels, such as the ability to buy services and receive customer care online; its online platform receives 6 million queries per year.

Gas Natural Fenosa continues to develop its own network of natural gas service stations that are open to the public. At the end of 2017, it had 53 service stations (both compressed and liquefied natural gas). A total of 30 stations are open to the public and 23 are private.

The integrated energy services solutions business continues to expand. A survey conducted by DBK identified Gas Natural Servicios as market leader in energy services.

Unión Fenosa Gas

In 2017 Unión Fenosa Gas (equity accounted, 100% aggregates) supplied 41,326 GWh of gas in Spain, compared with 35,741 GWh the previous year. Additionally, a total of 25,048 GWh of energy was traded in international markets, compared with 22,500 GWh in 2016.

Electricity

5.1.3.7. Electricity in Spain

The electricity business in Spain basically includes power generation in Spain, wholesale and retail electricity supply in the liberalised market in Spain, and electricity supply at the Small Consumer Voluntary Price (PVPC).

Results

	2017	2016	%
Net sales	5,375	5,279	1.8
Purchases	(4,270)	(3,813)	12.0
Net personnel expenses	(158)	(138)	14.5
Other revenues and expenses	(645)	(613)	5.2
EBITDA	**302**	**715**	**(57.8)**
Depreciation, amortisation and impairment expenses	(442)	(523)	(15.5)
Change in operating provisions	(31)	(38)	(18.4)
Operating income	**(171)**	**154**	**(211.0)**

Net sales in the electricity business in Spain amounted to Euros 5,375 million, 1.8% more than in the previous year, while EBITDA amounted to Euros 302 million, 57.8% less than last year.

EBITDA performance was shaped by weather: Gas Natural Fenosa's hydroelectric output shrank by 71.4%, since 2017 proved to be a very dry year, in contrast with 2016, which was classified as very wet. It was also affected by the fact that higher fuel prices increased generating costs.

The implementation in 2017 of the group's 2018-2020 efficiency plan had a negative impact on personnel expenses in the amount of Euros -23 million. Excluding that effect, EBITDA declined by 54.5%.

Depreciation and amortisation and impairments amounted to Euros 442 million, a decline of Euros 81 million (-15.5%) with respect to the previous year, basically because of extending the useful lives of the combined cycle plants from 25 to 35 years on 1 January 2017 following technical surveys completed in the first quarter, in line with the practices adopted by the leading players in the industry.

Market situation

Overall, demand in Spain in 2017 was 1.1% higher than in 2016 (1.6% after adjusting for temperatures and the calendar effect).

The physical balance of interchanges amounted to imports of 9,159 GWh in 2017, i.e. 19.4% more than the 7,669 GWh imported in 2016.

Pumped storage consumption in the full year amounted to 3,662 GWh, i.e. 24.0% less than in 2016 due to high market prices in comparison with last year.

Net generation in Spain in 2017 was practically unchanged with respect to 2016.

Renewable output declined by 16.7% and covered 32.9% of demand, compared with 39.9% in 2016.

Wind output in 2017 amounted to 47,484 GWh (+0.4%) and covered 18.8% of demand, 0.1 points less than in 2016.

Other renewable output declined by 32.1%, comprising increases by solar photovoltaic (5.1%), solar thermal (5.7%) and other renewables (8.1%) and a decline in hydroelectric output (-47.5%: conventional -50.2% and other hydroelectric -31.7%).

Hydroelectric energy capability in 2017 resulted in it being classified as an extremely dry year, with an exceedance probability of 99% when compared with the historical average: i.e. statistically, 99 out of every 100 years would be wetter than 2017.

Non-renewable output increased by 11.2% in 2017 as a whole.

The thermal gap increased by 25.7%, and coverage was 6 points higher than in 2016 (30.3% vs. 24.3%).

Nuclear output decreased by 0.9%. Coal-fired output increased by 21.1%. Utilisation of the former capacity guarantee units was 41% in 2017, compared with 59% for other coal-fired units. CCGTs increased output by 32.0% with respect to 2016. CCGT output covered 13.4% of demand in the full year, i.e. 3 points more than in 2016. Other non-renewable thermal, cogeneration and waste-to-power experienced an increase of 8.1% in 2017.

The average price in the electricity pool was Euros 52.24/MWh in 2017, i.e. 32% more than in 2016 (Euros 39.66).

The main electricity market and related price indices (i.e. in addition to those referred to in section 5.1.3.6) performed as follows (accumulated annual data):

	2017	**2016**	**%**
Average price in the daily power generation market (EUR/MWh)	53.6	40.8	31.4
Carbon API 2 CIF (USD/t)	84.5	59.8	41.3
CO_2 EUA (EUR/ton)	5.8	5.4	7.4

Main aggregates

The main aggregates in Gas Natural Fenosa's electricity business in Spain were as follows:

	2017	2016	%
Installed capacity (MW)	12,716	12,716	-
Generation	11,569	11,569	-
Hydroelectric	1,954	1,954	-
Nuclear	604	604	-
Coal	2,010	2,010	-
CCGT	7,001	7,001	-
Renewables and Cogeneration	1,147	1,147	-
Wind	979	979	-
Small hydroelectric	110	110	-
Cogeneration and others	58	58	-
Electricity produced (GWh)	27,953	28,504	(1.9)
Generation	25,668	26,046	(1.5)
Hydroelectric	1,126	3,933	(71.4)
Nuclear	4,578	4,463	2.6
Coal	5,953	5,687	4.7
CCGT	14,011	11,963	17.1
Renewables and Cogeneration	2,285	2,458	(7.0)
Wind	1,801	1,844	(2.3)
Small hydroelectric	407	562	(27.6)
Cogeneration and others	77	52	48.1
Power generation availability factor (%)	93.6	88.2	5.4 p.p.
Electricity sales (GWh)	35,151	36,384	(3.4)
Liberalised market	30,098	31,167	(3.4)
Small Consumer Voluntary Price System (PVPC)	5,053	5,217	(3.1)
Generation market no renewable share	17.1	17.0	0.1 p.p.

Electricity generated by Gas Natural Fenosa in mainland Spain declined by 1.9% in 2017, while conventional output declined by 1.5%.

Conventional hydroelectric output fell by 71.4% year-on-year.

Reservoirs in the Gas Natural Fenosa watersheds were at 16% of capacity, 7 points lower than at the end of 2016.

Nuclear output increased by 2.6% in 2017.Coal-fired output increased by 4.7%, and capacity utilisation stood at 35%.The combined cycle (CCGT) plants increased output by 17.1% in 2017. CCGT utilisation in 2017 was 23%, seven points more than that of the industry as a whole.

Consolidated emissions of CO_2 in 2017 from Gas Natural Fenosa's coal-fired power plants and CCGTs that are affected by the regulation governing greenhouse gas emission trading totalled 11.2 million tons (+0.8 million tons with respect to 2016). This increase was attributable mainly to the CCGTs, because they operated longer due to the low level of precipitation in 2017.

Gas Natural Fenosa applies a comprehensive approach to its portfolio of CO_2 emission rights for the post-Kyoto (2013-2020) period, acquiring the necessary emission rights and credits through active participation in the secondary market.

Electricity supply, including sales to the liberalised market and under the last resort tariff, declined by 3.4% in 2017. The electricity supply portfolio is in line with Gas Natural Fenosa's strategy of maximising margins, optimising market share, and hedging against price variations in the electricity market.

In the area of renewables and cogeneration, in 2017 Gas Natural Fenosa Renovables (GNFR) commenced construction of 8 of the 13 wind farms registered under the maximum quota of 450 MW authorised for the Canary Islands by the Ministry of Industry, Energy and Tourism. The eight plants under construction total 41 MW of capacity; construction is practically complete and waiting for Red Eléctrica de Spain to finish the power offtake infrastructure. At the same time, work continues in order to obtain the necessary permits to begin building the other projects. This capacity will enjoy a special remuneration system, conditional upon it being commissioned by 31 December 2018.

Also, during the fourth quarter of 2017, the necessary authorisations were obtained to shortly begin construction of the first wind and photovoltaic projects associated with the adjudications that GNFR obtained in the two auctions held by the Spanish government in 2017: 667 MW of wind and 250 MW of photovoltaic capacity.

At 31 December 2017, GNF Renovables had a consolidable total operational capacity of 1,147 MW, of which 979 MW are wind, 110 MW are small hydroelectric and 58 MW are cogeneration and photovoltaic. Those figures include the slurry-based cogeneration plants (43 MW) that are currently mothballed.

5.1.3.8. <u>International Electricity</u>

This area encompasses all of the Group's international power generation assets and holdings in Mexico, Puerto Rico, the Dominican Republic, Panama, Costa Rica, Brazil (commercial operation in September 2017) and the power generation projects in Australia and Chile, as well as assets operated for third parties via group company O&M Energy.

Results

	2017	**2016**	**%**
Net sales	890	738	20.6
Purchases	(511)	(385)	32.7
Net personnel expenses	(37)	(38)	(2.6)
Other revenues and expenses	(66)	(76)	(13.2)
EBITDA	**276**	**239**	**15.5**
Depreciation, amortisation and impairment expenses	(121)	(124)	(2.4)
Change in operating provisions	-	-	-
Operating income	**155**	**115**	**34.8**

EBITDA in the International Electricity business amounted to Euros 276 million in 2017, up 15.5% compared with the previous year, due basically to a higher EBITDA contribution from Mexico.

Depreciation and amortisation and impairments amounted to Euros 121 million, a decline of 2.4% with respect to the previous year, basically because of extending the useful lives of the combined cycle plants from 25 to 35 years on 1 January 2017 following technical surveys completed in the first quarter, in line with the practices adopted by the leading players in the industry.

The following table details international electricity EBITDA by country and its performance from 2016:

	2017	2016	variation	Currency translation	Ajusted variation
Mexico	258	216	19.4%	-5	21.8%
Rest	18	23	-21.7%	-	-21.7%
Total	**276**	**239**	**15.5%**	**-5**	**-103.1%**

EBITDA in Mexico increased by 19.4% because the contribution margin increased, basically due to higher surplus power, better availability, better performance, and favourable trends in the contracts' benchmark indices.

Higher efficiency in managing the commercial mix enabled Bii Hioxo to improve its results despite the problems resulting from the Oaxaca earthquake in early September.

EBITDA in the Dominican Republic declined by 14.9% due to the impact on margins of lower spot prices after expiration of the power purchase agreement (PPA) with the distribution companies.

EBITDA in Panama increased by 6.8% due to higher precipitation in the areas where the plants are located.

Main aggregates

The key physical aggregates in this business are as follows:

	2017	2016	%
Installed capacity (MW)	2,732	2,590	5.5
Mexico (CCGT)	2,109	2,035	3.6
Mexico (wind)	234	234	-
Brazil (solar)	68	-	-
Costa Rica (hydroelectric)	101	101	-
Panama (hydroelectric)	22	22	-
Dominican Republic (oil-fired)	198	198	-
Electricity generated (GWh)	18,436	17,857	3.2
Mexico (CCGT)	16,340	15,648	4.4
Mexico (wind)	656	793	(17.3)
Costa Rica (hydroelectric)	48	-	-
Panama (hydroelectric)	369	398	(7.3)
Dominican Republic (oil-fired)	98	98	-
Kenya (oil-fired)	925	920	0.5
Availability factor (%)			
Mexico (CCGT)	96.6	93.4	3.2 p.p.
Costa Rica (hydroelectric)	97.5	93.2	4.3 p.p.
Panama (hydroelectric and oil-fired)	90.5	94.4	-3.9 p.p.
Dominican Republic (oil-fired)	92.1	89.4	2.7 p.p.

