

General Shareholders' Meeting

Annual Financial Report / 2017

Consolidated / Financial Year 2016



Independent audit report

IBERDROLA, S.A. AND SUBSIDIARIES

**Consolidated financial statements and Consolidated management report
for the year ended December 31, 2016**

*(Translation of a report and consolidated financial statements originally issued in Spanish.
In the event of discrepancy, the Spanish-language version prevails)*

Translation of a report and consolidated financial statements originally issued in Spanish. In the event of discrepancy, the Spanish-language version prevails (See Note 54)

INDEPENDENT AUDIT REPORT ON THE CONSOLIDATED FINANCIAL STATEMENTS

To the Shareholders of IBERDROLA, S.A.:

Report on the consolidated financial statements

We have audited the accompanying consolidated financial statements of IBERDROLA, S.A. (the parent company) and its subsidiaries (the Group), which comprise consolidated statement of financial position at December 31, 2016, the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity, the consolidated cash flow statement, and the notes thereto for the year then ended.

Directors' responsibility for the consolidated financial statements

The directors of the parent company are responsible for the preparation of the accompanying consolidated financial statements so that they give a true and fair view of the consolidated equity and consolidated financial position and the consolidated results of IBERDROLA, S.A. and its subsidiaries, in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union, and other provisions in the regulatory framework applicable to the Group in Spain, and for such internal control as they determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

Our responsibility is to express an opinion on the accompanying consolidated financial statements based on our audit. We conducted our audit in accordance with prevailing audit regulations in Spain. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

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

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

Opinion

In our opinion, the accompanying consolidated financial statements give a true and fair view, in all material respects, of the consolidated equity and consolidated financial position of IBERDROLA, S.A. and its subsidiaries at December 31, 2016, and its consolidated results and consolidated cash flow for the year then ended, in accordance with IFRS, as adopted by the EU, and other provisions in the regulatory framework for financial information applicable in Spain.

Report on other legal and regulatory requirements

The accompanying consolidated 2016 management report contains such explanations as the directors of the parent company consider appropriate concerning the situation of the Group, the evolution of its business and other matters; however, it is not an integral part of the consolidated financial statements. We have checked that the accounting information included in the aforementioned consolidated management report agrees with the 2016 consolidated financial statements. Our work as auditors is limited to verifying the consolidated management report in accordance with the scope mentioned in this paragraph, and does not include the review of information other than that obtained from the accounting records of IBERDROLA, S.A. and its subsidiaries.

ERNST & YOUNG, S.L.

The original signed in Spanish

February 23, 2017



Annual Financial Report

Iberdrola, S.A. and subsidiaries / Financial Year 2016

**CONSOLIDATED FINANCIAL STATEMENTS AND CONSOLIDATED MANAGEMENT REPORT
FOR THE YEAR ENDED 31 DECEMBER 2016**

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Translation of Consolidated financial statements originally issued in Spanish and prepared in accordance with accounting principles generally accepted in Spain (see Note 54). In the event of a discrepancy, the Spanish-language version prevails.

IBERDROLA, S.A. AND SUBSIDIARIES

Consolidated statements of financial position at 31 December 2016 and 2015

Thousands of euros			
ASSETS	Note	12.31.2016	12.31.2015 (*)
Intangible assets	8	19,934,163	20,759,606
Goodwill		8,711,053	9,352,789
Other intangible assets		11,223,110	11,406,817
Investment property	9	462,342	480,741
Property, plant and equipment	10	63,834,384	61,788,590
Property, plant and equipment in use		57,343,025	56,827,455
Property, plant and equipment in progress		6,491,359	4,961,135
Non-current financial assets		3,903,994	3,711,006
Investments accounted for using the equity method	13.a	2,239,655	2,050,183
Non-current equity instruments		59,489	91,619
Other non-current financial assets	13.c	695,668	608,712
Derivative financial instruments	26	909,182	960,492
Non-current trade and other receivables	14	887,083	615,261
Deferred tax assets	28	6,958,154	6,629,508
NON CURRENT ASSETS		95,980,120	93,984,712
Assets held for sale		–	43,675
Nuclear fuel	16	322,630	349,882
Inventories	17	1,633,502	1,797,199
Current trade and other receivables		5,862,492	6,047,818
Income tax receivables	29	503,403	411,322
Other tax receivables	29	143,379	266,640
Other current trade and other receivables	18	5,215,710	5,369,856
Current financial assets		1,474,790	1,287,623
Current equity instruments		4,584	4,583
Other current financial assets	13.c	776,341	683,010
Derivative financial instruments	26	693,865	600,030
Cash and cash equivalents	19	1,432,686	1,153,273
CURRENT ASSETS		10,726,100	10,679,470
TOTAL ASSETS		106,706,220	104,664,182

(*) The Consolidated statements of financial position at 31 December 2015 are presented for comparative purposes only.

The accompanying Notes 1 to 54 and the Appendix are an integral part of the Consolidated statements of financial position at 31 December 2016 and 2015.

Translation of Consolidated financial statements originally issued in Spanish and prepared in accordance with accounting principles generally accepted in Spain (see Note 54). In the event of a discrepancy, the Spanish-language version prevails.

IBERDROLA, S.A. AND SUBSIDIARIES

Consolidated statements of financial position at 31 December 2016 and 2015

Thousands of euros			
EQUITY AND LIABILITIES	Note	12.31.2016	12.31.2015 (*)
Of shareholders of the parent	20	36,690,965	37,158,658
Issued share capital		4,771,559	4,752,652
In unrealised asset and liability revaluation reserves		(149,394)	(222,051)
Other reserves		31,506,301	31,304,757
Treasury shares		(1,083,367)	(639,239)
Translation differences		(1,059,117)	(459,039)
Net profit for the year		2,704,983	2,421,578
Of non-controlling interests		3,445,898	3,246,287
Subordinated perpetual obligations		550,526	551,108
EQUITY		40,687,389	40,956,053
NON-CURRENT EQUITY INSTRUMENTS HAVING THE SUBSTANCE OF A FINANCIAL LIABILITY	21	43,664	117,209
Deferred income	22	6,590,302	6,511,452
Provisions		4,904,875	5,005,174
Provisions for pensions and similar obligations	23	2,380,590	2,233,460
Other provisions	24	2,524,285	2,771,714
Bank borrowings		26,926,882	24,899,010
Bank borrowings and other financial liabilities- loans and others	25	26,509,052	24,567,364
Derivative financial instruments	26	417,830	331,646
Other non-current payables	27	737,269	689,694
Deferred tax liabilities	28	12,740,661	11,896,477
NON-CURRENT LIABILITIES		51,899,989	49,001,807
CURRENT EQUITY INSTRUMENTS HAVING THE SUBSTANCE OF A FINANCIAL LIABILITY	21	93,390	99,221
Provisions		143,643	245,346
Provisions for pensions and similar obligations	23	9,771	10,396
Other provisions	24	133,872	234,950
Bank borrowings		5,404,119	5,662,019
Bank borrowings and other financial liabilities - loans and others	25	4,711,630	4,877,111
Derivative financial instruments	26	692,489	784,908
Trade and other payables		8,434,026	8,582,527
Trade payables	30	5,490,634	5,577,148
Income tax payables	29	237,123	250,361
Other tax payables	29	914,493	1,000,712
Other current liabilities	27	1,791,776	1,754,306
CURRENT LIABILITIES		13,981,788	14,489,892
TOTAL EQUITY AND LIABILITIES		106,706,220	104,664,182

(*) The Consolidated statements of financial position at 31 December 2015 are presented for comparative purposes only.

The accompanying Notes 1 to 54 and the Appendix are an integral part of the Consolidated statements of financial position at 31 December 2016 and 2015.

Translation of Consolidated financial statements originally issued in Spanish and prepared in accordance with accounting principles generally accepted in Spain (see Note 54). In the event of a discrepancy, the Spanish-language version prevails.

IBERDROLA, S.A. AND SUBSIDIARIES

Consolidated income statements for the years ended at 31 December 2016 and 2015

Thousands of euros			
	Note	12.31.2016	12.31.2015 (*) Restated (Note 2.a)
Net revenue	32	29,215,382	31,418,693
Procurements	34	(16,299,160)	(18,576,018)
GROSS MARGIN		12,916,222	12,842,675
Staff costs	35	(2,517,301)	(2,430,227)
Capitalised staff costs	35	632,826	497,133
Net staff costs		(1,884,475)	(1,933,094)
External services		(2,299,556)	(2,444,299)
Other operating income		612,281	638,576
Net external expenses		(1,687,275)	(1,805,723)
Net operating expenses		(3,571,750)	(3,738,817)
Taxes other than income tax	37	(1,536,730)	(1,706,463)
GROSS OPERATING PROFIT / EBITDA		7,807,742	7,397,395
Amortisation and provisions	38	(3,253,706)	(3,568,108)
OPERATING PROFIT/ EBIT		4,554,036	3,829,287
Result of companies accounted for using the equity method - net of taxes	13.a	48,723	55,318
Finance income	40	1,060,181	585,017
Finance cost	41	(1,963,625)	(1,608,071)
Finance profit/(loss)		(903,444)	(1,023,054)
Gains on disposal of non-current assets	39	53,032	131,845
Losses on disposal of non-current assets	39	(4,886)	(6,775)
Non-current asset profit/(loss)		48,146	125,070
PROFIT BEFORE TAX		3,747,461	2,986,621
Income Tax	28	(904,619)	(527,092)
NET PROFIT FOR THE YEAR		2,842,842	2,459,529
Non-controlling interests		(114,911)	(16,496)
Subordinated perpetual obligations owners	20	(22,948)	(21,455)
NET PROFIT FOR THE YEAR ATTRIBUTABLE TO THE PARENT		2,704,983	2,421,578
EARNINGS PER SHARE IN EUROS (BASIC AND DILUTED)	52	0.421	0.368

(*) The Consolidated income statement at 31 December 2015 is presented for comparative purposes only.

The accompanying Notes 1 to 54 and the Appendix are an integral part of the Consolidated income statements for years ended 31 December 2016 and 2015.