Output from the CCGT plants in Mexico increased year-on-year as a result of the different schedule of maintenance shutdowns and greater sales of surplus energy from Naco Nogales, Norte Durango and Tuxpan, which began selling surpluses in February 2017. The capacity increase year-on-year was attributable to Durango, mainly because of the high fogging process implemented in 2017.

Wind power output by Bii Hioxo declined due to lower winds and also to the impact of the Oaxaca earthquake early in September 2017. Differences in maintenance calendars between years resulted in higher availability than in 2016.

Hydroelectric output in Costa Rica was impaired by lower precipitation. As discussed in the section on the financial result, the Costa Rica concessions are accounted for as finance leases in accordance with IFRIC 12.

Output in Panama was in line with the previous year as a result of lower precipitation in the fourth quarter of 2017 in the areas where the plants are located. The lower availability with respect to last year is attributable to differences in the maintenance schedule, notably the fact that the Los Algarrobos hydroelectric plant underwent its annual overhaul in the second quarter of 2017.

Output in the Dominican Republic increased slightly year-on-year due to higher demand and the withdrawal of the more efficient plants from the system to a greater extent in 2017.

Gas Natural Fenosa's first photovoltaic power project in Brazil entered commercial operation in September 2017: the Sobral I and Sertao I solar farms, with an installed capacity of 68 MW, are located in the Piauí region in northern Brazil.

<u>Ecoeléctrica</u>

Ecoeléctrica, the CCGT plant in Puerto Rico (equity accounted), increased its contribution to the consolidated figures to Euros 58 million in 2017 (from Euros 49 million in 2016) as a result of higher capacity revenues and a higher energy margin because of lower fuel costs. Output in 2017 totalled 2,765 GWh (100%), i.e. less than in 2016 (3,346 GWh) due to lower dispatching by PREPA and the effects of hurricane Maria.

5.2 Service excellence

What resources are relevant for this undertaking?	How do we measure our performance?
Financial Manufactured Human Social	Overall satisfaction with service quality

What does it mean for Gas Natural Fenosa? Risks and management approach

Gas Natural Fenosa directs its efforts to provide its customers with a service and experience that, In addition to complying with legal requirements, is in accordance with your needs and fulfills the commitments voluntarily assumed by the group.

What is our commitment?

- To work 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 Gas Natural Fenosa to their needs.
- Facilitating the administrative needs of customers through simple and efficient operations.
- Offering innovative products and services that encourage energy efficiency and which contribute towards the sustainability of society.
- Diversifying and extending the commercial offer to include products and services of high value-added that respond to the evolving needs of customers.
- Applying technological innovation and the technical enhancements available as a means of maintaining an efficient, safe and sustainable supply.

What are our main milestones in 2017?

- Continuing to make progress in the Customer Experience and Advocacy projects and in group complaints
- Execute the joint project with Repsol of LNG stations at the main points of the Spanish transport network.
- Customising management to high-value SME customers
- Developing new interactive tools for procurement that respond to the needs of the new organised market
- Developing new value-added services that respond to environmental requirements driven by regulation and social awareness on energy saving and environment

Analysis of the 2017 results

Quality and reliability of the service

Maintenance of the gas and electricity facilities is an essential aspect within Gas Natural Fenosa'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.

In 2017, the main investment projects undertaken in Latin America were the renewal of the gas network in Argentina (24.6 km), Mexico (46.1 km, mainly in Monterrey) and in Brazil (40 km in Rio de Janeiro); the renewal of connections in Argentina (12,481 connections in Buenos Aires), Mexico (5,190 connections) and Brazil (1,643 connections).

Products and services adapted to customers' requirements and priorities

Gas Natural Fenosa's commercial strategy pays special attention to current customer satisfaction, as well as optimisation of the commercial supply. The loyalty schemes are targeted at contributing towards the customer's welfare, while also company looks for generating security and trust in management.

Gas Natural Fenosa offers value added products and services on top of the gas and electricity supply in order to maximize its commercial offer and retain the customers. These services allow customers to manage their domestic and business needs in a comprehensive way, helping them to be efficient in their energy usage.

In 2017, we have consolidated the catalogue of products and services for residential and SME customers with new energy tariffs and types of maintenance that include smart devices.

Customer's satisfaction and experience

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

Gas Natural Fenosa has a model to measure customers' experience, through which it constantly monitors its satisfaction and recommendation level. During 2017, we have extended the Customer Experience Management (CEM) tool as an instrument to measure and manage the customer experience by adding new functionalities. Following the customer's interaction with the company, the former receives a short questionnaire to find out their level of satisfaction and recommendation, and they are asked to grade their experience.

The measurement model rests on two complementary pillars:

- General overview: of all of the company's customers and of the competitors' customers, which represents the global satisfaction index.
- Contact point of view: where we analyse the experience of customers that have made recent use of the services and channels made available to them.

In the retail sector, Gas Natural Fenosa continues to spearhead satisfaction in Spain for a further year

<u>Communication and transparency with customers</u>

Gas Natural Fenosa has adapted communication with customers through the use of new technologies, which encourages ongoing contact.

Also, Gas Natural Fenosa is aware that the bill continues to be the main channel of communication with its customers. That is why includes information of interest to the customer, helping to explain the content of the bill and how regulatory changes affect this.

In 2017, Gas Natural Fenosa has worked on the introduction of billing methods and on the development of estimation alternatives, introducing a range of improvements in the billing process:

- Receiving the bill before the bank debit and on time.
- The possibility of paying non-direct debit bills 24 hours a day, 365 days a year.
- Launch of the card payment in Portugal.
- Launch of the "Understand your Bill" service for Energy Class and Premium customers.

<u>Customer service</u>

Gas Natural Fenosa has is looking to develop a more personal and customized model. This model has been developed in in Brazil, Chile, Colombia, Spain, Mexico, Panama and Portugal and is divided into three parts:

- Operational and training model: the aim is to anticipate customers' needs.
- Technological model: this involves a major technological renewal in the implementation.
- Economic model of procurement: we have opted for a partnership model with suppliers worldwide and an alignment of objectives.

Furthermore, for the sixth year running, the company has continued to provide the Energy Class service, a pioneer in the energy sector and which offers an exclusive service to the company's major customers. In 2017, over 104,000 gas and electricity customers enjoyed preferential treatment and advice on their energy supply and management of their contracts.

Privacy and security of the customer's data

Gas Natural Fenosa has defined an Information Security Policy that ensures proper processing of this data throughout its life cycle, from collection and processing through to removal or safeguarding this data once the relationship has terminated.

A total of 730 complaints concerning customer privacy were individually analyzed, investigated and resolved in 2017, as part of the process defined by the company.

According to the external report of data audit, Gas Natural Fenosa satisfactorily complies with the security measures required in the Implementing norms of the Personal Data Protection Act (LOPD).

During 2017 we have undertaken the analysis project to adapt Gas Natural Fenosa to the new General Regulations governing Personal Data Protection (RGPD) at European level. This project includes some adaptation actions that were carried out in 2017 and a proposal for action scheduled for 2018.

5.3 Responsible management of the environment

What resources are relevant for this undertaking?	**How do we measure our performance?**
Financial Manufactured Environmental Social	Direct greenhouse gas emissions Emission factor for electricity generation Installed capacity free of emissions Net production free of emissions Activity with ISO 14001 environmental certification

What does it mean for Gas Natural Fenosa? Risks and management approach

Gas Natural Fenosa 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.

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.
- Promoting the efficient and responsible use of water, introducing activities targeted at greater awareness of this resource and improving water management.
- Guaranteeing the prevention of pollution through ongoing improvement, the use of best available techniques and the analysis, control and minimisation of environmental risks.

What are our main milestones in 2017?

- Definition of the new Environmental Strategy to 2020 based on the environmental pillars of climate and air quality, water, natural capital and circular economy.
- Growth in low or zero-emission renewable power in alignment with climate and air quality strategy.
- Consolidation of risk and opportunity analysis in relation with climate.
- Progress in the certification of new environmental management systems in compliance with ISO 14001, with adaptation to the 2015 revision of the standard.
- Upholding our scores to remain in leadership band A of the Carbon Disclosure Program (CDP) questionnaire in relation with climate and water.

– Defining positioning and roll-out of lines of action in relation with circular economy.

Analysis of the 2017 results

	Unit	2017	2016
Direct greenhouse gas emissions	$MtCO_2e$	20.5	19.5
Emission factor for electricity generation (1)	tCO_2/GWh	431	411
Installed capacity free of emissions (2)	%	22.4	22.1
Net production free of emissions (2)	%	9.7	16.4
Activity with ISO 14001 environmental certification (3)	%	87.7	86.3

(1) Factor for power generation facilities operated by Gas Natural Fenosa and in which has a controlling interest (Corporate Responsibility Rerport perimeter).
(2) By historic traceability, including nuclear power generation.
(3) Taking into account only the Ebitda of companies with environmental impact.The ebitda of the certificated activity with ISO 14001 represents the 78.8% of total ebitda.

Integrated environmental management

In 2017, Gas Natural Fenosa activities that have a significant environmental impact was covered by the environmental management model set out in the ISO 14001 standard. It should be pointed out that the system was successfully switched over to the 2015 version of the standard over the course of the year. Variations are due to the increase in certified businesses and disinvestments made by the group which had been certified according to this standard. In 2017, environmental certification was extended to electricity and gas distribution companies in Chile.

Environmental planning is included in the Quality, Environment, Security and Health Plan. This plan consists of strategies and lines of action which define the working guidelines for each period. There were 257 environmental management-related objectives defined in 2017 with satisfactory fulfilment of the plan.

Environmental training is a basic tool for preventing and reducing environmental impacts and improving environmental operational control in our activities. In this sense, a total of 3,826 hours of training were received by 1,572 participants in 2017, with plan objectives being met by 140% and 133%, respectively.

Environmental Strategy to 2020

The Environmental Strategy is based on four environmental and two transversal pillars. The environmental pillars are defined according to the key vectors of the company’s environmental management system:

– Climate and Air: Reducing emissions through our operations and promoting the use of sustainable energy.
– Water: Promoting the efficient and responsible use of water.
– Natural Capital: Minimising the impacts on ecosystems and promoting natural capital.
– Circular Economy: Optimising resource consumption and enhancing resource recirculation.

The transversal pillars are necessary for integrating environmental sustainability into the decision-making process within the group’s businesses.

In turn, these pillars have been transposed into 22 lines of action (16 environmental and 6 transversal). Each line of action is divided into a series of actions that sets out the guidelines to enable each business to define objectives (specific actions).

The Strategy is instrumented through the Gas Natural Fenosa’s environmental management model, based on the international ISO 14001 standard, and forms a basic part of the company‘s integrated management system (IMS) for quality, the environment, and health and safety.

1. Climate and air

The climate and air quality pillar aims to reduce emissions through our operations and to promote the use of sustainable energy. The lines of action associated with this pillar are:

- Reducing emissions through the operations.
- Reducing emissions by means of energy efficiency.
- Developing sustainable services and products.
- Integrating internal climate change management.
- Determining impact and performance.