IBERDROLA, S.A. AND SUBSIDIARIES

Consolidated statements of comprehensive Income for the years ended 31 December 2016 and 2015

Thousands of euros	12.31.2016				12.31.2015 (*)			
	Of the Parent	Of non-controlling interests	Of perpetual obligations owners	Total	Of the Parent	Of non-controlling interests	Of perpetual obligations owners	Total
NET PROFIT FOR THE YEAR	2,704,983	114,911	22,948	2,842,842	2,421,578	16,496	21,455	2,459,529
OTHER COMPREHENSIVE INCOME/(LOSS) TO BE RECLASIFIED TO PROFIT OR LOSS IN SUBSEQUENT PERIODS								
In unrealised asset and liability revaluation reserves	15,706	(10,690)	–	5,016	79,311	(1,268)	–	78,043
Change in the value of available-for-sale investments	(13)	–	–	(13)	29	–	–	29
Change in the value of cash flow hedges	15,118	(17,701)	–	(2,583)	110,475	(2,076)	–	108,399
Tax effect	601	7,011	–	7,612	(31,193)	808	–	(30,385)
In translation differences	(843,875)	171,949	–	(671,926)	1,502,588	7,769	–	1,510,357
TOTAL	(828,169)	161,259	–	(666,910)	1,581,899	6,501	–	1,588,400
OTHER COMPREHENSIVE INCOME/(LOSS) NOT TO BE RECLASIFIED TO PROFIT OR LOSS IN SUBSEQUENT PERIODS								
In other reserves	(231,493)	13,891	–	(217,602)	60,940	–	–	60,940
Actuarial gains and losses on pension schemes	(256,000)	22,978	–	(233,022)	92,315	–	–	92,315
Tax effect	24,507	(9,087)	–	15,420	(31,375)	–	–	(31,375)
In unrealised asset and liability revaluation reserves	73,496	–	–	73,496	4,532	–	–	4,532
Change in the value of cash flow hedges	96,192	–	–	96,192	5,672	–	–	5,672
Tax effect	(22,696)	–	–	(22,696)	(1,140)	–	–	(1,140)
TOTAL	(157,997)	13,891	–	(144,106)	65,472	–	–	65,472
OTHER COMPREHENSIVE INCOME/(LOSS) FROM COMPANIES ACCOUNTED FOR USING THE EQUITY METHOD (AFTER TAX)								
In other reserves	(16,453)	–	–	(16,453)	5,002	–	–	5,002
In unrealised asset and liability revaluation reserves	(16,545)	–	–	(16,545)	16,746	–	–	16,746
TOTAL (Note 13.a)	(32,998)	–	–	(32,998)	21,748	–	–	21,748
OTHER COMPREHENSIVE INCOME/(LOSS) FOR THE YEAR	(1,019,164)	175,150	–	(844,014)	1,669,119	6,501	–	1,675,620
TOTAL COMPREHENSIVE INCOME FOR THE YEAR	1,685,819	290,061	22,948	1,998,828	4,090,697	22,997	21,455	4,135,149

(*) The Consolidated statement of comprehensive income for 2015 is presented for comparative purposes only.
The accompanying Notes 1 to 54 and the Appendix are an integral part of
the Consolidated statements of comprehensive income for the years ended 31 December 2016 and 2015.

IBERDROLA, S.A. AND SUBSIDIARIES

Consolidated statements of changes in equity for the years ended 31 December 2016 and 2015

Thousands of euros	Issued share capital	Treasury shares	Other reserves					In unrealised asset and liability revaluation reserves	Translation differences	Net profit for the year	Non-controlling interests	Subordinated perpetual obligations	Total
			Legal reserve	Revaluation reserves	Share premium	Other restricted reserves	Retained earnings						
Balance at 01.01.2016	4,752,652	(639,239)	958,271	505,241	14,667,676	410,793	14,762,776	(222,051)	(459,039)	2,421,578	3,246,287	551,108	40,956,053
Total comprehensive income for the year	–	–	–	–	–	–	(247,946)	72,657	(843,875)	2,704,983	290,061	22,948	1,998,828
Transactions with shareholders or owners													
Free capital increase (Note 20)	136,805	–	–	(136,805)	–	–	(916)	–	–	–	–	–	(916)
Capital reduction (Note 20)	(117,898)	946,566	–	–	–	117,898	(946,603)	–	–	–	–	–	(37)
Distribution of 2015 profit	–	–	–	–	–	–	2,234,861	–	–	(2,421,578)	–	–	(186,717)
Acquisition of free-of-charge allocation rights (Note 20)	–	–	–	–	–	–	(514,265)	–	–	–	–	–	(514,265)
Transactions with treasury shares (Note 20)	–	(1,390,694)	–	–	–	–	2,707	–	–	–	–	–	(1,387,987)
Other changes in equity													
Equity instruments-based payments (Note 20)	–	–	–	–	–	–	(35,160)	–	–	–	–	–	(35,160)
Other movements	–	–	–	–	–	–	(272,227)	–	243,797	–	(90,450)	(23,530)	(142,410)
Balance at 12.31.2016	4,771,559	(1,083,367)	958,271	368,436	14,667,676	528,691	14,983,227	(149,394)	(1,059,117)	2,704,983	3,445,898	550,526	40,687,389

Thousands of euros	Issued share capital	Treasury shares	Other reserves					In unrealised asset and liability revaluation reserves	Translation differences	Net profit for the year	Non-controlling interests	Subordinated perpetual obligations	Total
			Legal reserve	Revaluation reserves	Share premium	Other restricted reserves	Retained earnings						
Balance at 01.01.2015 (*)	4,791,362	(815,990)	956,019	577,893	14,667,676	299,431	13,882,638	(327,003)	(1,404,052)	2,326,516	199,611	551,197	35,705,298
Total comprehensive income for the year	–	–	–	–	–	–	65,942	100,589	1,502,588	2,421,578	22,997	21,455	4,135,149
Transactions with shareholders and owners													
Free capital increase (Note 20)	72,652	–	–	(72,652)	–	–	(664)	–	–	–	–	–	(664)
Capital reduction (Note 20)	(111,362)	827,884	–	–	–	111,362	(827,917)	–	–	–	–	–	(33)
Distribution of 2014 profit	–	–	2,252	–	–	–	2,137,134	–	–	(2,326,516)	–	–	(187,130)
Acquisition of free-of-charge allocation rights (Note 20)	–	–	–	–	–	–	(115,028)	–	–	–	–	–	(115,028)
Transactions with treasury shares (Note 20)	–	(651,133)	–	–	–	–	4,178	–	–	–	–	–	(646,955)
Transactions with non-controlling interests (Note 42)	–	–	–	–	–	–	(394,867)	4,363	(557,575)	–	948,079	–	–
Other changes in equity													
Equity instruments-based payments (Note 20)	–	–	–	–	–	–	(4,385)	–	–	–	–	–	(4,385)
Modification of the consolidation perimeter (Note 42)	–	–	–	–	–	–	–	–	–	–	2,074,185	–	2,074,185
Other movements	–	–	–	–	–	–	15,745	–	–	–	1,415	(21,544)	(4,384)
Balance at 12.31.2015	4,752,652	(639,239)	958,271	505,241	14,667,676	410,793	14,762,776	(222,051)	(459,039)	2,421,578	3,246,287	551,108	40,956,053

(*) The Consolidated statement of changes in equity for 2015 is presented for comparative purposes only.

The accompanying Notes 1 to 54 and the Appendix are an integral part of the Consolidated statements of changes in equity for the years ended 31 December 2016 and 2015.

Translation of Consolidated financial statements originally issued in Spanish and prepared in accordance with accounting principles generally accepted in Spain (see Note 54). In the event of a discrepancy, the Spanish-language version prevails.

IBERDROLA, S.A. AND SUBSIDIARIES

Consolidated statements of cash flow for the years ended 31 December 2016 and 2015

Thousands of euros	Note	12.31.2016	12.31.2015 (*)
Profit before tax		3,747,461	2,986,621
Adjustments for			
Amortisation charge, provisions and staff costs for pensions	35, 38	3,362,519	3,802,655
Results of companies accounted for using the equity method net of taxes	13	(48,723)	(55,318)
Grants credited to income	22	(277,241)	(232,246)
Finance income and costs	40,41	903,444	1,023,054
Profit from the disposal on non-current assets	39	(48,146)	(125,070)
Changes in working capital			
Change in trade and other receivables		312,847	(309,353)
Change in inventories		190,950	272,978
Change in trade and other payables		(294,873)	(49,406)
Effect of translation differences on working capital of foreign companies		–	12,900
Change in non-current receivables and other payables		(15,448)	31,039
Provisions paid		(464,802)	(473,554)
Income taxes paid		(743,362)	(691,622)
Dividends received		95,258	67,258
Cash flows from operating activities		6,719,884	6,259,936
Subsidiary acquisitions	42	–	(541,389)
Change in cash due to variations in the perimeter of consolidation	42	–	43,217
Investments in intangible assets	8	(284,662)	(262,979)
Investments in associates	13	(47,460)	(69,448)
Equity instruments		(16,689)	(3,176)
Other investments	13	(1,525)	(1,707)
Investments in investment property	9	(7,321)	(4,713)
Investments in property, plant and equipment	10	(4,732,931)	(3,828,998)
Capital grants	22	15,380	31,793
Changes in working capital due to current financial assets		(9,171)	(1,375)
Interest received		157,943	188,443
Income taxes		(11,437)	(33,718)
Proceeds from disposals of non-financial assets		2,015	20,245
Proceeds from disposals of financial assets		110,090	55,904
Net cash flows from investing activities		(4,825,768)	(4,407,901)
Free-of-charge allocation rights acquisition	20	(514,265)	(115,028)
Dividends paid		(186,717)	(187,130)
Dividends paid to non-controlling interest		(77,656)	–
Subordinated perpetual obligation issue		(30,188)	(30,188)
Issues and disposal from borrowings		9,277,651	6,058,274
Repayment of borrowings		(7,646,334)	(6,546,927)
Interest paid excluded capitalised interest		(1,037,353)	(1,122,931)
Movement of working capital by revenue shortfall		(90,444)	285,389
Cash outflows due to capital reduction		(37)	(33)
Cash outflows due to capital increase		(916)	(664)
Treasury shares acquisition	20	(1,453,188)	(941,042)
Proceeds from disposals of treasury shares	20	83,513	92,782
Net cash flows from financing activities		(1,675,934)	(2,507,498)
Effect of exchange rate changes on cash and cash equivalents		61,231	3,203
Net increase / (decrease) in cash and cash equivalents		279,413	(652,260)
Cash and cash equivalents at the beginning of the year		1,153,273	1,805,533
Cash and cash equivalents at the end of the year		1,432,686	1,153,273

(*) The Consolidated cash flow statement for 2015 is presented for comparative purposes only.
The accompanying Notes 1 to 54 and the Appendix are an integral part of
the Consolidated cash flow statements for the years ended 31 December 2016 and 2015.

IBERDROLA, S.A. AND SUBSIDIARIES

Notes to the Consolidated financial statements for the year ended 31 December 2016

1. GROUP ACTIVITIES

Pursuant to article 5 of its By-laws, the corporate purpose of Iberdrola, S.A. (hereinafter, IBERDROLA), incorporated in Spain is as follows:

- To carry out all manner of activities and construction work and provide services required for, or related to, the production, transmission, switching and distribution or retailing of electric power or electricity by-products and their applications, and involving the raw materials or primary energies required for electric power generation, energy services, engineering, computer and telecommunication services, services relating to the Internet, the treatment and distribution of water, the integral provision of urban and gas retailing services, and other gas storage, regasification, transmission or distribution activities, which will be provided indirectly through the ownership of shares or other equity investments in companies that do not engage in the retailing of gas.
- The distribution, representation and marketing of all manner of goods and services, products, articles, merchandise, computer programs, industrial equipment, machinery, machine and hand tools, spare parts and accessories.
- To engage in the research, study and planning of investment and corporate organisation projects, and to promote, set up and develop industrial, commercial and service companies.
- To provide assistance and support services to the group companies and other investees, providing for them the guarantees and collateral required for this purpose.

The aforementioned activities may be performed in Spain and abroad, and may be performed totally or partially either directly by IBERDROLA or through the ownership of shares or other equity investments in other companies, subject in all cases to the legislation applicable at any given time and, in particular, to the applicable legislation to the electricity industry (Note 3).

In general, the corporate purpose of the subsidiaries consists of the production, switching, distribution and retailing of electricity and gas, telecommunication services, real estate and engineering activity as well as other related activities in Spain and abroad.

IBERDROLA's registered address is at Plaza Euskadi 5, in Bilbao.

2. BASIS OF PRESENTATION OF THE CONSOLIDATED FINANCIAL STATEMENTS

2.a) Applicable accounting legislation

The IBERDROLA Group's 2016 Consolidated financial statements were prepared by the directors on 21 February 2017, in accordance with International Financial Reporting Standards (hereinafter, IFRS), as adopted by the European Union, in conformity with Regulation (EC) number 1606/2002 of the European Parliament and of the European Council. The directors of IBERDROLA expect these Consolidated financial statements to be approved at the General Shareholders' Meeting without modification.

The IBERDROLA Group's 2015 Consolidated financial statements were approved at the General Shareholders' Meeting on 8 April 2016.

On 31 December 2016, the IBERDROLA Group presents a negative working capital of EUR 3,256 million. However, as shown in Note 50, the IBERDROLA Group has a liquidity of EUR 8,016 million, consequently, these Consolidated financial statements were prepared following the going concern principle.

These Consolidated financial statements have been prepared on a historical cost basis, except for available-for-sale financial assets and derivative financial instruments, which have been measured at fair value. The carrying amounts of assets and liabilities hedged by fair value hedges are adjusted to reflect variations in their fair value as a result of the risk hedged.

The accounting policies used in the authorization for issue of these Consolidated financial statements correspond with those used for the year ended on 31 December 2015, except for:

- The application, from 1 January 2016, of the following standards, amendments and interpretations published by the International Accounting Standards Board (IASB) that have been adopted by the European Union for its use in Europe:
 - o Annual improvements to the 2010-2012 cycle.
 - o Amendments to IAS 19: Defined benefit plans - employees' contributions.
 - o Amendments to IFRS 11: Acquisition of an interest in a joint operation.
 - o Amendments to IAS 16 and 38: Acceptable methods of depreciation and amortization.
 - o Annual improvements to the 2012-2014 cycle.
 - o Amendments to IAS 1: Disclosure initiatives.

Based on IAS 1: "Disclosure initiatives", the IBERDROLA Group has included the following headings in the Consolidated income statement: "Net staff costs", "Net external services", "Net operating expenses", "Gross operating profit/EBITDA", "Finance profit/(loss)" and "Income from non-current asset profit/(loss)". These headings comprise items consisting of amounts recognized and measured in accordance with IFRS.

The rest of amendments to the standards mentioned above have not had a material impact on these Financial statements.

- Starting 1 January 2016, the IBERDROLA Group has decided to modify the accounting policy regarding the recognition of government grants, recording the annual effect to be transferred to the Consolidated income statement under the "Other operating income" heading compared to the previous criterion that was to reduce the depreciation of subsidised assets recorded under "Amortisation and provisions".

IAS 20: "Government grants" allows both options for recognition of the transfer to results of capital grants. After making a comparison with the accounting policies applied by companies in the industry, it has been considered that this change in accounting policy allows for greater comparability.

As is established in IAS 8: "Accounting policies, changes in accounting estimates and errors", the comparative information of the previous period has been restated. The effect in 2016 and 2015 amounts to EUR 82 million and EUR 91 million, respectively, and corresponds mainly to the effect of ITC (Investment Tax Credit) (Note 3).

Such change of presentation has no impact on the Group's net profit.

The IBERDROLA Group has not applied in advance of the authorization for issue of these Consolidated financial statements any published standard, interpretation or amendment that has not yet come into force.

On the other hand, at the date these Consolidated financial statements were authorised for issue, the following standards, amendments and interpretations had been issued, all of which are effective subsequent to 1 January 2016:

		Mandatory application	
Standard		IASB	European Union
Amendments to IAS 28 and IFRS 10	Sales or contributions of assets between an investor and its associate/joint venture	Postponed	(*)
Amendments to IAS 7	Statement of Cash Flows: Disclosure initiative	01.01.2017	(*)
Amendments to IAS 12	Recognition of deferred tax assets for unrealized losses	01.01.2017	(*)
IFRS 15	Revenues from contracts with customers	01.01.2018	01.01.2018
IFRS 9	Financial instruments	01.01.2018	01.01.2018
Modification to IFRS 2	Classification and measurement of share-based payment transactions	01.01.2018	(*)
IFRIC 22	Foreign Currency Transactions and Advance Consideration	01.01.2018	(*)
Modification to IAS 40	Transfer of investment Property	01.01.2018	(*)
2014-2016 cycle	Annual improvements to several standards	01.01.2017/ 01.01.2018	(*)
IFRS 16	Leases	01.01.2019	(*)
Modification to IFRS 15	Clarifications to the standard	01.01.2018	(*)
(*) Pending approval from the European Union			

The IBERDROLA Group is currently analysing the impact of applying the approved standards, interpretations and amendments, whose application is not mandatory for the year ended 31 December 2016. In regards to IFRS 9, IFRS 15 and IFRS 16 specifically, said analysis will continue throughout 2017 given the complexity of these three standards. As to the rest of standards, the IBERDROLA Group believes that their application would not have had a material impact on these Consolidated financial statements, and, furthermore, would not have a material impact when they are applied.

- Pursuant to application of IFRS 16, the IBERDROLA Group expects its assets to increase in terms of usage rights as a result of registration of user rights arising from its lease contracts categorised as operating lease contracts pursuant to current regulations. The counterpart to this financial asset will primarily be greater debt, which is expected to increase by an amount greater than the sum of minimum lease payments disclosed in Note 36 to these Consolidated financial statements.

Moreover, when IFRS 16 becomes applicable, the outlay on these operating leases, booked under the "External services" heading on the Income statement in these Consolidated financial statements, will be booked under the "Amortisation and provisions" heading - in respect of amortisation of these user rights - and under the "Finance cost" heading, in order to reflect debt at its current value - on the Consolidated income statement.

The IBERDROLA Group's main leases concern land used for wind farms and transformer plants, buildings and vehicles, among others. Under the current version of IAS 17, most of these leases are considered operating leases.

With some exceptions, the IBERDROLA Group has elected to exclude intangible assets, short-term leases (less than 12 months) and leases of assets which, considered individually, are of little value, from the scope of the standard. Transition to the new standard is expected to be carried out using the modified retroactive application alternative. The new definition of leases in IFRS 16 will also be applied to all contracts ongoing at the date of initial application.

The IBERDROLA Group is currently modifying IT systems to adapt its accounting to the new regulatory requirements.

- With regard to application of IFRS 15 as of 1 January 2018, following the preliminary analysis performed, the IBERDROLA Group believes that its application would not have had a material impact on these Consolidated financial statements beyond activating customer acquisition costs. However, the IBERDROLA Group is examining the possible impact of the standard on the booking time for revenue from a number of joint energy sale contracts, green certificates and other services and accounting treatment of facilities assigned/funded by third parties.
- With regard to application of IFRS 9 as of 1 January 2018, following the preliminary analysis performed the IBERDROLA Group believes for the time being that:
 - o Its financial assets will continue to be measured at amortised cost, with the sole exception of equity instruments and financial derivatives, which will be measured at fair value.
 - o It will apply the general model for calculation of expected loss on financial assets other than trade and lease receivables, where the simplified model will be applied irrespective of whether or not they have a significant financial component. In view of the considerable creditworthiness of the financial assets, it is felt that the defaults applicable will be non-material.

- IFRS 9 will enable hedge accounting to be applied to economic hedges that do not meet hedging requirements under the current version of IAS 39: mainly the hedging of risk components in non-financial contracts and consideration as a hedged item of a combination of a derivative and an item which could meet the characteristics of a hedged item. Transition to the new standard in relation to hedge accounting will be carried out prospectively.

The IBERDROLA Group will not opt for early application of any of the above standards.

2.b) Basis of consolidation

The appendix to these Consolidated financial statements lists all IBERDROLA subsidiaries, jointly controlled entities and associates, together with the consolidation or measurement basis used and other related disclosures.

The subsidiaries over which the IBERDROLA Group exercises control are fully consolidated, except when they are scantily material with respect to presenting fairly the financial statements of the IBERDROLA Group.

The IBERDROLA Group considers that it controls a company when it is exposed, or has a right, to variable returns from its involvement in the company and has the capacity to influence such yields through that control. For the purposes of these Consolidated financial statements, it is considered that the Group has control over the companies in which it owns more than a 50% of the share capital and whose control can be proved. The Appendix to these Consolidated financial statements shows the companies that are less than 50% owned and fully consolidated and those which are more than 50% owned but are not fully consolidated.