Thermal power stations operation increased significantly in 2017 compared to 2016 as a consequence of the lower availability of renewable resources in Spain. The lack of rains and wind hindered normal operations of zero-emissions installations, making it necessary to bring in manageable and CO_2-emitting energies to satisfy demand. As a result, emission values were recorded that were significantly higher than those of 2016, a year with more favorable weather conditions, although not as high as those recorded in 2015.

Gas Natural Fenosa is firmly committed to sustained growth in its renewable energy generation installations. Given the circumstances described, power generated from renewable energy sources was lower than the previous year's figure. Despite 2017 being a dry year with less wind, lower environmental impact was appreciated when compared to years with similar weather patterns, such as 2012. Mention should be made of the new developments in renewable technologies taking place in Brazil and those earmarked for 2018 in the Canary Islands.

Gas Natural Fenosa takes an active role in the global business initiatives and climate action and in the most relevant international forums, such as the United Nations Conference of the Parties.

In 2017, there was an increase in absolute emissions of SO_2, NO_x and total suspended particles (TSP) into the atmosphere, due to increased operations of the thermal power stations, caused by the decrease in renewables production (hydroelectricity and wind power) in Spain.

Likewise, there was significant progress made in 2017 in relation to the development of renewable gas and the promotion of sustainable, low-emission mobility.

2. Water

For the purpose of promoting the efficient and responsible use of water, the lines of action associated with this pillar are:

- Optimising water consumption and reducing water discharge.
- Fostering the sustainable use of water among our stakeholders.
- Including water in the decision-making process.
- Determining impact and performance.

In general terms, there was a significant increase in the volume of water consumed in 2017, mainly owing to increased demand created by activity at coal-fired and combined-cycle power stations.

In this context, a series of studies and actions were conducted to enable a gradual and consolidated reduction in water consumption in the medium and long term. Among these, mention must be made of the risk and opportunities analyses performed by Gas Natural Fenosa in relation with water.

3. Natural capital

The aim or this pillar is to minimise the impacts on ecosystems and to promote natural capital. In this sense, the associated lines of action are:

- Reducing and compensating for our impacts and enhancing the value of natural environments.
- Determining our impact on natural capital.

- Determining impact and performance.

The company continues to extend the focus of its environmental management towards valuing natural capital, in other words, the reserves of renewable and non-renewable natural assets found in nature, in order to identify and assess the dependency and impact (both positive and negative) of its activities.

The company conducted a large number of actions to preserve biodiversity, some of these in response to the requirements set out by the environmental authorities and others of a voluntary nature.

4. Circular economy

Gas Natural Fenosa focuses its efforts in the field of circular economy on optimising resource consumption and enhancing resource recirculation. For this purpose, the following lines of action have been developed:

- Optimising the consumption of raw materials.
- Reducing the production of waste and encouraging its transformation into by-products.
- Contributing to the development of circular economy regulation.
- Determining impact and performance.

In 2017, generation of the most significant non-hazardous waste increased compared to 2016. Owing to reasons previously explained, mention must be made of increased ash and slag production.

5.4. Interest in People

What resources are relevant for this undertaking?	How do we measure our performance?
Financial Human Social	Total number of employees Average age and length of service Voluntary rotation index Total training hours Corporate University participants Percentage of staff taking part Training hours per employee Investment in training per person People with disabilities integration index Diversity men/women Women in management posts

What does it mean for Gas Natural Fenosa? Risks and management approach

For Gas Natural Fenosa it is essential to foster a quality working environment, based on respect, diversity and personal and professional development. Gas Natural Fenosa 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.

What is our commitment?

- To apply 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.).
- To encourage 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.
- To promote 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.
- To ensure 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.

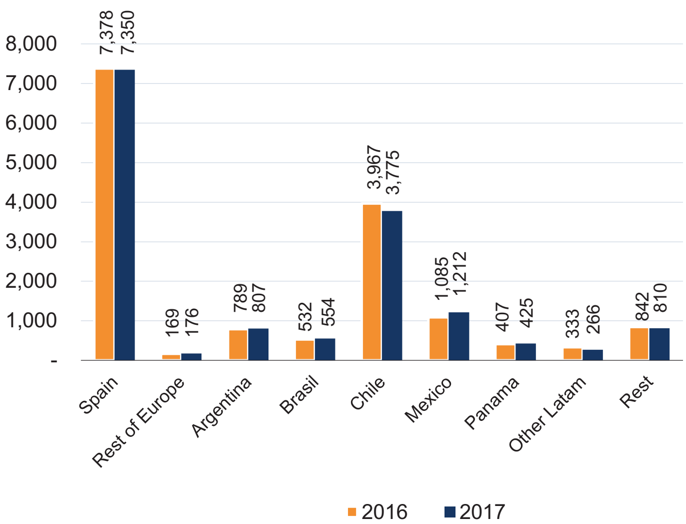
- To promote diversity and equal opportunities in an environment of respect, understanding and ongoing dialogue, with a special focus on the inclusion of disabled persons and extending this commitment to suppliers and collaborating companies.
- To foster constant liaison between the company and workers' representatives that enables feedback in order to take decisions.

What are our main milestones in 2017?

- Consolidation of the Strategic Workforce Planning model for planning and management of workforces.
- Cultural transformation and development of PIP services to accompany the implementation of an innovation culture.
- Talent management, diversity, leadership and internationalization.
- Consolidation of the operational model of human resources management.

Analysis of the 2017 results

Geographic distribution number of employees at the end of the year



	2017	2016
Total number of employees	15.375	15.502

Note: Does not include the number of people corresponding to discontinued operations amounting to 1,396 people in 2017 (1,727 people in 2016) nor the number of employees of the companies recorded under the equity method amounting to 819 people in 2017 (848 people in 2016).

Average age and length of service

	Years
Average age	44.1
Average length of service	14.7

Voluntary rotation index

	2017	2016
Voluntary rotation index	2.9	2.5

Employee rotation amounts to 6.4 in 2017 and 7.1 in 2016.

Training

	2017	2016
Total training hours	613,623	889,626
Corporate University participants	97,604	138,872
Percentage of staff taking part	93.7	87.4
Training hours per employee	38.4	51.0
Investment in training per person (€)	897	803

Note 1: There is a decrease in average hours per employee, and in general in all training indicators, for the consolidation of data from Chile, with a smaller training volume than the rest of the group and by reducing the number of transversal programs.
Note 2: Corporate University remained closed for three months for the implementation of the new corporate systems, therefore the final indicator of hours of training performed has been affected by this event.

Diversity and equality (%)

	2017	2016
People with disabilities integration index in Spain	2.57	2.42
Diversity men/women	71/29	71/29
Women in management posts	26.2	25.7

People management strategy

During 2017, the strategy of managing people at Gas Natural Fenosa focused on levers of cultural transformation, employee experience, strategic planning of people and new models of organizational performance.

Areas and levers of the people management strategy

Organizational performance	**Cultural development**	**Leadership and talent**
Smart simplicity	Cultural transformation	Strategic planning of people
- New organizational models - Evolution of people management processes	- Target culture - Evolution of people management processes - Role-modelling	- We take care of the experience - Diversity - Internationalization of the group profile - Strategic workforce planning
Extended workforce	Employee experience	Leadership
- Subcontracting borders - Model of relationship Gas Natural Fenosa-Suppliers - Occupational risk management	- Employee journey - Employer branding	- Employee journey - Employer branding - Meritocracy
Human resources operating model		
- HR analytics - CSC productivity		

Gas Natural Fenosa pretends to offer its employees stable, quality employment together with a solid, structured and attractive professional career, where 96% of the positions have open-ended contracts.

In this regard, we can highlight the fact that 84% of employees declare they have a high level of commitment to the company (Workplace Climate Survey 2017).

In 2017, the talent management cycle has been applied to all professionals that hold executive positions, and it has been integrated into the new talent management digital platform “Evolution”, based on SAP technology. In-class training sessions have taken place in all countries directed to guarantee experience in using the new platform and the understanding of the annual talent cycle.

Through the global talent management model, the company assesses professional skills, individual development plans, talent segmentation and internal mobility and promotion.

The model is implemented in all countries, with the aim of offering development opportunities for all professionals through customized learning actions, mobility, project assignment or by joining coaching and mentoring programs.

Internal mobility is a fundamental pillar of commitment to people and to that end employees have the possibility of internal mobility through the digital communication platforms.

For Gas Natural Fenosa it is essential to promote diversity and equal opportunities in an environment of respect, understanding and ongoing dialogue, with a special focus on the inclusion of individuals with various disabilities and extending this commitment to suppliers and collaborating companies.

In 2017, the company's commitment to diversity remained strong, consolidating the Integrated Diversity Plan (IDP) which brings together specific initiatives for people management, classified into three areas: gender, disabilities and age.

Gas Natural Fenosa continued to promote an appropriate work-life balance through a significant number of flexible employment measures, services and benefits adapted to employees' needs.

Compensation and remuneration

Gas Natural Fenosa's remuneration policy seeks to respond to 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 not included in the 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 Gas Natural Fenosa employees is supplemented with a social benefits system, which includes a join promotion pension plan, the main vehicle of funding post-employment commitments.

Internal communication with employees

The purpose of internal communication has the aim to contribute towards compliance with the company's strategic objectives based on growth, safety, leadership, innovation and the client as the focal point, supported through the different business areas and with the aim of contributing to increase the pride and the sense of belonging.

Gas Natural Fenosa has a range of channels to disseminate these messages, such as the corporate Intranet and the magazine Natural, which is distributed internationally. During 2017 we have been working on creating a new corporate channel for the informative contents which hitherto were disclosed on the Intranet, which will be called Naturalnews and the launch of which is scheduled for the beginning of 2018. This is a move towards communication that is more digital, with a friendly design, accessible through mobile devices, multi-language, interactive with new informative content to increase employees' satisfaction and encourage their participation and collaboration.

More than 950 news items were published in 2017 on Naturalnet along with some 40 videos with major participation by employees. The magazine Natural has also been redesigned to make it more attractive and supportive.

Yammer, the company's corporate social network, is growing more consolidated and already has almost 9,000 registered users at international level.

5.5 Health and safety

What resources are relevant for this undertaking?	How do we measure our performance?
Financial Manufactured Human Social	Accidents requiring medical leave Days lost Mortalities Frequency rate Severity rate Incidence rate

What does it mean for Gas Natural Fenosa? Risks and management approach

The activities of Gas Natural Fenosa are planned and developed taking into account the health, safety and well-being of people as a critical aspect of great relevance. Health and safety at work is a strategic and unwavering commitment at Gas Natural Fenosa, as reflected in its Code of Ethics, in the Corporate Responsibility Policy and the Human Rights Policy.

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.
- 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 work environment by integrating the prevention of occupational risks and actions to protect and promote health and well-being into business management.
- 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.

What are our main milestones in 2017?

- The introduction of the awareness program on health and safety “Journey to Safety for Collaborating Companies”.
- The implementation of the methodology for calculating accident indicators for collaborating companies.
- The implementation of the new management model of health and safety training in the global scope of the company.
- The introduction of preventive medicine at the company.
- The consolidation of the healthy business model in countries already certified, and achieving new certifications.