The joint ventures in which the IBERDROLA Group invests were measured by the equity method.

The associates over which the IBERDROLA Group does not exercise control, but does have a significant influence on are accounted for in the Consolidated statement of financial position by the equity method. For the purpose of these Consolidated financial statements, it is considered that a significant influence is exercised over companies in which the Group has an ownership of over 20% in the share capital and it can be proved that such significant influence exists.

Despite having a stake of less than 20% in Gamesa Corporación Tecnológica, S.A. (hereinafter, GAMESA), IBERDROLA believes that it has a significant influence over the company, among other reasons, because IBERDROLA is the leading shareholder and has three directors on a board of twelve; and by the fact that there are significant transactions between both companies.

The Appendix to these Consolidated financial statements sets out disclosures on companies in which the Group has an interest of less than 20% but which have been consolidated using the equity method, and on companies in which the Group has an interest of more than 20% but less than 50% that have not been consolidated using the equity method.

On 31 December 2016 and 2015, there were no significant restrictions regarding the Group's capacity to access or use the assets and liquidate the liabilities of the subsidiaries, joint ventures or associates, particularly those related to the transfer of cash, dividends or other capital distributions, except the restrictions imposed by the financial loans regarding the dividend distribution described in Note 25.

The closing date of the Financial statements of subsidiaries, joint ventures and associates is 31 December. These companies' accounting policies are the same as or have been conformed to those used by the IBERDROLA Group.

The Financial statements of each of the foreign companies have been prepared in their respective functional currencies, defined as the currency of the economic environment in which each company operates and in which it generates and uses cash.

The operations of the IBERDROLA Group are consolidated in accordance with the following basic principles:

1. On the acquisition date, assets, liabilities and contingent liabilities of a subsidiary are recognised at fair value. Any excess of the subsidiary's acquisition cost over the market value of its assets and liabilities is recognised as goodwill, as it corresponds to assets that cannot be identified and measured separately. If the difference is negative, it is recognised as a credit to income in the Consolidated income statement.
2. The results of the subsidiaries acquired or disposed during the year are included in the Consolidated income statement from the effective date of acquisition or until the effective date of disposal.
3. Gain or losses on acquisitions from non-controlling interests in companies over which the Group exercises control and sales transactions without loss of control are recognised as a debit or credit to reserves.
4. The result of accounting for investments using the equity method is classified under the "Other reserves" and the "Result of companies accounted for using the equity method - net of taxes" heading in the Consolidated statement of financial position and in the Consolidated income statement, respectively.
5. The interest of minority shareholders in equity and the results of the fully consolidated subsidiaries is presented under the "Equity – Of non-controlling interests" heading on the liability side of the Consolidated statement of financial position and under the "Non-controlling interests" heading in the Consolidated income statement, respectively.
6. The financial statements of foreign companies were converted to euros using the year end exchange rate method. This method consists of converting to euros all the assets, rights and obligations at the exchange rates prevailing at the date of the Consolidated financial statements; for at the average exchange rates for the year the Consolidated income statement items; and at the historical exchange rates at the date of acquisition for equity (or in the case of retained earnings at the average exchange rates for the year in which they were generated provided that there are no significant transactions that make the use of the average exchange rate inappropriate), as appropriate. The resulting translation differences are taken directly to reserves.
7. All balances and transactions between the fully consolidated companies have been eliminated in the consolidation process. Gains or losses on transactions with associates and joint ventures are eliminated in proportion to the percentage ownership of the companies concerned.

2.c) Comparative Information

When comparing the figures for 2016 included in these Consolidated financial statements with those corresponding to the year 2015, it is necessary to take into account:

- Such as is indicated in Note 42, on 25 February 2015 the Boards of Directors of IBERDROLA, IBERDROLA USA, Inc. a company which, as a consequence of this transaction, has been renamed as Avangrid, Inc. (hereinafter, AVANGRID) and UIL Holdings Corporation (hereinafter UIL) approved the terms to make UIL part of the IBERDROLA Group through its absorption by Green Merger Sub, Inc. (hereinafter GREEN MERGER SUB), a wholly-owned investee of AVANGRID. This acquisition, after obtaining the deemed approvals and authorizations, was culminated on 16 December 2015.

UIL is a US company listed on the New York Stock Exchange, and it is the parent of a group of companies, engaged in the regulated transmission and distribution of electricity and gas in Connecticut and Massachusetts (United States of America).

Consequently, while the Consolidated income statement, the Consolidated statement of comprehensive income, the Consolidated statement of changes in equity and the Consolidated statement of cash flows for the year ended 31 December 2016 include the activities carried out by UIL throughout the year, those for the year 2015 only include those carried out since 16 December.

- In addition, effective as of 1 January 2016, the IBERDROLA Group has changed the way of reporting their activities in Brazil assigning them to different lines of business (until 31 December 2015 they were integrated into the Networks segment). The effect of this change in the segment information is not significant and, as established by IAS 8 "Accounting policies, changes in accounting estimates and errors" the comparative information for the previous period has been restated (Note 7).

3. INDUSTRY REGULATION AND FUNCTIONING OF THE ELECTRICITY AND GAS SYSTEM

IBERDROLA and some of the Group companies carry out electricity and gas activities in Spain and abroad (see the Appendix to these Consolidated financial statements) that are heavily influenced by the regulatory frameworks. Below is a summary of the main regulations affecting the IBERDROLA Group (the management report describes them in detail).

3.1. European Union

In the member states of the European Union in which IBERDROLA is present, particularly in the UK and Spain, it should comply with EU regulations.

The aim of the European legislation is the implementations of the single gas and electricity markets in order to facilitate the exchange of energy flows and allow any consumer in the European Union to deal freely with any supplier in the EU. In this respect, there are two types of legislation: the directives, which set out common criteria to be observed in internal markets and which the member states should transpose into national legislation; and the Regulations, which establish norms for the supranational issues, especially those related to the transit of gas and electricity, and are applicable directly.

Another set of regulations that indirectly affects the energy sector are those arising from the energy and climate policy agreed in 2007. It involves the triple objective of reducing emissions of greenhouse gases (GHGs) by 20%, setting a quota of renewable energy of 20% and a target for reducing consumption by 20% vs. "Business as Usual" case, all by 2020. To meet these objectives by 2020 there have been four documents accompanying the legislation: the reform of the Emissions Trading System, EU (EU-ETS), the national targets for emissions from non-EU ETS, and the national objectives on renewable energy.

Since 2009, the EU institutions and Member States have worked to implement the regulation approved in that year related to, on the one hand, the internal gas and electricity markets and, on the other hand, to promote renewable energy and to combat climate change. This regulation will be reviewed from 2016 to 2020.

The development of the regulation derived from these agreements is still pending.

The legislation on infrastructures is also relevant. The European Union has powers with regards to trans-European networks, specifically those of energy. During the last few years, various regulations and programmes have been created to promote a greater connectivity among the Member States. Specifically, programmes like the Trans-European Energy Networks (TEN-E), the European Energy Programme for Recovery (EEPR) and the Connecting Europe Facility (CEF). Lastly, in December 2014, the European Council approved the creation of a Strategic Investment Plan for the European Union, to mobilize EUR 315,000 million in 2015 – 2017. It will be structured as a European Fund for Strategic Investments allocated to investments in infrastructure, including energy and renewable energy networks. The regulations implementing the Plan will be developed during 2015. In January 2015, the European Commission submitted the proposal of a Regulation on the European Fund for Strategic Investments to create the required legal framework. On 27 May 2015, an agreement was reached between the Council, the Parliament and the European Commission on the proposed Regulation.

In October 2014, the European Council agreed new targets for 2030: a 40% reduction in GHGs compared to 1990, a share of 27% for renewable energy and a reduction in consumption, also of 27% (to be potentially upgraded to 30% following new proposals as explained below regarding the *Clean Energy for all Europeans* package). It also agreed to ensure that in 2020 the electricity exchange capacity among countries was at least 10% of the installed capacity.

On 25 February 2015, the European Commission launched a framework strategy for a resilient Energy Union with a Forward-Looking Climate Change Policy, that includes fifteen action points to be implemented during the mandate of the current European Commission, including, among others, setting out the goals of an energy union and the steps of the Commission will take to achieve it, a new legislation to redesign and reform the electricity market, ensure the supply for electricity and gas, EU funding for energy efficiency, a new renewables energy package and a structural reform of EU-ETS, facilitating the compliance of 2030 Targets set by the European Council in October 2014. On 18 November 2015, the European Commission presented its first State of Energy Union reporting advances achieved in 2015 and steps to be undertaken in 2016. A guidance on Governance of the Energy Union process was also provided.

On 15 July 2015, the European Commission (EC) has published a package of documents that anticipated legislative action in the field of energy markets and emissions trading:

- *Communication on Market Design*: the EC analysed the functioning of the EU electricity markets, arose key proposals for improvement and opened the discussion on capacity mechanisms.
- *Communication on retail market ("New Deal" for customers)*: made proposals to fully liberalise retail markets and facilitate more interaction with customers. It also attached a document on "best practices" in self-consumption.
- *ETS Legislative proposal reform*: regarding the trading emissions, in July 2015 the EC sent its legislative proposal to reform the ETS Directive to the European Parliament and the Council, covering, inter alia, the Market Stability Reserve (MSR) and the protection of sectors in leak of carbon.

As set out in Decision 2015/1814 of the European Union and of the Council, the MSR (Market Stability Reserve) will come into operation on 1 January 2019. The MSR was established to reduce 900 million allowances of the auctioned volume during the period 2014-2019, reintroducing them in the auctions of 2019 and 2020. Beginning in 2019, an amount of allowances corresponding to 12 % of the number of allowances in circulation should be deducted each year from the auction volumes and placed in the Reserve. If the total number of allowances in the market is less than 400 million, then the MSR releases 100 million into the market. This mechanism is intended to stabilize the EU ETS (EU Emissions trading system) and strengthen the carbon price signal reducing gradually the surplus allowances. The MSR is included in the EU ETS review currently in discussion.

Discussions on the review of ETS have been held since July 2015 and overlap debate on Non-ETS sectors (transport, buildings, agriculture, waste, land-use and forestry) since 20 July 2016, when the EC has sent to EU legislative bodies its draft on the Effort Sharing Regulation.

On 30 November 2016 the EC has published the package Clean Energy for all Europeans, containing the legislative proposals to complete the implementation of the energy internal market and to achieve the environmental 2030 Targets, materialising the ideas drafted in July 2015 communications. November 2016 package involves the wholesale and retail markets and the frameworks for renewable energy sources and energy efficiency. It assesses the implementation of capacity mechanisms fully compatible with EU State Aid Guidelines on Energy and Environment.

The full package represents over 70 documents of which 8 are legislative proposals of high impact on energy markets to be discussed by the European Parliament and Council over the next two years. Practical implementation to market operation is expected to take in place by 2020.

Other EU regulation

The following regulations of significance to the energy sector were approved in 2015 and 2016:

- On 28 November, the Directive 2015/2193 on the limitation of emissions of certain pollutants into the air from medium combustion plants. This Directive establishes the mandatory register of this units, specific limit for certain components (sulphur dioxide, nitrogen oxides, ammonia and volatile organic compounds) and rules to control other pollutants (carbon monoxide). The maximum deadline of adaptation contemplated in the Directive for certain existing plants is 2030.
- In January, the OJEU published Delegated Regulation 2016/89 amending Regulation 347/2013, concerning the Union's list of projects of common interest. It is an update of the first list of Projects of Common Interest of 2013. New projects are added and others disappear (basically those for which implementation has begun). This list was published for the first time by the European Commission on 18 November 2015, at the time of the State of the Energy Union Report.
- Paris Agreement: On 11 April 2016, Decision (EU) 2016/590 of the Council was published, regarding the firm, on behalf of the European Union, of the Paris Agreement approved by virtue of the United Nations Framework Convention on Climate Change. The signing took place in New York on 22 April 2016.

Following the vote of the Plenary Session of the European Parliament of 3 October backing the decision of the Environmental Council of 30 September, the Paris Agreement adopted at COP21 was ratified. On 7 October, the Slovak Presidency submitted the instrument of ratification to the UN. Thus, the EU can attend the summit of Marrakesh from 7 to 18 November (COP22) with full capacity to take part in the conversations regarding the implementation of the Agreement. Notwithstanding, the ratification should be backed by all Member States, a step that has so far only been taken by seven countries (Hungary, France, Slovakia, Austria, Malta, Portugal and Germany). The Paris Agreement enters into force 30 days after being ratified by 55% of countries that make up at least 55% of emissions. Prior to this ratification, 62 countries representing 52% of global CO₂ emissions had ratified it.

- On 17 November 2016 the OJEU published the Regulation 2016/1952/EU on European statistics on natural gas and electricity prices and repealing Directive 2008/92/EC. This legislation establishes a harmonised framework to elaborate and disclose the statistics on gas and electricity prices, both for residential customers and for companies. The new rules allow more transparent understanding of the different price components, splitting energy, networks and "taxes and other". This last component reflects, inter alia the VAT, other taxes and support to policies through customer charges, particularly the support to renewable energies.

- On 19 December 2016 the OJEU published the Directive (EU) 2016/2284 on the reduction of national emissions of certain atmospheric pollutants, amending Directive 2003/35/EC and repealing Directive 2001/81/EC. This new Directive establishes stricter emission limits for each Member State in the period 2020–2030 for five pollutants: sulphur dioxide (SO₂), nitrogen oxides (NO_x), non-methane volatile organic compounds (NMVOC), ammonia (NH₃) and microparticles (PM_{2.5}). Levels for 2020 are equivalent to the adopted by the UE in previous regulations but levels for 2030 are significantly reinforced. The Directive shall be transposed to local regulation by 30 June 2018. Each Member State shall develop a national air pollution control programme by 2019 to ensure the compliance of the targets of this Directive regarding transport, agriculture and energy sectors.

3.2. Spain

The main new features that have been published in Spain in the year 2016 are as follows:

Biomass and wind energy auctions

On 21 January, the Resolution of 18 January 2016 by the General Directorate of Energy and Mining Policy was published, resolving the auction for the allocation of the specific remuneration regime to new biomass-based electricity production facilities within the mainland power system and to wind technology facilities, pursuant to the provisions of Royal Decree 947/2015, of 16 October.

Royal Decree 947/2015 stipulates an auction for the granting of the specific remuneration regime to new biomass-based electricity production facilities within the mainland power system and to wind technology facilities (200 MW of biomass and 500 MW of wind). The allocation procedure and the remuneration parameters are set out in ministerial order IET/2212/2015, and the auction was called by the State Secretariat for Energy's Resolution of 30 November 2015. Said auction was held on 14 January. All of the MW, both wind and biomass, were awarded, with the peculiarity that in both technologies, the discount proved to be 100%, so that no awardee will receive remuneration for investment costs.

Nuclear moratorium

On 13 January 2016, the Resolution by the General Directorate for Energy and Mining Policy was published, which determines the annual payment for 2015 and the amount pending offsetting at 26 October 2015 for the nuclear plant projects permanently stopped under additional provision seven of Law 54/1997, of 27 December, on the Electricity Sector. This resolution entails the permanent closure of the nuclear moratorium, since as of 26 October 2015, the Fund for securitisation of assets remaining from the nuclear moratorium, settles all of its payment commitments, leaving at zero the amount pending offsetting for the Lemóniz, Valdecaballeros and Trillo II plants (plants included in the nuclear moratorium).

Distributors Remuneration

On 17 June, Order IET/980/2016 of 10 June was published, by which the remuneration of the electrical energy distribution companies is established for 2016. The remuneration methodology was established in Royal Decree 1048/2013, of 27 December, by which the methodology for calculating the remuneration of the electrical energy distribution activity is established. Said Royal Decree states that by Order of the Ministry of Industry, Energy and Tourism, the reference unit values for the installations of mainland distribution will be established.

These unit values were approved by means of Order IET/2660/2015, of 11 December, which approves the standard installations and benchmark unit values per item of property with regard to investment, operation and maintenance, and the remuneration unit values of other regulated tasks used to calculate the remuneration of electrical energy distribution companies, and establishes the definitions of natural growth and relevant capacity increase, as well as the compensation for use and reservation of premises.

Given that the order was approved during the month of December 2015, it was not possible to make the remuneration calculations resulting from applying the unit values approved in Order IET/2660/2015, of 11 December. For this reason, Order IET/2735/2015, of 17 December –by which access tolls to electrical energy are established for 2016, and specific model facilities and remuneration parameters for electrical energy installations from renewable energy, cogeneration and waste sources are approved established an amount as payment on account until company remuneration was established under the mentioned Royal Decree.

Lastly, Order IET/980/2016, of 10 June, was published, by which remuneration of electrical energy distribution companies is established for 2016. This remuneration, with the exception of the incentive or penalisation for reduction of losses, will be definitive for the year 2016, and will amount to EUR 5,162.6 million, of which the amount of EUR 1,655.5 million corresponds to Iberdrola Distribución Eléctrica, S.A. (hereinafter, IBERDROLA DISTRIBUCIÓN).

Transmission Remuneration

That same day, Order IET/981/2016, of 15 June, was published, by which remuneration of companies owning electrical energy transmission systems is established for 2016. Final remuneration for 2016 for companies that own transmission facilities will amount to EUR 1,710 million.

Social tariff financing

The Order/IET/1451/2016 was published on 10 September 2016. This order establishes the percentages of distribution of the amounts to be financed regarding the Social tariff ('bono social') corresponding to 2016. This Order assigns 37.95% to Iberdrola España, S.A.U., to be applied as from the settlement number 8 of the Social tariff (August). Up until the publication of the Order a provisional percentage of 37.97% was applied.

On 30 November, the decisions of the appeals filed by the companies Viesgo, Endesa, Iberdrola and Gas Natural against Royal Decree 968/2014 were published. This royal decree developed the methodology for fixing the percentages of distribution of the amounts to finance relating to the social bonus, were published. In the aforementioned judgments, the Supreme Court recognizes the claim of the companies and annuls the system of financing deeming it to be discriminatory because it does not apply to all companies that carry out electricity activities in Spain. The financing companies must be compensated for the amounts contributed in 2015 and 2016 (affected by the annulled articles of royal decree 2014), with their corresponding interests. Consequently, the last settlement of the social tariff made in 2016, up to the closing date of the fiscal year, was the liquidation 8 for the period from January to August. As a result of the sentence received on 31 December 2016, the IBERDROLA Group has an accounts receivable amounting to EUR 193,387 thousand which has been recorded under the "Other current trade and other receivables" heading in the Consolidated statement of financial position, with a credit to the "Taxes other than income tax" and "Financial income" headings of the Consolidated income statement of EUR 184,501 thousand and EUR 8,886 thousand, respectively.

Subsequently, on December 24, Royal Decree-law 7/2016 was published, which regulates the mechanism for financing the cost of the Social tariff and other measures to protect vulnerable electricity consumers. This royal decree-law establishes a new mechanism for financing the Social tariff, charged to the retail activity, with immediate entry into force. Until the regulatory development, Iberdrola will finance 35.5% (up from 37.95% attributed to the Iberdrola group in the previous system).

In addition, it creates a second group of "severe vulnerable consumers" who must not have their supply interrupted, as well as co-financing their invoices by the competent Administrations and by the same Social tariff funders. This measure must be developed by regulation in three months.

Commercial margin

On 6 February 2016, the Supreme Court issued a judgment (dated on 3 November 2015) that cancels the commercial fix margin used to establish the PVPC, which is the Reference Trader's remuneration. The Supreme Court overturns the current value of 4 €/kW/year with effect from 1 April 2014 and orders the Government to set a new value after establishing a new methodology. Until then, the current value will be used for billing as a temporary value, as it is set out in the Order IET/2735/2015 of electric tolls for 2016.

On 25 November Royal Decree 469/2016 was published. It modified Royal Decree 216/2014 of 28 March and established the methodology of calculation of the Voluntary Price for the Small Consumer of electrical energy (this Royal Decree established a Reference Trader's remuneration of 4 €/kW). It also established its contracting legal regime.

The methodology included the recognition of the costs to carry out the reference marketing activity, taking as reference the costs of the three most efficient reference trader and excluding the face-to-face channel, plus a fee for the exercise of the activity (1.05% on energy price).

On 24 December 2016 a Ministerial Order was published with the concrete values, both for the past (from 1 April 2014 to 31 December 2016) and the future (for 2017 and 2018), establishing a fixed and variable term for the allocation of the Reference Trader's remuneration.