Analysis of the 2017 results

Accident indicators of employees and collaborating companies

	2017					
	Employees			Collaborating companies		
	Total	Men	Women	Total	Men	Women
Accidents requiring medical leave	45	40	5	491	459	32
Days lost	1,708	1,605	103	12,674	11,789	885
Mortalities	-	-	-	2	2	-
Frequency rate	1.3	1.65	0.49	4.41	4.87	1.88
Severity rate	0.05	0.07	0.01	0.11	0.13	0.05
Incidence rate	2.65	3.34	0.99	7.41	8.19	3.15

An overall decrease is recorded in all the indicators that strengthen the “Health and Safety Commitment” of the group:

- 31% decrease in accidents requiring medical leave and 24% decrease in frequency rate from 2016.
- 30 % decrease in days lost and 17 % decrease in the severity rate from 2016.
- 24% decrease in the incidence rate.

It is important to note that since the start of the Commitment, a 77% accumulate decrease has been recorded in the frequency rate (5.60 to 1.30), as well as since 2015 there have been no mortalities of own employees.

Health and Safety Strategy

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. It seeks to achieve a common culture in which all levels of the company, spearheaded by the Board of Directors, will acquire a firm commitment to continuous improvement in this area.

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:

Safety continues to represent the largest area of training at the company, with 159,475 hours, and extending the culture to collaborating companies is guaranteed through the 36,730 work inspections and supervisions that have been introduced as a mechanism to support compliance with the operational discipline.

Risk prevention

To ensure safety in the activities of Gas Natural Fenosa, measures aimed at preventing accidents and incidents have been introduced that are supported on these principles:

Gas Natural Fenosa 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.

In addition, Gas Natural Fenosa 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 Gas Natural Fenosa. Among other things, this plan that 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.

Communication to employees and action plans

The Health and Safety Commitment sets out as the main communication objectives the reinforcement of the commitment and acknowledging the effort. These two communication objectives have been introduced through the following actions:

- Putting the focus on the risk of falls at the same level, raising awareness of road safety and the safety of collaborating companies.
- Providing value-added to the employee through participatory actions.
- Giving prominence to the employee through recognition.

Training and awareness

Gas Natural Fenosa has looked for a cultural change achieved at the company in recent years in health and safety issues is largely through the efforts made in providing quality training, both for our own employees as well as collaborating companies.

Certifications

Throughout 2017, there were a total of 42 internal audits conducted by qualified auditors and 32 external audits of the management system pursuant to OHSAS 18001. Additionally, this year, we introduced an internal audit system that allow to analyze the degree of implementation of the Health and Safety Commitment in each of the company’s business.

Safety in facilities and processes

Industrial risk management is included in the preventive activity of Gas Natural Fenosa. In risk management, its main objectives are the detection and minimization of risks affecting activities, products and services that may have an effect on the company's facilities or its environment, causing economic, environmental and social damages.

In addition, in 2017, safety audits were carried out of the company’s different technical processes to verify compliance with the prevailing rules and regulations of the country, of the technical procedures established by the group and the business unit’s own internal regulations. We also review the monitoring and control of operational risks relating to technology, accidents and breakdowns and impacts on the environment, and relevant management parameters. The main goal is to bring value to the business lines and assist in the continuous improvement of processes.

Health

Gas Natural Fenosa is firmly committed to offering its employees a healthy working environment and well-being. The Comprehensive Medical and Health Assistance Unit contributes to achieving this goal.

Defines the strategic guidelines and establishes the general framework for action of Gas Natural Fenosa in the field of healthcare, ergonomics and psycho/sociology.

Master Health Plan targets	
Standardized actions	Ensuring the health of workers, developing standardized 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.

5.6 Responsible supply chain

What resources are relevant for this undertaking?

Financial
Manufactured
Human
Social

How do we measure our performance?

Total number of suppliers
Total purchase volume awarded
Assessment of suppliers ESG
Number of critical supplies
Official-approval suspended suppliers

What does it mean for Gas Natural Fenosa? Risks and management approach

Suppliers and collaborating companies are key players in the optimum performance of the value chain of Gas Natural Fenosa, and the company therefore pretends to promote long-term relations, based on trust, that are stable, sound and of mutual benefit, under the principles of risk efficiency and management.

What is our commitment?

- Extending the culture of Gas Natural Fenosa to the supply chain, passing on the target of excellence in service 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 Gas Natural Fenosa in the supply chain, in particular in the area of human rights, ethics and health and safety.
- Promoting procurement of suppliers from the country or region where the company carries out its activities, helping to generate a positive social impact.
- Ensuring fairness, independence and transparency in the procurement process.

- Promoting the development of suppliers by identifying opportunities for collaboration and innovation and encouraging a climate of transparent communication, to guarantee that partner companies satisfy the group's standards of Corporate Social Responsability, quality, safety and service.

What are our main milestones in 2017?

- Finalisation of the implementation of the supplier classification process in the entire group
- Finalisation of the extension and implementation of the Bravo platform at the main subsidiaries

Analysis of the 2017 results

The company therefore promotes long-term relations based on trust, under the principles transparency, objectivity and risk management.

	2017	2016
Total number of suppliers	9,877	12,072
Total purchase volume awarded (millions of euros)	3,428	3,599
Assessment of suppliers ESG [1]	4,758	1,556
Number of critical supplies	2,457	1,556
Official-approval suspended suppliers	7	15

[1] Enviromental Social and Governance

Management of the supply chain

The management of the supply chain is based on application of unified and universal contractual conditions for the entire scope of action:

- Code of ethics applicable to procurement processes.
- Classification of suppliers in accordance with what they can supply and the level of risk that this supply involves.
- Monitoring of the requirements set out in the contractual conditions given to suppliers that are awarded contracts and of the service levels actually provided.
- Evaluation of the performance of suppliers awarded contracts to obtain an objective assessment of suppliers that can be used for subsequent bidding processes, actions for improvement and development of suppliers.

Gas Natural Fenosa actively participates at associations and 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, Colombia, Spain and Italy. Furthermore, the company subscribes to the worldwide Procurement Leaders network and in 2017 took an active part in the CPOnet Congress. It is also a member of the Procurement Leadership Council, an initiative led by the Corporate Executive Board.

Stages in the supply chain management process:

1. Contractual model: Universal and unified contractual conditions for the company's entire scope of action. Code of ethics applicable to the procurement processes, set out in the Supplier Code of Ethics, based on principles of transparency, traceability, auditing capability and fairness.

2. Classification and approval process: Classification of suppliers in accordance with the purchase category that are able to supply and the level of risk that this supply involves. The results of this process is the supplier tree that pools together all suitable suppliers to take part in the different bids according to their different risk levels. The processes that require approval are determined according to Quality, Health and Safety, Environmental, Social and Governance and Operational risk factors, to searching to ensure that suppliers comply with the requirements requested.

3. Contractual compliance and documentary management: Monitoring and analysis of the performance of suppliers from different points of view, to obtain an objective assessment of suppliers that can be used for subsequent bidding processes and actions for improvement and development of suppliers.

4. Performance evaluation: Monitoring and analysis of the performance of suppliers from different points of view, to obtain an objective assessment of suppliers that can be used for subsequent bidding processes and actions for improvement and development of suppliers.

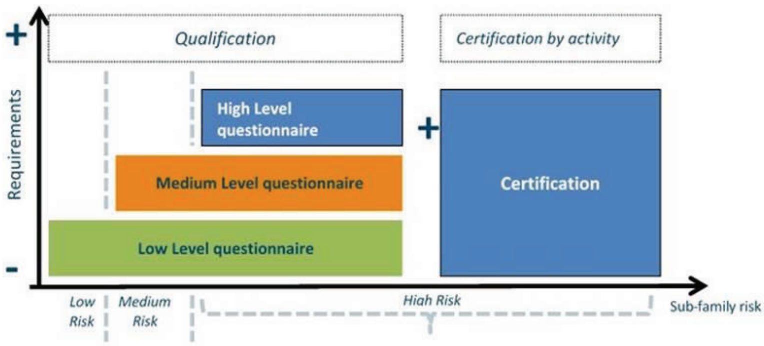
5. Development of suppliers: Introduce strategic relations that facilitate opportunities for partnership and improvement in products and services supplied.

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 Gas Natural Fenosa.
- 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.
- Operational risk: The potential impact on operations incurred by Gas Natural Fenosa 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

Supplier assessment at Gas Natural Fenosa comprises the business classification of the supplier and the approval process of the supplier for the supply. Both processes are based on the procurement sub-family risk map.



Regarding the process of supplier classification, during 2017 extended the new supplier classification model introduced in Spain, Brazil, Colombia, Italy and Chile to the subsidiaries in Argentina, Mexico and Panama, set to come into operation at the beginning of 2018.

Audits are carried out in the process of approval and monitoring of active suppliers. The audits, in situ or remote, check compliance with the specific requirements defined for the service or material of categories classified as high level in any of the risk factors.

For service providers, surveys are conducted with units of Gas Natural Fenosa to measure their satisfaction with suppliers. In 2017, these surveys were conducted with suppliers that have performed relevant or key activities in the company's processes, and mainly focused on activities classified as high risk in health and safety. Surveys were conducted in Argentina, Brazil, Colombia, Spain, Italy, Mexico, Moldova and Panama.

5.7. Social commitment

What resources are relevant for this undertaking?	How do we measure our performance?
Financial Manufactured Human Social	Economic value distributed Social action investment

What does it mean for Gas Natural Fenosa? Risks and management approach.

Gas Natural Fenosa is committed to the economic and social development of those regions where it performs its activities, searching to provide expertise, management capacity and creativity, as well as spending part of its profits on social investment. The company tries, through fluid and ongoing dialogue with society, to be aware of the expectations and interests of those communities where it operates and thus be able to involve itself in their development, seeking to give a more appropriate response to their needs.

What is our commitment?

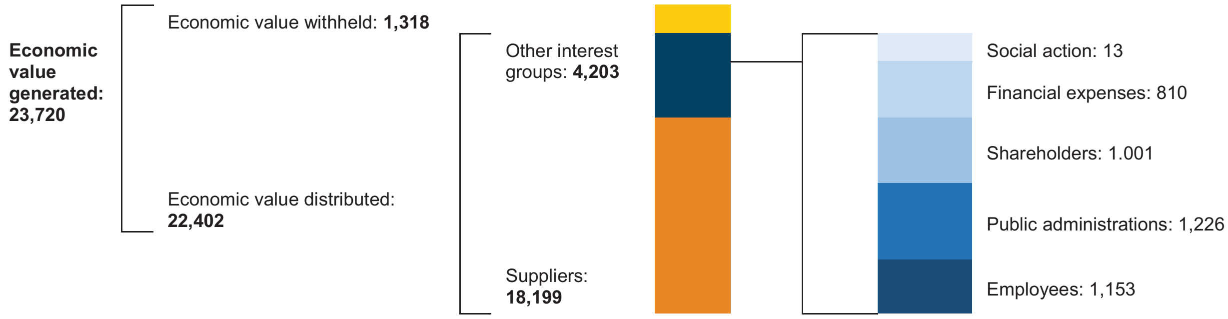
- Guarantee fluid and two-way dialogue and to encourage involvement in local communities, respecting the culture, rules and the environment, so that their concerns are responded to appropriately and expeditiously.
- Assess the social impact that the company’s activity could cause, to avoid or mitigate the adverse effects these could generate and to foster positive effects.
- Develop initiatives within the venture philanthropy framework 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 to use the necessary and/or existing mechanisms as a vehicle for transmitting the service quality levels to collaborating companies and suppliers.

What are our main milestones in 2017?