The Reference Traders will regularize the past through a customer refurbishment in the 9 months after the publication of the Ministerial Order (consumptions made from 1 April 2014 to the publication of the order).

Electricity Access tolls

Order ETU/1976/2016, establishes the electricity access tolls for 2017. This order maintains:

- The actual current tolls, as well as capacity payments.
- The distribution remuneration for 2016. (It is provisional and until a Ministerial Order is approved with the values for 2017).
- The same amount of compensation for non-peninsular systems and the contribution of 50% of this cost by the State Budget.
- The remunerations of the Market Operator and the System Operator and the calculation parameters to surcharge its cost between market agents.

The forecasts included in the Economic Report of the Order foreseen a tariff balance in 2016 and 2017.

Gas Access tolls

On 31 December, Order ETU/1977/2016 was published which establishes the tolls and fees associated with third party access to gas installations and the remuneration of regulated activities for 2017. This order maintains the current tolls in force, except for the reduction of refills except in the case of the coefficients applicable to short-term contracts.

Last resort of natural gas tariff

Resolution of 29 December of the General Directorate of Energy Policy and Mines, publishes the last resort of natural gas tariff effective from 1 January 2017. Prices increase by an average of 3%, in relation to the previous quarter. The increase is due to the boost in the cost of the raw material, both in its component referenced to Brent and the one referenced to the NBP.

Interruptibility

On 12 October was published the resolution approving the calendar and characteristics for the 2017 electric season of the competitive auction procedure. These auctions took place during the week of 14 November to 18 November. The total cost amounted to EUR 524.8 million with a total allocated power of 2,975 MW and an average price of EUR 176,420/MW.

Also related to the interruptibility, Resolution of 7 October 2016 has been published, which sets the average price of energy to be applied in the calculation of the remuneration of the service of interruptibility offered by consumers of non-mainland electric systems to which it applicable the Order ITC/2370/2007, of 26 July, during the fourth quarter of 2016. Its value is fixed at EUR 42.40/MWh.

Alternative energies for transport

Royal Decree 639/2016, of 9 December, establishes a framework of measures for the implementation of an infrastructure for alternative fuels. This is the transposition of the Directive, which requires each State to set specific objectives and measures to foster infrastructures that allow the deployment of alternative mobility to oil. It contemplates the use of electricity for transportation by road and the supply in ports and airports. It also contemplates the use of natural gas (CNG or LNG) in transport by road or ports.

3.3. United Kingdom

The main new features in 2016 in the United Kingdom are:

Competition and Markets Authority's (CMA) investigation

The Competition and Markets Authority (CMA) completed its investigation in December 2016 by finalising all the orders needed to implement the remedies in the final report. In parallel, OFGEM has been consulting on taking forward the matters which are for it to address and dealing with its responsibilities under the Orders. The key elements of the package include a price control on electricity and gas sold through prepayment meters, a database remedy to enable rivals to market to customers who had been on standard variable tariff for three years and a proposal to allow people with complex meters to access single rate tariffs. The package also includes the expected proposals to improve transparency in microbusiness sales, improve the responsiveness of the industry code modification process, reduce regulatory tariff restrictions, improve settlements accuracy, strengthen OFGEM's competition duties and introduce zonal transmission losses charges.

BREXIT

Following the vote on 23 June 2016 to leave the European Union, Prime Minister David Cameron resigned and was replaced by Theresa May who undertook an extensive reshuffle of senior and junior ministers and merged the Department of Energy and Climate Change into parts of the business ministry to create a new Department for Business, Energy and Industrial Strategy (BEIS), led by Greg Clark.

The UK Government was successfully challenged in the High Court on BREXIT, which ruled that Parliamentary authority was required before the Article 50 withdrawal process could be triggered. This was appealed to the Supreme Court which ruled early in 2017 that an Act of Parliament is indeed required and the Government accordingly brought forward a bill to that effect.

Capacity Market

During the first half of 2016, DECC (Department of Energy and Climate Change) has made a number of announcements and proposals aimed at reforming the capacity market. These include strengthening the penalties for non-delivery of promised new plant, increasing the volume procured, running a new auction for delivery in winter 2017/18, and a proposal to recover the costs of capacity payments more cost-reflectively. The Government also announced consideration of the air quality aspects of embedded diesel generation.

On 2 December 2016, OFGEM brought out an updated open letter signalling that it continued to believe that significant reforms were needed on some of the benefits for embedded generation, which may be distorting the outcomes of the capacity auctions. They cautioned that it would be prudent for investors to anticipate that by no later than 2020 embedded benefits would be curtailed according to the most adverse proposals arising in relation to get the industry code modifications from Scottish Power, Ltd. (SCOTTISH POWER) and EdF. On 28 October 2016, BEIS brought forward for consultation a proposal to recover the costs of capacity payments more cost-reflectively, so that these payments do not provide a further hidden subsidy for embedded generation.

The T-4 Capacity Market Auction duly took place in December 2016 and cleared at a price of GBP 22.50 per kW. Only limited new transmission connected gas generation was contracted. Some 1.4 GW of demand side management, 1.2 GW of embedded units and 0.5 GW of batteries were successful.

3.4. United States

The main new features in 2016 in the United States are:

Environmental regulation

On 8 November Donald Trump won the presidential election and Republicans retained control of the House and Senate. The election results affect federal policies and the legislative agenda in Washington, D.C., including energy policies. On 9 February 2016 the Supreme Court granted a stay on implementation of the Clean Power Plan that will remain in effect while the courts address the merits of the litigation. The Federal DC Circuit Court of Appeals subsequently heard oral argument in the cases, and a decision is expected soon. President Trump has also vowed to reverse the regulation. An appeal to the US Supreme Court is certain, but even if upheld, the Trump Administration and Republican Congress are not expected to sufficiently fund or staff EPA (Environmental Protection Agency) for Clean Power Plan implementation.

PTC and ITC

In December 2015 Congress enacted legislation extending and phasing-out the renewable production tax credit (PTC) and extending and phasing-down the solar investment tax credit (ITC). Developers that start construction on a wind project before 2017 will qualify for the full credit, while those starting construction between 2017 and 2019 will qualify for a reduced-value credit. Developers that start construction on a solar project before 2020 will qualify for a 30% investment tax credit. Projects for which construction begins after 2019 are eligible for a lower ITC. The Treasury Department subsequently issued guidance implementing the PTC, which is generally quite favorable. Wind developers will have at least four years from the start of construction, or until 31 December 2018, to complete a project under the "safe harbor" qualifying rules.

NARUC manual

In November 2016 NARUC issued its manual dealing with Distributed Energy Compensation. The NARUC manual provides regulators and stakeholders with information on how to address DER (Distributed Energy) opportunities, while maintaining affordable, reliable, safe, and secure electricity. The manual discusses rate design and compensation, the availability and use of new technologies, an explanation of what is DER, and describes a set of certain types of DER.

Reforming the Energy Vision

In April 2014 the NYPSC instituted its Reforming the Energy Visions, or REV, proceeding, the goals of which are to improve electric system efficiency and reliability, encourage renewable energy resources, support DER, and empower customer choice. In this proceeding, the NYPSC is examining the establishment of a Distributed System Platform, or DSP, to manage and coordinate DER, and provide customers with market data and tools to manage the use of their energy. The NYPSC has determined distribution utilities should be the DSP providers. The NYPSC also is examining how its regulatory practices should be modified to incent utility practices to promote REV proceeding objectives. The REV proceeding involves a two-phased schedule with an initial order relating to policy determinations for DSP and related matters issued in February 2015 and an initial order for regulatory design and regulatory matters issued in May 2016. All electric utilities were ordered to file an initial Distributed System Implementation Plan, or DSIP, by 30 June 2016. The DSIP was filed by NYSEG and RG&E and included information regarding the potential deployment of Automated Metering Infrastructure, or AMI. A separate petition for the cost recovery associated with full deployment of AMI was filed by NYSEG and RGE in December 2016.

New York Rate Cases

On 19 February NYSEG and RG&E submitted to the NYPSC its three years Settlement Agreement, known as a "Joint Proposal," addressing its electric and gas rate plan. PSC Commissioners approved the plan 15 June and it became effective on 1 May (with a make-whole) and new tariffs were put in place on 1 July 2016.

UI Rate Case

In December 2016, Public Utilities Regulatory Authority (PURA) of Connecticut approved distribution rate schedules for UI for three years that became effective 1 January 2017 and which, among other things, provides for USD 57 million of cumulative distribution rate increases, an allowed ROE of 9.10%.

3.5. Brazil

Tariff flags

In January 2016, ANEEL reviewed Tariff Category amounts for 2016 and the time when each one should be activated. ANEEL also divided the red category into two levels to better reflect different generation scenarios. Currently, the Tariff Categories are as follows:

- Green category: It is activated when the variable cost per unit (VCU) of the last coal-fired plant dispatched is less than BRL 211.28/MWh. It does not entail any additional cost for the customer.
- Yellow category: It is activated when the VCU of the last coal-fired plant dispatched is greater than BRL 211.28/MWh and less than BRL 422.56/MWh. It implies a surcharge of BRL 15/MWh for the customer.
- Red 1 category: It is activated when the VCU of the last coal-fired plant dispatched ranges from BRL 422.56/MWh to BRL 610.00/MWh. This implies a surcharge of BRL 30/MWh for the customer.
- Red 2 category: It is activated when the VCU of the last coal-fired plant dispatched is greater than BRL 610.00/MWh. It implies a surcharge of BRL 45/MWh for the customer.

In recent months, the country's improved water situation has enabled dispatch from fewer coal-fired plants than necessary previously for energy security reasons. This has enabled a green category from April 2016 to December 2016.

Hydrological Risk (Generation Scalling Factor - GSF)

ANEEL and the Chamber of Commerce for Power (CCEE) have defined the terms for implementing hydrologic risk renegotiation. Generators who, during the last year, had precautionary measures concerning hydroelectric plant guaranteed power output (GSF), may divide the payment that they must make into up to 6 settlements, with the appropriate adjustments. As a result, between April and May 2017, CCEE may make the financial payments for months in arrears for 2016. This agreement is the result of a discussion that extended throughout 2015, and will allow payment creditors to receive the arrearages and to regularize transactions on the energy market.