- Launch of the fourth edition of CINERGÍA.
- Review and update of the General Regulations on Sponsorship and Donations.
- Consolidate the activity of the Gas Natural Fenosa Foundation in Chile.
- The introduction, in partnership with the Gas Natural Fenosa Foundation, of the pilot program targeted at groups that are vulnerable to energy poverty.

Analysis of the 2017 results

Economic Value Distributed. Detail by group of interest (euros millions)



Economic contributions

Economic contributions to social investment programs are another important part of the Gas Natural Fenosa commitment. In 2017, they totalled 12.9 million euros.

	Million euros
Social action investment	**12.9**

Creation of wealth and well-being where the company operates

Gas Natural Fenosa develops its commitment to society through four main lines of action that are aligned with the company's core activities.

1. Access to energy

Gas Natural Fenosa performs its activity in areas where the energy supply does not reach the entire population. The company considers it very important to reach the people that live in these areas. This is why it actively works in developing its distribution networks.

The project carried out at Cuartel V in Argentina or in Chile made it possible to provide access to clean and reliable energies to tens of thousands of people. Among the initiatives introduced by the company, we can highlight the integral gas supply model in Argentina, providing vulnerable customers with access to energy in Brazil, Mexico and Spain.

In addition, the company has developed a Vulnerability Plan for the protection of vulnerable customers, in Spain, to prevent supply cut-off to customers that the municipal social services have reported as vulnerable.

To do this, Gas Natural Fenosa has launched a specific package of 20 measures with a financial endowment of 4.5 million euros and a team of 60 employees. The initiatives are both of an operational and social nature, allowing us to conduct comprehensive monitoring and development towards energy vulnerability.

2. 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. The programme was once again successfully carried out in Argentina, Brazil and Colombia, and Mexico and Panama began to develop it for the first time.
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. On discovering that the majority of Latin America countries were performing corporate volunteer actions related to caring for the environment and the planting of trees, the COIL Social Investment designed the Sowing the Future programme. As regards the Responsible Consumption programme, we continued using the Natural Family, in all the group's subsidiaries in Latin America, to transmit the contents of this programme in an educational and fun way for both children and adults.
Talent promotion	This pillar promotes projects that foster the studies and access to employment for the children and relatives of collaborators: "Training for Leadership", “Planning your Future", "Natural Vocation" and "Summer Internship".

3. Relationship with communities

Gas Natural Fenosa, under its Policy on Human Rights, makes a firm commitment to the respect of local communities. To achieve this commitment, the social impact that company activities may have on affected communities and contributing to improving the living conditions of these communities are key aspects.

Gas Natural Fenosa 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.

4. Patronage and sponsorship

Gas Natural Fenosa provides one-off economic support to specific sponsorship projects and donations.

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.

- Social action focused on underprivileged groups
- Promotion of music, theatre and films. In 2017 we launched the fourth edition of Cinergía, to bring energy saving closer through the cinema and to encourage talent in the Spanish film industry.
- Fostering cultural enrichment: The Gas Natural Fenosa Museum of Contemporary Art (MAC) has consolidated itself as a cultural benchmark in Galicia, where it is based, and in Spain.

Corporate volunteers and employee participation

Through corporate volunteering, Gas Natural Fenosa aims to promote social cohesion, values and a spirit of solidarity. To achieve this programme objectives have been defined the in three areas simultaneously - corporate, employees and the environment-, and an integrated structure of committees that includes both the areas of persons as well as communication and the environment of all countries that form part of the programme.

Throughout 2017, employees have spent more than 7,004 hours volunteering, featuring participation by 1,649 employees worldwide. Worldwide, a total of 22 environmental volunteer actions, 45 social volunteer actions were carried out along with 1 energy volunteer action, in which employees contributed their time and their personal and professional skills.

This programme is of a global nature and involves seven countries where Gas Natural Fenosa has a presence: Argentina, Brazil, Spain, Mexico, Moldova, Panama and the Dominican Republic.

Gas Natural Fenosa Foundation

The Gas Natural Fenosa Foundation 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 with a particular focus on actions targeted at relieving energy vulnerability. In the cultural sphere, it performs actions targeted at both preservation and dissemination of the historic heritage of the gas and electricity sector, through the Gas Museum and the Bolarque Museum, as well as dissemination and artistic stimulation of society, through the multidisciplinary space of the Museum of Contemporary Art, in A Coruña.

During 2017, the foundation held 19 seminars on energy and environment in Spain, with 2,265 participants. It has also forged ahead with the "First Export Programme", with a total of 13 seminars in a number of different autonomous regions across Spain, which were attended by 1,475 people. It also offered customised assessment to 13 companies.

It also has an educational programme for schools and performs activities for children, adults and families. The activities are spread throughout Spain, which has involved 51,000 students and has had more than 150,000 users.

As regards the Energytruck, in its second year it has already visited 208 Spanish municipalities and has travelled more than 51,200 km nationwide.

The international activities of the foundation were developed in nine countries: Argentina, Algeria, Brazil, Chile, Colombia, Costa Rica, Mexico, Morocco and South Africa. 15 programmes were developed, which benefited more than 50,500 people and more than 1,600 companies and institutions.

5.8 Integrity and transparency

What resources are relevant for this undertaking?	How do we measure our performance?
Financial	Number of employees trained in Human Rights
Human	Correspondence received concerning the code of ethics
Social	Fiscal contribution

What does it mean for Gas Natural Fenosa? Risks and management approach.

Gas Natural Fenosa considers that the trust of its customers, its professionals, suppliers and external collaborators, shareholders, investors and funders, regulatory bodies and other market agents and social groups, 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.

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 respecting and 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 UN Guiding Principles on Business & Human Rights, and the OECD Principles of Corporate Governance.
- Act with responsibility in business 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, not to allow 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 actions and initiatives and to offer a specific response to the information required by the company's stakeholders.

What are our main milestones in 2017?

- Disseminate and communicate our Corporate Hospitality Policy
- Finalize the process of declaration of the Anticorruption Policy
- Update the Human Rights Policy text to concepts and terminology of the UN Guiding Principles on Business & Human Rights

Analysis of the 2017 results

Number of employees trained in Human Rights	2017	2016
Number of persons trained on Human Rights	10,132	10,180

Correspondence received concerning the code of ethics	2017	2016
Queries	37	58
Notifications	104	120
Total	141	178

The number of communications received per 200 employees in 2017 amounted to 1.67 (1.92 in 2016).

The Code of Ethics of Gas Natural approved by the Board of Directors, is the document that establishes guidelines that must govern the ethical behavior of managers and employees of Gas Natural Fenosa, 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.

Gas Natural Fenosa has an Anticorruption 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.
In 2017, 2% of the notifications received were related to alleged fraud, none of which had any significant impact.

29% of the notifications were related to “Respect for people" chapter of the Code of Ethics, and they were all solved appropriately. None of them were related to discrimination.

Gas Natural Fenosa expects a high level of commitment in fulfilling its Code of Ethics and Anticorruption Policy of all its employees. Therefore, emphasis is placed on transmitting a culture of integrity of the company. Its breach is analysed according to internal procedures, legal regulations and existing agreements.

During 2017, we managed various disciplinary situations from complaints made to the Code of Ethics Committee, or from situations covered in the Code of Ethics or the Anticorruption Policy. In total, 3 misdemeanours, 4 serious offences and 17 very serious offences, of which 13 have resulted in dismissals through breach of the Code of Ethics, were handled.

The Code of Ethics Committee also has a multi-year work plan, which includes actions in the short- and medium-term, with the ultimate goal of extending the code to the highest possible number of activities and people at the company.

The company set up local committees in Argentina, Brazil, Colombia, Chile, Italy, Mexico, Moldova, Panama and South Africa.

In 2017, the Code of Ethics Committee held five working meetings, and the local committees held 29.

Protocol of Investigation and Response to irregular conduct and fraud

The protocol defines the action procedure and system to ensure that any notification from any employee, supplier or external partner of Gas Natural Fenosa concerning allegedly irregular or fraudulent conduct can be formulated and reported in a safe and confidential way in compliance with prevailing legislation, as well as the system for establishing all of the procedures required to enable an efficient investigation into irregular conduct and fraud reported.

The Gas Natural Fenosa reporting channel, through which all the employees and suppliers can send the Code of Ethics Committee queries or notify breaches of the code, in good faith, in a confidential manner and without fear of reprisal.

Crime Prevention Model

The company has a Crime Prevention Model that is updated every year, and which incorporates the control structure that already exists at Gas Natural Fenosa to efficiently prevent the occurrence of criminal offences set out in Organic Law 5/2010 on reform of the Penal Code.

From an organisational standpoint, the Board of Directors has assigned the functions of Autonomous Body, described in Organic Law 1/2015, to the Compliance Assessment Committee, which is responsible for taking significant decisions in relation to the regular monitoring and oversight of the working and compliance with the Crime Prevention Model.

The model contains 21 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.

Each year, the model is assessed by an independent third party. In 2017, it issued a satisfactory report on its design and effectiveness.

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 Gas Natural Fenosa Anticorruption Policy complies with national and international legislation on corruption and bribery, and mainly that dictated by the Spanish Penal Code.

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 Gas Natural Fenosa with regard to the prevention, detection, investigation and correction of any corrupt practice within the organisation.

The policy establishes fourteen 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 Gas Natural Fenosa Anticorruption programme covers three key areas:

- Establishment of an antifraud and anticorruption 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.

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 counterpart 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.

In the security area, in 2017 there were 7,010 investigation and antifraud cases of action that took place in Argentina, Brazil, Colombia, Spain, Mexico, Moldova and Panama.

<u>Tax policies</u>

Tax strategy and Policy for controlling and managing tax risks

At a meeting on 9 January 2018 the Board of Directors adopted the Tax strategy and Policy for controlling and managing tax risks, which sets out the basic principles guiding Gas Natural Fenosa's tax function and the main lines of action to mitigate tax risks and guide proper oversight of same.

The basic principles underlying the tax strategy of Gas Natural Fenosa are as follows:

- Responsibility in fulfilling tax obligations.
- Low tax risk profile.
- Adoption of tax treatments for economic reasons.
- Transparency in tax information.
- Cooperation with the tax authorities.

The main lines of the Policy for controlling and managing tax risks are as follows:

- Clearly defined tax-related governance.
- Tax risk oversight procedures derived from Compliance.
- Procedures for assessing and exercising oversight over grey areas.
- Supervision of the Tax Control Framework
- Regular reports to the Board of Directors on the tax situation.

All of Gas Natural Fenosa's tax policies are aligned with:

- Gas Natural Fenosa's Corporate Responsibility Policy, which establishes that 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."
- Gas Natural Fenosa'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."
- Code of Best Tax Practices, adopted on 20 July 2010 in plenary session by the Foro de Grandes Empresas, a body established by the Spanish Internal Revenue Service with the country's largest companies, including Gas Natural SDG, S.A. That Code contains recommendations from the tax authorities, which have been adopted voluntarily by Gas Natural Fenosa, with the aim of improving the application of the tax system by enhancing legal certainty, reducing litigation, fostering reciprocal cooperation based on good faith and legitimate trust, and the application of responsible tax policies.

To align that Gas Natural Fenosa's tax practices with those principles, the group has a General Standard governing the Tax Control Framework that has been designed in accordance with the guidelines of the Organization for Economic Cooperation and Development (OECD) for multinational companies, as well as for the design and implementation of a Tax Control Framework.

Gas Natural Fenosa also has a Risk Map that specifically identifies tax risks and disputes about the interpretation or application of tax law. The main issues of significance for tax purposes are detailed in Note 21 ("Tax situation") to the Consolidated Financial Statements.

Tax havens

The creation or acquisition of interests in entities domiciled in countries or territories that are designated as tax havens must be reported to the Board of Directors through the Audit Committee.

In accordance with the Spanish regulations that determine which countries are considered to be tax havens (Royal Decree 1080/1991, of 5 July, and Royal Decree 116/2003, of 31 January), Gas Natural Fenosa has only two holdings in companies incorporated in such territories, which were in process of redomiciliation or liquidation:

- A 95% stake in Buenergía Gas & Power, Ltd., domiciled in the Cayman Islands. This is a company that indirectly owns a stake in just one industrial holding: Ecoeléctrica, S.A., the company that generates electricity using a combined cycle plant in Puerto Rico; the latter is taxed in Puerto Rico and Gas Natural Fenosa does not obtain any tax advantage from this arrangement. On 2 february 2018 the change of registered office to Puerto Rico has been completed, which is in public registry process.

- The 52.2% stake in Gasoducto del Pacífico (Cayman), Ltd., domiciled in the Cayman Islands. This is a dormant company that was acquired by the group as a result of the acquisition of the CGE group and does not provide any tax advantage to Gas Natural Fenosa. The company was fully liquidated on 12 January 2018, and it will be dissolved once it is struck off the public record within three months from that date.

The only intercompany transactions with those companies in the year 2017 are dividends received, as follows:

Recipient	Distributor	Amount (Euros thousand)
Global Power Generation, S.A.	Buenergía Gas & Power, Ltd.	49,504

Tax contribution

Gas Natural Fenosa gives priority to fulfilling its obligation to pay the taxes that are due in each territory in accordance with the applicable regulations.

Gas Natural Fenosa's total tax contribution amounted to Euros 3,272 million in 2017 (Euros 3,419 million in 2016). 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):

Country	Own taxes						Third-party taxes								Total	
	Income tax (1)		Others (2)		Total		VAT		Tax on hydrocarbons		Others (3)		Total			
	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016	2017	2016
Spain	112	199	537	512	649	711	845	1,007	342	352	228	229	1,415	1,588	2,064	2,299
Argentina	15	10	67	42	82	52	19	13	-	-	34	22	53	35	135	87
Brazil	51	38	67	49	118	87	74	58	-	-	7	9	81	67	199	154
Colombia	60	75	57	78	117	153	-	7	-	-	11	14	11	21	128	174
Chile	101	42	11	11	112	53	81	117	-	-	22	18	103	135	215	188
Mexico	66	31	4	3	70	34	57	39	-	-	19	11	76	50	146	84
Panama	10	89	9	7	19	96	-	-	-	-	4	3	4	3	23	99
Rest of LatAm	8	12	1	1	9	13	4	2	-	-	4	3	8	5	17	18
Total LatAm	311	297	216	191	527	488	235	236	-	-	101	80	336	316	863	804
Italy	4	19	7	7	11	26	27	27	35	42	5	5	67	74	78	100
Remainder	11	10	28	23	39	33	143	128	76	49	9	6	228	183	267	216
Total	**438**	**525**	**788**	**733**	**1,226**	**1,258**	**1,250**	**1,398**	**453**	**443**	**343**	**320**	**2,046**	**2,161**	**3,272**	**3,419**

(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 Euros 260 million in 2017 (Euros 244 million in 2016), local taxes, employer social security contributions and other specific taxes in each country.

(3) Includes basically employee withholdings and employee social security contributions.

Human Rights Policy

Since 2011, Gas Natural Fenosa has a Human Rights Policy approved by the Management Committee. The policy has been developed and approved in response to society's growing demands. It is particularly applicable in locations in which local legislation does not provide a sufficient level of protection for human rights.

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 UN Guiding Principles on Business and Human Rights.

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. Towards the end of 2017, the course had been completed by 10,132 people.

6. Forecast Group performance

6.1. Foundations of strategy

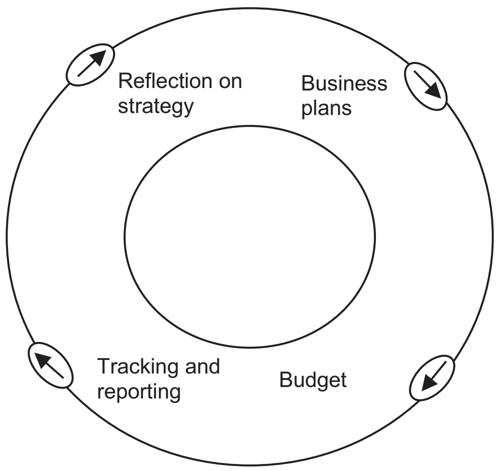
In order to achieve its goals, Gas Natural Fenosa defines medium-term strategies that are updated regularly to adapt to the current and future situation, taking account of the specific features of the company's various lines of business.

The strategic planning cycle is defined as a recurring process that starts from a reflection on strategy, is materialised in each business and corporate unit's business plans and is integrated into the group's integrated business plan.

Energy planning cycle

Reflection on strategy
- Formal adoption of the group's medium-term vision.
- Top-down approach.

Business plans
- Formal statement of goals for the business and corporate units.
- Bottom-up approach. Integrated business plan.
- Formal statement of goals for the group, integrating the business plans.



Tracking and reporting
- Single source of management information for the group and the business and corporate units.
- Strategic information management to support decision-making.

Budget
- Operations budget.
- Capex budget.

Coordination of the strategic planning, annual budgeting and continuous tracking processes facilitates agile and effective decision-making.

6.2. Gas Natural Fenosa strategy framework

The company's strategic vision for 2016-2020 adopted a number of commitments for 2018 and aspirations for 2020 and defined the outlook for the business areas and financial goals for the group in that period. Gas Natural Fenosa plans to present is 2018-2020 Strategic Plan, with updated targets for the group.

The key components of Gas Natural Fenosa's Strategic Plan are:

Framed by tracking of the business environment, the strategic plan establishes:

- Business management model and objectives.
- Execution of a new efficiency plan.
- Continuous management of the business portfolio and its strategic fit.

The strategic plan is materialised in the form of business plans.

6.3. Group outlook

The Strategic Vision 2016-2018 was grounded in three growth areas (networks, power generation and gas supply), the goal being to enable Gas Natural Fenosa to continue expanding in the future:

- Networks: in the area of gas, investment in gas networks in Chile and Mexico, entry into the gas distribution business in the Arequipa (Peru) region, new licences and additional growth as a result of conversion of the new liquefied petroleum gas (LPG) connection points in Spain; in the area of electricity, investment in smart grids in Spain, investments to meet additional demand in Chile and Panama, electricity subtransmission in Chile driven by new renewable energy projects.

- Electricity generation: improve generating fleet efficiency and performance by adding 3,500 MW overall; 2,500 MW in renewables (Spain and other countries) and 500-1,000 MW in CCGTs that will contribute to developing the downstream LNG business. Growth and development of the international power generation business via GPG.

- Gas supply: new gas procurement contracts totalling about 11 bcm in the two Cheniere projects (Sabine Pass and Corpus Christi) and the Yamal LNG project in Russia; additionally, existing gas supply contracts will be adapted and renegotiated to reflect benchmark market conditions. The LNG carrier fleet will be expanded by four vessels (two of which were added in 2016) and a mobile regasification unit. Because of their larger size, they represent almost 1 million cubic metres of additional capacity. EBITDA is expected to increase by around 10%.

The Strategic Plan 2018-2020 will update the strategies to be implemented to ensure that Gas Natural Fenosa maintains the trend of organic growth in 2018 and subsequent years.

7. Sustainable innovation

Risks and management approach

Gas Natural Fenosa, in order to address the new challenges and opportunities posed by the business environment, has promoted the implementation of a model of innovation that seeks to respond to the technological changes that the sector is facing and a strong innovative culture at the company

Analysis of the 2017 results

Innovation overview

Below we detail the 5 major blocks into which the company has structured its innovation activities:

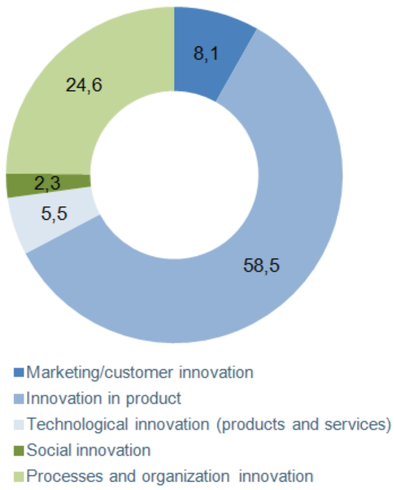
- Social Innovation. The company has been working to mitigate situations of energy vulnerability since 2014 with prevention actions, through agreements with local and regional governments, and activities to raise awareness with participation on forums and chat groups about poverty. These actions intensified during 2017 through the Vulnerability Plan.
- Marketing Innovation. This particular line encompasses all of the company's efforts to find out the actual and specific needs of each one of its customers, and to make sure that they have at their disposal cutting-edge products that help them in their day-to-day life. One of the major initiatives within this kind of innovation is the CEX (Customer Experience) project through which the company introduces a new methodology in which the customer is the starting point and the centre of activity.
- Organisational Innovation. In this framework we consider those actions targeted at covering the needs that arise with regard to new business models, those that have entailed a new organisation in the work and those that have been for the purpose of minimising risks and increasing quality and safety in the organisation's practices.
- Innovation in Product. Here, we can highlight the PIDIM (Smart Platform for the Sizing and Design of Multigeneration Facilities) project for the purpose of designing, developing and introducing facilities for the distributed generation of heating and cooling electricity that operates in the cloud by receiving data such as the customer's consumption. With this initiative we aim to promote the energy rehabilitation of

buildings and to characterise the energy demand of these buildings to calculate the baseline of consumption of the building and to forecast savings. In this sphere we should also highlight development of the Sustainable Logistics Train (SLT) in the quest for a feasible and economic solution for the sustainable management of the so-called "last mile" logistic, where the dissemination of services for customers is often in places where there is restricted traffic access.

- Process Innovation. We can point to the Integrated Control Centre (ICC) of hydraulic facilities, headquartered in A Batundeira (Velle - Ourense), which allows centralised and remote control management of the exploitation, operation and maintenance of all the company's power plants and dams in Spain.

The overall figure in 2017 for investment in innovation totalled 99 million euros, divided as follows:

Investment in innovation (millions of euros)



(Euros millions)	2017
Investment in innovation	99

Innovation Plan

The Innovation Plan is structured by five multidisciplinary working networks and eight technological innovation areas.

Liquefied Natural Gas (LNG)

Gas Natural Fenosa develops innovation projects in three areas of action: optimization of the LNG logistics chain (Small Scale), development of LNG as a cleaner and more efficient transport fuel (Bunkering) and development of the LNG Measure.

One key project is the DirectLink LNG – Floating Universal Transfer System (UTS), developed during 2016 and 2017. This is an integral patented solution for the transfer and bunkering of LNG from ship to shore, an alternative to the costly traditional infrastructures (port and jetties) and with minimum environmental impact.