Law 13.299 (former Provisional Measure 706/2015):

It was approved on 21 June 2016. This Law proposes changes in the electricity sector, especially in the Conta de Desenvolvimento Energético (CDE). The CDE covers, among other things, costs derived from the purchase of fossil fuels in isolated systems and the grid losses of the North and Northeast distributors. The law establishes modifications in the calculations that increase the subsidy to the thermal generation of isolated systems. To offset this effect, the law authorises the Federal Government to allocate funds to the CDE to finance this subsidy. Furthermore, the Law establishes that the annual CDE fee paid by distributors should be proportional to their energy market, which will put an end to the subsidy to distributors in the North and Northeast regions. Currently, by law, distributors in the South, Southeast and Central-West pay 4.3 times more for this item than the rest of distributors

Over-contracting of distributors

In 2016, with political crisis and the impeachment process occurred against former President Dilma Rouseff, the economic situation deteriorated, and the country faced a drop on GDP of 4.6% in the first semester and an increasing on inflation indexes, such as IPCA and IGPM. These conditions contributed to a drop on energy consumption, worsen distributors overcontracting situation. Elektro Redes, S.A. (ELEKTRO) surplus position was above 105% that are covered by tariffs. Many actions were taken to mitigate this position in 2016 together with *Associação Brasileira de Distribuidores de Energia Elétrica* (ABRADEE) and ANEEL, that are listed as following:

- As a result of the Public Hearing 04/2016, any quota's volume above reposition volume should be considered as involuntary contracting, which mitigated the over-contracting (and because of that with charge to tariff) regarding this issue (replace energy of ending contracts), reducing ELEKTRO exposure in 6.9%.
- ANEEL announced the result of the Public Hearing 085/2013 that dealt with the reduction of distributors' Power Purchase Agreements (PPAs) due to the migration of special customers to Free Energy Market, and approved the reduction of future PPAs due to the migration of special customers.
- Possibility to sign Bilateral agreements between distributors and generators, with temporary suspension of PPAs.
- Minister of Mines and Energy published the decree 8.828, which suspends the requirement to replace the minimum contracted amount for overcontracted distributors. The measure provides more flexibility to them, since now overcontracted distributors will not be penalized if they do not purchase energy to replace contracts about to expire. For ELEKTRO, there will be direct impacts from 2020 onwards, once we have quotes already allocated in this replacement.
- ELEKTRO and ABRADEE are discussing with ANEEL, as an extension and consequence of decree 8.828, an adjustment in calculation of "quotas step", considering that overcontracted distributors are no longer penalized for not purchasing the replacement amount.

- On August, the Chamber of Electricity Trading (CCEE) started the execution of New Energy Relocation Mechanism (MCSD Energia Nova), that enables the overcontracted distributors to negotiate contractual reductions with generators. There were already processed three mechanisms for 2016, with supply period of July to December, August to December, and October to December. The results of these three processing allowed ELEKTRO to reduce 2.3% of its energy surplus.
- Retroactive reprocessing of *MCSD Energia Nova* for the months of July and August 2016, allowing the participation of generators that could not participate the previous time. The result is expected to be published in February 2017.

Readjustment of tariffs

On 27 August 2016, Elektro applied its annual readjustment of tariffs, in line with Resolution 2,125. In this readjustment, costs not manageable by the distributor (generation and political positions), (Section A) were passed on in full to the tariff. In this regard, the reduction of some components, such as the price of the Itaipu energy tariff and the reduction of the Energy Development Account (Cuenta De esenvolvimiento Energético, CDE) produced an average reduction of the end tariff of 13.40%. On its part, the section that remunerates costs managed by the distributors (added value of distribution) (Section B) had a positive readjustment (+9.11%) due to an update to reflect inflation registered in the period and discounting the X factor (for productivity and efficiency). The tariff reduction does not have a negative impact on the Operating Margin as these adjustments are in section A and other financial items whose impact do not affect the Company results.

New sectorial changes

On 18 November 2016, the Provisional Measure 735 was converted into Law 13.360 by President Michel Temer. The main changes established are:

- From May 2017, the managing role of the CDE, the RGR (Global Reversion Reserve) and the CCC (Fuel Consumption Account) will be transferred from Eletrobras to CCEE (Chamber of Electricity Trading).
- The apportionment of CDE quotas between distributors will gradually adjust from 2017 to 2030, when the quotas will finally be apportioned proportionally to each distributor's energy market.
- Alters CDE's allocation between clients: Consumers with Social Energy Tariff (low income consumers) won't pay the charge, and Medium and High Voltage clients will pay gradually less each year.
- Increases in Itaipu's Tariff: The additional cost that was paid by the National Treasury to Paraguay for its energy surplus will now be included in the tariffs.
- Grants permission for distributors to negotiate their energy surpluses with free clients: still must be regulated by MME (Ministry of Mines and Energy) and ANEEL.
- Allow the transfer of control of the company instead of concession termination in certain cases this should facilitate the privatization of Eletrobras' distributors and the sale of Abengoa's assets.
- New generation projects could sell energy in A-5 and A-7 auctions. Existing generators can participate in new energy auction until two years after construction.

- For delay in the beginning of operation in generation and transmission enterprises, there is the possibility of extending the contract in case of excluding of responsibility. The law defines which causes could be classified as excluding of responsibility.

3.6. México

The main new features in 2016 in Mexico are as follows:

Wholesale Electricity Market

On 27 January 2016, the Short-term Energy Market for the Baja California Interconnected System came into effect, followed by the National Interconnected System two days later. For its part, the Baja California Sur Interconnected System did not begin to operate as the Advance Day Market until 22 March 2016.

Throughout March, the Secretariat of Energy (SENER) has officially published the following manuals:

- *Account Statement, Invoicing and Payments Manual* which sets out the business processes carried out by the CENACE and the participants for the financial settlement process for transactions on and off the market.
- *Dispute Resolution Manual* which creates a committee to resolve disputes arising between the CENACE, market participants, transporters and distributors; it also determines the procedures for resolving disputes.
- *Performance Guarantees Manual* stipulating the procedures for estimating potential charges for market participants and the transactions carried out on the wholesale electricity market, considering possible default on obligations assumed with the CENACE.

Legal separation of the Federal Electricity Commission (CFE):

On 11 January 2016, the SENER published the *terms for the strict legal separation that establishes what the CFE must comply with to engage in the generation, transportation, distribution, sales and supply of primary inputs* in the DOF (Mexican Official Gazette). The purpose of the legal separation is to promote the efficient operation of the electricity sector and the open and not unduly discriminatory access to the transmission and distribution networks. According to these terms and conditions CFE will be divided vertically, creating legally independent companies for generation, transmission, distribution and supply, as well as horizontally.

On 28 January, the CRE granted the CFE permission to provide the Basic Supply Service. Subsequently, on 29 March the CFE published in the DOF the resolutions establishing the creation of Subsidiary Production Companies (EPS) for generation, the supply of basic services, transportation and distribution. One of the generation companies created will have the rights of administration of contracts corresponding to the 29 plants owned by Independent Energy Producers with installed capacity of 12,952 MW.

All the EPS shall commence operations by no later than 28 June 2016 unless the SENER decides on a different date.

On 21 April 2016, the Board of Directors of CFE approved the establishment of the Subsidiary Company called "CFE Intermediación de Contratos, S.A. de C.V." for legacy contracts.

Finally, on November 4, CRE published in the DOF the terms for the assignment of assets and the Generation's contracts to the Subsidiaries Productive Companies and CFE Subsidiaries. For the allocation, it was considered the Firm Power Plants according to PRODESEN 2015, the existing plants in 2016 and the PIEs that will be in operation before 2020. As a detail, Generación V will be in charge of the PIEs, Generación VI is the subsidiary with greater capacity assigned (9.92 GW) and Generación I the lowest (6.55 GW); Generación II, III and IV have about 7 GW. By technology, it has been distributed between all the subsidiaries, except wind energy and geothermal, which were assigned only to Generación VI. Laguna Verde was not assigned to any of the six generation subsidiaries.

Obligations and Clean Energy Certificates

On 30 March, the CRE published in the DOF Resolution RES/174/2016, establishing the General Administrative Provisions for the functioning of the System of Management of Clean Energy Certificates and Fulfilment of Obligations. The flexibility mechanism already announced in the Energy Transition Act is established, stipulating that obliged participants may defer settlement of up to 50% for up to two years when there is not enough of a market for clean energy certificates. The deadline for enrolling in the Obligated Participants System will be 30 November 2017. The CELs obligation is 5% consumption for 2018, and 5.8% for 2019.

Long-term Auctions

On 30 March 2016, the first long-term auction was awarded, covering approximately 85% of the clean energy needs and Clean Energy Certificates (CELs) of the Basic Services Supplier (currently CFE). Awardees included 18 bids corresponding to 11 companies. In this first auction, capacity needs were not covered and will be accumulated for the next auction.

On 20 June 2016, CENACE published the final terms and conditions of the Second Long-Term Auction for 2016. The basic principles are similar to those of the first auction but with smaller regional differences in price (between USD 0 and 1 per MWh). On 4 July 2016 CENACE published its CFE purchase offers, where it stands out that the energy volume plus the clean energy certifications is 67% higher than that of the first auction. Furthermore, the maximum price for these products is USD 60/MWh (above average allocation prices for the previous auction: USD 47.8/MWh). On the other hand, CFE has presented capacity purchase offers for 1,483 MW/year at a price of USD 90,000/MW.

On 28 September 2016, CENACE published the results of the second auction, allocating 8.9 TWh of energy, 9.3 million of CEL, and 1,187 MW in Capacity, thereby covering 83.82% of the power purchase offer, 87.26% of the Clean Energy Certificates purchase offer and 80.05% of the Capacity Purchase offer (similar levels to those covered in the first auction). PhV represents 54% of energy allocated, wind power represents 44% and geothermal represents 2%. The resulting prices were USD 33.47/MWh for Clean Energy (combination of one MWh of energy and one Clean Energy Certificate), below those of the first auction (USD 48/MWh). As to capacity, the resulting price was USD 32,258 /MW per year.

Technologies of the Offeres Selected						
Technology	Amounts allocated per thechnology			Participation per technology		
	Clean Eenergy Certificates (mill.)	Energy (TWh)	Capacity (MW/year)	CEL	Energy	Capacity
Photovoltaic	4.9	4.8	184	54%	54%	15%
Wind	3.9	3.9	128	41%	44%	11%
Geothermal	0.2	0.2	25	2%	2%	2%
CCGT	-	-	850	-	-	72%
Hidroelectric	0.3	-	-	3%	-	-
Total	9.3	8.9	1,187	100%	100%	100%

Programme for the Development of the National Electricity Sector 'PRODESEN' 2016-2030

Published by SENER on 30 May 2016, carried out with the aim of satisfying future demand, diversifying the energy matrix, increasing the number of users with access to the supply, minimising costs and reducing electrical energy losses, under the criterion of an efficient expansion of the System.