Generation

Renewables and storage

Gas Natural Fenosa develops innovation projects in four areas of action:

- Renewable energy: a commitment to a balanced energy mix so that the emission-free generation technologies and the low-emission technologies represent a significant volume of the total installed capacity.
- Wind energy: with initiatives to monitor the condition of the assets, through measurement systems, smart models and data maintaining and optimizing the performance of the facilities through the implementation of improvements or tests.
- Hydraulic energy: a commitment to the introduction of new technologies both in areas of environmental control as well as in the establishment of mobility systems and remote monitoring, without overlooking improved performance of its hydraulic facilities.
- Storage: focusing on an even greater increase in quality and reliability of supply, on developing joint solutions with customers and also on allowing a greater and easier integration of renewable-source electricity into the grid.

Highlights the project Windex, developed in 2017, which involves application of sensor systems and development of information-processing tools to increase the useful and structural life of wind farms in a safe way.

Reduction of emissions and energy efficiency

The company is carrying out a range of technological developments at its facilities. In addition, the company continues to work to improve the efficiency of its coal and combined-cycle plants.

Highlights the project Optimisation of fuel through lasers, developed during 2017 which helps to significantly reduce NO_x at the Meirama Thermal Power Plant.

Grids

The company's commitment is two-fold of acting.

- Revitalisation of gas networks: where challenges focus on achieving greater automation of the grid (remote action, reduction of cut-offs and interruptions, improved operational efficiency and maintenance and increased energy performance) and greater interaction with the customer (energy efficiency and active management of demand).
- Electricity grids 4.0: focusing on digitalisation of the electricity distribution grids, moving forward in the management of operation and maintenance of the grid, and integrating the customer into the information flows, whilst simultaneously improving the levels of safety at work and the quality of supply.

Customer

Gas Natural Fenosa has two action lines open in the field of innovation associated to the customer.

- Smart Client: focusing on providing products and services with high value-added for different types of end customers. This Innovation area promotes initiatives based mainly on three core actions: GEDIS and Self-consumption, Integration of new solutions and Data Analytics.
- Energy efficiency and mobility.

One of the most important projects is the Remote Building Analytics Platform, based on the development of an energy management tool (virtual audit) for customers of the SMEs market. Data from smart meters are fed into the tool and these data allow us to define specific segmentation of customers for the purpose of proposing energy efficiency measures and actions en masse.

Automation and management of information

It is a cross-sectional area that aims to bring together projects already being developed in the company to gain synergies and enhance results.

Highlights the project Energy Harvesting UP4, which consists in testing the concept at laboratory level of a device based on a sheet of piezoelectric material to generate small amounts of electricity. The device is put into a gas tube and energy is produced through the flow interaction structure. The aim is to capture energy to feed sensors that will be installed in the gas network.

Annex I. Additional information

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.

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%.

Movements during 2017 and 2016 involving the treasury shares of Gas Natural SDG, S.A. are as follows:

	Number of shares	**Euros million**	**% Capital**
At 1 January 2016	-	-	-
Acquisitions	3,049,189	53	0.3%
Disposals	(2,298,644)	(40)	(0.2%)
At 31 December 2016	**750,545**	**13**	**0.1%**
Acquisitions	7,623,586	147	0,8%
Delivered to employees	(336,625)	(7)	-
*Disposals	(8,037,506)	(153)	(0.8%)
At 31 December 2017	**-**	**-**	-

In 2017, the profit on transactions involving treasury shares of Gas Natural Fenosa amounted to Euros 0.5 million, recognised under “Other reserves” (Euros 0.4 million profit in 2016).

Note 13 of the Notes to the Consolidated Financial Statements contains all the information on treasury shares.

2. 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:

	2017	**2016**
	Amount	**Amount**
Total payments	12,256	11,533
Total payments outstanding	403	417
Average supplier payment period (days) (1)	25	28
Transactions paid ratio (days) (2)	24	27
Transactions pending payment ratio (days) (3)	34	30

(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.

3. Subsequent events

Events subsequent to the end of the period are described in Note 38 of the Notes to the Consolidated Financial Statements.

Annex II. Alternative performance metrics

Gas Natural Fenosa'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 chosen APMs are useful for persons consulting the financial information as they allow an analysis of the financial performance, cash flows and financial situation of Gas Natural Fenosa, and a comparison with other companies.

Below is a glossary of terms with the definition of the APMs. Generally, the APM terms are directly traceable to the relevant items of the consolidated balance sheet, consolidated income statement, consolidated statement of cash flows or Notes to the Financial Statements of Gas Natural Fenosa. To enhance the traceability, a reconciliation is presented of the calculated values.

tive performance metrics	Definition and terms	Reconciliation of values at 31.12.2017	Reconciliation of values at 31.12.2016	Relevance
Ebitda	"Operating gross profit"(2)	Euros 3,915 million	Euros 4,664 million	Measure of earnings before interest, taxes, depreciation and amortisation and provisions
Cash Flow from Operating Activities (CFO)	"Operating cash flows"(3) before "changes in working capital"(3)	Euros 2,923 million = 2,768 + 155	Euros 3,370 million = 3,375 - 5	Operating cash flow
Net capital expenditure	"Investment in intangible assets" (4) (Note 5) + "Investment in property, plant and equipment"(4) (Note 6) + Financial investments – Receipts for divestment of property, plant and equipment and intangible assets – Other investing receipts/(payments) (6)	Euros 1,597 million = 389 + 1,393 + 44 – 229	2,225 millones de euros = 402 + 2.115 + 384 -667	Total investments net of the cash received from divestments and other investing receipts
Gross financial debt	"Non-current financial liabilities"(1) + "Current financial liabilities"(1)	Euros 18,459 million = 15,916 + 2,543	Euros 17,602 million = 15,003 + 2,599	Current and non-current financial debt
Net financial debt	Gross financial debt(5)– "Cash and cash equivalents"(1) – "Derivative financial assets"(4) (Note 8)	Euros 15,154 million = 18,459 - 3,225 – 80	Euros 15,423 million = 17,602 – 2,067 - 112	Current and non-current financial debt less cash and cash equivalents and derivative financial assets
Leverage (%)	Net financial debt(5) / (Net financial debt(5) + "Net equity"(1))	45.3% = 15,154 / (15,154 + 18,305)	44.8% = 15,423/(15,423 + 19,005)	The ratio of external funds over total funds
Cost of net financial debt	"Cost of financial debt"(4) (Note 30) – "Interest revenue"(4) (Note 30)	Euros 611 million = 630 - 19	Euros 735 million = 763 - 28	Amount of expense relative to the cost of financial debt less interest revenue
Ebitda/Cost of net financial debt	Ebitda(5)/ Cost of net financial debt(5)	6.4x = 3,915 / 611	6.3x = 4,664 / 735	Ratio between EBITDA and net financial debt
Net financial debt/ Ebitda	Net financial debt(5) / Ebitda(5)	3.9x = 15,154 / 3,915	3.3x = 15,423 / 4,664	Ratio between net financial debt and EBITDA
ROA (return on assets) (%)	"Profit attributed to the parent company"(2) / "Total assets"(1)	2.9% = 1,360 / 47,322	2.9% = 1,347 / 47,114	Ratio measuring the return on assets
Market capitalisation	No. of shares ('000) outstanding at end of period(6) * Market price at end of period(6)	Euros 19,263 million = 1,000,689 * Euros 19.25	Euros 17,922 million de euros = 1,000,689 * 17.91 euros	Measure of the company's total value based on its share price
Earnings per share	"Attributable income in the period"(2) / Average No. of shares in the period (in thousands)(6)	Euros 1.36 euros = 1,360 / 1,000,478	1.35 euros = 1,347 / 1,000,468	Ratio between the income attributed to the parent company and the number of shares
Price-earnings ratio (P/E)	Closing share price / Earnings per share (6)(6)	14.2x = 19.25 / 1.36	13.3x = 17.91 / 1.35	Ratio between the share price and earnings per share
Enterprise value (EV)	Market capitalisation(5) + Net financial debt(5)	Euros 34,417 million = 19,263 + 15,154	Euros 33,345 million = 17,922 + 15,423	Measure of the company's total value based on its share price plus net financial debt
EV/Ebitda	Enterprise value(5) / Ebitda(5)	8.8x = 34,417 / 3,915	7.1x = 33,345 / 4,664	Ratio between enterprise value and EBITDA

tive performance metrics

	Definition and terms	Reconciliation of values at 31.12.2017	Reconciliation of values at 31.12.2016	Relevance
Personnel expenses, net	Personnel expenses – “Own work capitalised” (Note 25)[4]	Euros 1,031 million = 1,153 - 122	Euros 974 million = 1,083 - 109	Personnel expenses recognised in the income statement
Other revenues/expenses	“Other operating revenues”[2], “Other operating expenses”[2] Income on asset disposals”[2] “Recognition of fixed asset grants and other”[2]	Euros -1,681 million = 238 - 1,984 + 23 + 42	Euros -1,659 million = 240 -1,991 + 51 + 41	Other revenues and expenses recognised in the consolidated income statement
Payout	Dividends paid[6] / “Net profit attributed to the parent company”[2]	73.6% = 1,001 / 1,360	74.3% = 1,001 / 1,347	Measures the portion of profit used for shareholder remuneration through dividends
Dividend yield	Dividends paid per share / Closing share price	5.2% = 1 / 19.25	5.6% = 1 / 17.91	Ratio between remuneration (dividend) per share and the share price

(1) Consolidated balance sheet line item.
(2) Consolidated income statement line item.
(3) Consolidated statement of cash flows line item.
(4) Figure detailed in the Notes to the consolidated financial statements.
(5) Figure detailed in the APMs.
(6) Figure detailed in the Directors' Report.

Annex III. Glossary of non-financial indicators

Indicator	Definition
Overall satisfaction with service quality	Clients leve of satisfaction with global service quality in a range of 1 to 10 (in Chile 1 to 7), broken down by country or geographical region.
Direct GHG emissions	Greenhouse gas (GHG) emissions from sources owned or controlled by the company.
Emission generation factor (t CO2/GWh)	Rate of emissions as a result of electricity generation, obtained as the ratio between the amount of pollutant emitted (tonnes of carbon dioxide) and the power produced (GWh).
Emissions-free installed capacity (%)	Installed capacity in hydroelectric, mini-hydro, wind and solar technologies as a percentage of total installed capacity.
Emissions-free net production (%)	Net production using hydroelectric, mini-hydro, wind and solar technologies as a percentage of total net production.
Activity with ISO 14001 environmental certification (%)	Ebitda percentage corresponding to certified companies (*) through the environmental management model included in ISO 14001, with respect to the total of ebitda generated by activities that produce environmental impact. (*) As certified companies, companies that can be assimilated to certified companies have been included according to the following definition: - Those dominant companies whose dependent companies, of which they hold more than 50% ownership, are almost all certified - Those companies that concentrate corporate services only of certified companies. - Those companies whose dominant company concentrates corporate services and is certified.
No. of employees	Headcount at year-end.
Employees: detailed breakdown	Distribution of employees by geographical regions
Average age and seniority	Average age of employees in the workforce
Voluntary rotation rate	Voluntary redundancies/average workforce.
Total training hours	Total training hours received by employees in the workforce
Participants in the Corporate University	Number of persons attending training offered by the Corporate University
Trained workforce (%)	Percentage of workforce that has received training
Training hours per employee	Average number of training hours received by each employee (total training hours/Total employees on the payroll at year-end).
Investment in training per person	Amount in euros of the average investment in training per employee
Disabled persons integration rate	Percentage of disabled employees on the payroll
Men/women	Percentage of male employees at year-end / Percentage of women employees at year-end.
Women in management roles	Percentage of women in management over the total number of management personnel at year-end.
No. of accidents leading to days lost	Number of workplace accidents leading to days of work lost.
Days lost	Number of days lost due to workplace accidents. Counted in calendar days from the first day after receiving medical leave.
Fatalities	Number of employees killed as a result of workplace accidents.
Frequency	Number of accidents at the workplace leading to days lost per million hours worked.
Severity accident index	Number of days lost as a result of workplace accidents per 1,000 hours worked.
Incidence	Number of workplace accidents per 1,000 employees
Total number of suppliers	Number of suppliers from whom a product or service has been contracted in the year.
Total volume of purchases allocated	Total monetary amount used to cover the company's purchases.
Supplier *ESG assessment*[1]	Suppliers responding to the assessment survey which examines environmental, social and governance (labour practices) criteria

Indicator	Definition
Number of critical suppliers	Suppliers classified as high-risk based on any of the risk factors assessed (health and safety, quality, ESG, operating and legal)
Disqualified suppliers	Suppliers that have failed to pass the supplier approval process.
Investment in social action	Financial contribution to social action and social investing programmes, sponsorship and patronage
Persons trained in human rights	Number of employees trained in human rights policy
No. of notifications received related to the Code of Ethics (queries and complaints)	Number of notifications received by the Ethics Committee from employees and suppliers in relation to the Code of Ethics and Anti-Corruption Policy.
Tax contribution	Amount of taxes actually paid by country and divided between those that suppose an effective cost for the group and those that are retained or are passed on to the final taxpayer.
Investment in innovation	Amount in euros earmarked for innovation activities

[1] *Environmental, Social and Governance*

Annex IV. About this report

This report has been prepared in accordance with the information reporting (IR) framework published by the International Integrated Reporting Council (IIRC). Furthermore, in relation to non-financial aspects, Global Reporting Initiative (GRI) Standards were taken into account.

As stablished in Royal Decree 18/2017, of 24 de November, by which are modified the Comercial Code, Consolidated text of the law on capital companies approved by the Royal Legislative Decree 1/2010, of 2 july, and the Law 22/2015, of 20 de july, of Audit Accounts, in terms of non-financial information and diversity, the consolidated state of non-financial situation is incorporated, in what refers to environmental, social matters, as well as the ones referred to personnel, about respect to human rights and the fight against corruption and bribery contained in the section 5 of this management report.

Likewise, for the preparation of the report recommendations in the "Guide for the elaboration of the management report of the listed companies" that the "Comisión Nacional del Mercado de Valores" (CNMV) published in 2013 have been taken into account.

In 2017, the materiality analysis was updated, bringing it into line with the company's commitments and strategy in corporate responsibility and, for the first time, an analysis of the Sustainable Development Goals was included.

Material aspects identified at corporate level are those that:

- Are most critical for the continuity of the company's operations
- May trigger a more significant change in terms of economic, environmental and social impact
- Are considered to be most relevant for the company's stakeholders

Materiality of the main aspects identified has been assessed and prioritised the most relevant contents for inclusion in the Directors' Report, as detailed below:

Identification of significant aspects	Based on internal and external analyses, a list was drawn up of aspects that may substantially affect Gas Natural Fenosa's capacity to create value in the short, medium and long term. The following were taken into account: – Stakeholders' expectations: the main aspects defined by GRI Standards and sector-specific GRI supplements "Electric Utilities" and "Oil&Gas", on the basis of the materiality study conducted by Gas Natural Fenosa. – Investors' expectations: feedback from investors and *ESG*[1] analysts received during the various roadshows held in 2017. – Analysis of best practices: based on a selection of companies of acknowledged performance in terms of integrated disclosures.
Assessment of the materiality of the aspects identified	Classification of the various aspects identified in line with their significance for Gas Natural Fenosa according to their potential impact (positive or negative) on its capacity to generate value. According to the degree of significance, those aspects to be considered as part of the contents of the Directors' Report are obtained.
Prioritising contents	Once determined, the contents of the report are prioritised based on their materiality so as to focus the report on the most significant aspects.

[1] *Environmental, Social and Governance.*

Gas Natural Fenosa has identified ten material aspects of maximum significance. It has also identified the rest of matters of interest:

	Matters identified		Nature of the matter
Matters of maximum significance	1	Access to energy	Social
	2	Emissions and climate change	Environmental
	3	Workplace health and safety	Social
	4	Energy efficiency and energy consumption	Environmental
	5	Social action and development of local communities	Social
	6	Assessment of the supply chain	Social and environmental
	7	Employability and employment	Social
	8	Biodiversity	Environmental
	9	Customer service and satisfaction	Social
	10	Human rights assessment	Social
Other notable matters	11	Anti-corruption	Economic
	12	Technology and innovation	Economic
	13	Socio-economic and environmental compliance	Economic, environmental and social.
	14	Health and safety of consumers and society	Social
	15	Diversity and equality	Social
	16	Materials used, recycled and re-used	Environmental
	17	Freedom of association and collective bargaining	Social
	18	Water management	Environmental
	19	Management of leaks, spillages and waste	Environmental
	20	Responsible procurement	Economic
	21	Training, education and remuneration	Social
	22	Competitive practices	Economic
	23	Management of company-employee relations and internal communication	Social
	24	Tax matters	Economic
	25	Economic performance	Economic
	26	Cybersecurity and information security	Social
	27	Indirect economic impacts	Economic
	28	Resettlements	Social

Scope

The financial and non-financial information on Gas Natural Fenosa presented in this report is consolidated and refers to all the activities undertaken in 2017 as a global gas and electricity operator, although there are certain specific aspects:

In the sphere of human resources, the information reported corresponds to the countries in which Gas Natural Fenosa is present and has companies incorporated with their own staff and in which the company manages its human resources policies centrally, except on the number of employees and the average men/women that takes into account all the employees of the group according to consolidation perimeter.

With regard to the environment, the disclosures refer solely to those companies or activities that are at least 50% owned or controlled by the company, which have the capacity to influence environmental management or have the capacity to make a significant impact, based on global data.

Appendix I of the Consolidated Annual Financial Statements, titled “Gas Natural Fenosa Companies”, contains a complete list of companies belonging to the Gas Natural Fenosa group at 31 December 2017. Moreover, any changes in the consolidation scope are described in Annex II of the Consolidated Financial Statements.

As a result of the divestments of the gas distribution and supply business in Italy, gas distribution and supply in Colombia, electricity distribution in Moldova and electricity generation in Kenya, described in Note 9 “Non-current assets and disposal groups of assets held for sale and discontinued operations” to the Consolidated Annual Financial Statements, the consolidated income statement for 2016 has been restated for purposes of comparison with the information relating to 2017, in compliance with IFRS 5.

As regards non-financial information, since Gas Natural Fenosa managed these businesses during 2017, despite the divestment process, the figures relating to these businesses are included unless when it is specified that they are year-end figures in which case they are not included. Regarding, 2016 information it has not been re-stated.

Verification

The non-financial information in the Directors' Report was subject to an independent external revision process. The independent assurance report, where objectives and scope of the process as well as the procedures applied and conclusions are included, is attached as an annex hereto.

Annex V. Independent verification report

Free translation from the original in Spanish. In the event of a discrepancy, the Spanish language version prevails.

INDEPENDENT LIMITED ASSURANCE REPORT ON THE NON-FINANCIAL INDICATORS

To the Board of Directors of Gas Natural SDG, S.A.:

We have carried out our work to provide limited assurance on certain non-financial indicators contained in the 2017 Consolidated Directors' Report of Gas Natural SDG, S.A. and its subsidiaries (hereinafter 'Gas Natural Fenosa') for the year ended 31 December 2017, prepared in accordance with the criteria defined by Gas Natural Fenosa described in the section 'Glossary of non-financial indicators' included as Annex III of the mentioned Consolidated Directors' Report.

Specifically, we have reviewed the quantitative non-financial indicators included in table format in the sections '5.3. Responsible environmental management, '5.4. Interest in people', '5.5. Health and safety', '5.6. Responsible supply chain', '5.7. Social commitment', 'Analysis of the 2017 results' within the section '5.8. Integrity and transparency', and '7. Sustainable innovation', hereinafter, 'the non-financial indicators', of the 2017 Consolidated Directors' Report of Gas Natural Fenosa.

Responsibility of the Directors of Gas Natural Fenosa

The Directors of Gas Natural Fenosa are responsible for the preparation, content and presentation of the non-financial indicators included in the Consolidated Directors' Report in accordance with the criteria defined by Gas Natural Fenosa. This responsibility includes designing, implementing and maintaining the internal control required to ensure that the non-financial indicators are free from any material misstatement due to fraud or error.

The Directors of Gas Natural Fenosa are also responsible for defining, implementing, adapting and maintaining the management systems from which the information required to prepare the non-financial indicators included in the Consolidated Directors' Report, is obtained.

Our responsibility

Our responsibility is to issue a limited assurance report based on the procedures that we have carried out and the evidence obtained. Our limited assurance engagement was done in accordance with the International Standard on Assurance Engagements 3000 (Reviewed) "Assurance Engagements other than Audits or Reviews of Historical Financial Information", issued by the International Auditing and Assurance Standards Board (IAASB) of the International Federation of Accountants (IFAC).

The scope of a limited assurance engagement is substantially less extensive than the scope of a reasonable assurance engagement and thus, less security is provided.

The procedures that we have carried out are based on our professional judgment and have included consultations, observation of processes, document inspection, analytical procedures and random sampling tests. The general procedures employed are described below:

- Meetings with Gas Natural Fenosa's personnel from various departments who have been involved in the preparation of the non-financial indicators.

- Analysis of the procedures used for obtaining and validating the data presented in the non-financial indicators.

- Analysis of the Gas Natural Fenosa's non-financial indicators adaptation to the requirements established by Gas Natural Fenosa, described in the Annex III of the Consolidated Directors' Report.

- Verification, through random sampling tests revisions, internal control tests and substantive and analytical tests on the quantitative information of the Gas Natural Fenosa's non-financial indicators. We have also verified whether they have been appropriately compiled from the data provided by Gas Natural Fenosa's sources of information.

Our Independence and Quality Control

We have fulfilled our work in accordance with the independence requirements and other ethical requirements of the Code of Ethics for Professional Accountants of the International Ethics Standards Board for Accountants (IESBA), which are based on basic principles of integrity, objectivity, professional competence and diligence, confidentiality and professional conduct.

Our firm applies the International Standard on Quality Control 1 (ISQC 1) and thus employs an exhaustive quality control system which includes documented policies and procedures on the compliance of ethical requirements, professional standards, statutory laws and applicable regulations.

Limited assurance conclusion

As a result of the procedures carried out and the evidence obtained, no matters have come to our attention which may lead us to believe that the non-financial indicators included in the Gas Natural Fenosa's Consolidated Directors' Report, for the financial year ending 31 December 2017, contain significant errors or have not been prepared, in all of their significant matters, in accordance with the criteria defined by Gas Natural Fenosa.

Use and Distribution

Our report is only issued to the Directors of Gas Natural Fenosa, in accordance with the terms and conditions of our engagement letter. We accept no responsibility to third parties other than the addressees of our report.

PricewaterhouseCoopers Auditores, S.L.

Mª Luz Castilla

February 14, 2018