The PRODESEN includes the Indicative Programme for Installation and Removal of Electrical Plants (PIIRCE, in its Spanish acronym), and plans to dismantle 15,820 MW of capacity over the next 15 years, especially conventional thermal power plants. Furthermore, the PIIRCE firmly includes two IBERDROLA projects in the generation category under the new LIE:

- CCC Escobedo Privados, 1,000 MW, coming online in 2019.
- CCC Tamazuchale II, 1,000 MW, coming online in 2020.

Power Purchase Agreements (CCE)

On 25 July 2016, the Mexican Regulatory Commission, CRE, published RES/528/2016, establishing the requirements and minimum amounts of CCE (energy, capacity and Clean Energy Certificates) that suppliers must meet as representatives of load centres. The main points are: postponement until 2017 of the requirements for capacity and energy and reduction of percentages of capacity and energy contract requirements for the Basic Services Supplier in 2016, which will gradually be increased over following years.

Gas Sector

During the second half of 2016 CENAGAS was empowered to conduct the future bidding processes for natural gas transportation auctions, (no longer CFE or Pemex) and all capacity rights of the SISTRANGAS were transferred to CENAGAS to control manage.

SENER issued a Public Policy to create a Natural Gas Open Market by 2018, in order to promote new players and to reduce the role of Pemex in the commercialization.

As part of this public policy, CENAGAS issued an Open Season for Transportation Capacity in the SISTRANGAS, which will grant firm capacity rights to the winning bidders for year 2017 and will help to identify the sections that need to be expanded in the future. The Open Season is for all the capacity available that has not been reserved or contracted under pre-existing long term supply agreements.

Regulation on hydrocarbons (Natural Gas):

On 28 September 2016, CRE published the resolution approving to CENAGAS the proposal of the open season procedure of SISTRANGAS (RES/1037/2016). The open season consists in a process of capacity allocation on a firm basis among those interested in the use of pipeline transportation. On the other hand, on 21 December 2016, CRE amended the calendar of CENAGAS "*Open Season of Natural Gas Transportation Capacity*", extending it until 10 February 2017, the deadline for receiving applications and until 1 July 2017, the deadline to start the operation.

The first electric power line in direct current auction:

On 10 October 2016, SENER published the pre-bases of this project. It will be approximately 610 km of line in 500 kV DC, from Oaxaca to the Valley of Mexico with 3,000 MW of capacity. The project will be financed through charges associated with the Transmission Tariff. The project is currently being redefined and new dates will be set.

4. ACCOUNTING POLICIES

4.a) Goodwill

Goodwill represents future economic benefits arising from other assets acquired in a business combination that are not individually identified and separately recognised.

Goodwill arising from acquisitions of companies with a functional currency, other than the euro is converted to euros at the exchange rate prevailing at the reporting date of the Consolidated statement of financial position.

Goodwill acquired on or after 1 January 2004 is measured at acquisition cost and the ones that are acquired earlier are measured at the carrying amount at 31 December 2003 in accordance with Spanish GAAP in effect on that date and as provided in IFRS 1: "First-time adoption of International Financial Reporting Standards".

Goodwill is not amortised. However, at the end of each reporting period goodwill is reviewed for its recoverability and any impairment is written down (Note 4.i).

4.b) Other Intangible assets

Concessions, patents, licenses, trademarks and others

The amounts recognised as concessions, patents, licenses, trademarks and others relate to the cost incurred in their acquisition.

The electricity distribution and transmission concessions held in UK by SCOTTISH POWER and those linked to the activities of AVANGRID, are not subject to any limits of a legal or other nature. Accordingly, intangible assets with an indefinite useful life are not amortised by the IBERDROLA Group, although they are assessed for indications of impairment each year, as described in Note 4.i.

This heading also includes the concession that will permit the IBERDROLA Group to build the hydro-electric complex in Alto Tâmega in Portugal.

On the other hand, IFRIC 12: "Service concession arrangements" concerning public-private service concession arrangements that meet two prerequisites:

- the grantor controls or regulates which services the operator must provide to the infrastructure, to whom it must provide them to and at what price; and
- the grantor controls any significant residual interest in the infrastructure at the end of the term of the arrangement.

Infrastructures within the scope of a service concession arrangement are not recognised as property, plant and equipment of the operator, because the operator does not have the right to control the use of the infrastructure.

If the operator performs more than one service (i.e. operation services and construction or upgrade services), the consideration received under the agreement for provision of services is recognised separately in the Consolidated income statement, pursuant to the standards applicable in each case, IAS 18: "Revenue" and IAS 11: "Construction contracts".

IFRIC 12 only affects the electricity distribution activities carried out by the IBERDROLA Group in Brazil. Remuneration for network construction and upgrade work carried out by the IBERDROLA Group in this country consisted, on the one hand, of an unconditional right to receive cash and, on the other hand, of the right to charge certain amounts to consumers. As a result, by applying IFRIC 12, two different assets were recognised for the two types of consideration received:

- A financial asset, which is recognised under "Other non-current financial assets" in the Consolidated statement of financial position (Note 13.c).
- An intangible asset, amortisable in the concession period, which is recognised under "Other intangible assets" in the Consolidated statement of financial position (Note 8).

The costs incurred in relation to the other items included under this heading in the Consolidated statement of financial position are amortised on a straight-line basis over their useful lives, between five and ten years.

Computer software

The acquisition and development costs incurred in relation to the computer software are recorded with a charge to "Other intangible assets" in the Consolidated statement of financial position.

Maintenance costs of computer software are recorded with a charge to the Consolidated income statement for the year in which they are incurred.

Computer software is amortised on a straight-line basis over a period of between three and five years from the entry into service of each software.

Research and development expenditure

The IBERDROLA Group's policy is to record research expenses in the Consolidated income statement for the period when they are incurred. The Consolidated income statements for the years ended 31 December 2016 and 2015 recognised EUR 211,447 thousand and EUR 200,197 thousand, respectively, for this concept.

Development costs are recognised as an intangible asset in the Consolidated statement of financial position if the Group can identify them separately and show the technical viability of the asset, its intention and capacity to use or sell it, and how it will generate probable future economic benefits.

Other intangible asset

This heading includes, among other items, wind farm projects in the development phase which meet the identifiability requirement under IAS 38: "Intangible assets", as they are separable and susceptible to individual sale and are carried at acquisition cost. The IBERDROLA Group transfers these assets to "Property, plant and equipment" in the Consolidated statement of financial position when construction of each wind farm commences.

4.c) Investment property

Investment property is recognised at acquisition cost and its carrying amount represents 0.72% and 0.77% of the IBERDROLA Group's total property, plant and equipment at 31 December 2016 and 2015, respectively.

Investment properties are depreciated on a straight-line basis, minus material residual value, over each asset's estimated useful life which ranges between 37.5 and 75 years based on the features of each asset concerned.

The investment property owned by the IBERDROLA Group relates primarily to properties used for leasing. The rental income earned in 2016 and 2015 from the lease of investment property amounted to EUR 30,655 thousand and EUR 23,314 thousand, respectively, and are presented under the "Net revenue" heading in the Consolidated income statements. These amounts represented approximately 0.10% and 0.07% of the net amount of the Group's revenues in 2016 and 2015, respectively.

Direct operating expenses arising on the investment property in 2016 and 2015 are not material.

The fair value of the IBERDROLA Group's investment properties is disclosed in Note 9. The fair value is determined on the basis of appraisals by independent valuers commissioned each year according to the Valuation Standards of the Royal Institution of Chartered Surveyors (RICS) of Great Britain, in the January 2014 edition. The appraisals at 31 December 2016 and 2015 are determined by Knight Frank Spain.

The assets have been individually appraised and not as part of a property portfolio.

The methods used for the calculation of fair value are the discounted cash flows method, income capitalisation and the comparative method, contrasted where possible the amounts with comparable transaction in order to reflect the market and prices at which transactions involving similar assets are being carried out.

The discounted cash flow method involves estimating possible net cash flows that a investment property could generate over a period, and considering the residual value of the asset at the end of the period. Cash flows are discounted at a target internal rate of return considered appropriate to each asset in order to reflect the urbanistic, construction and commercial risk.

For leased property, the key variables and assumptions used in the discounted cash flow analysis are:

- Net income from property over a specific period of time, bearing in mind the initial contractual situation, changes in tenants and expected rent, retailing expenses, disposal costs (variable percentage of 1%-3% depending on the selling price), etc.
- The discount rate or internal rate of return adjusted to reflect the investment risk based on location, occupancy, quality of tenant, age of the property, etc.
- The disposal return, which consists of an estimate of the exit (sale) price of the property applying an estimated return for the close of the transaction at that date, to perpetuity.

For leased properties without as many variables, with long-term leases of 10 years or longer and a single tenant, the cost or income capitalisation approaches are used. This method entails the capitalisation to perpetuity of the contractual rent using a rate subsidy that factors in all the potential market risks.

4.d) Property, plant and equipment

Property, plant and equipment are stated at their acquisition cost, modified, when appropriate, as follows:

- Prior to the transition to IFRS (1 January 2004), the IBERDROLA Group revalued certain Spanish assets under the "Property, plant and equipment" heading in the Consolidated statement of financial position as permitted by the applicable legislation, including the Royal Decree-law 7/1996, and considered the amount of these revaluations as part of the cost of the assets, in accordance with IFRS 1.
- In the case that the IBERDROLA Group is required to dismantle facilities or to recondition the site on which they are located, the present value of such costs is added to the carrying amount of the asset, based on their net present value, with a credit to the "Provisions - Other provisions" heading in the Consolidated statement of financial position (Note 4.r).

The IBERDROLA Group periodically reviews its estimates of this present value and increases or reduces the carrying amount of the assets on the basis of the results obtained.

On the other hand, the cost of acquisition includes the following items:

1. Finance costs relating to external funding accrued exclusively during the construction period, are determined as follows:
 - The interests accrued by specific-purpose sources of financing used to build certain assets are fully capitalised.
 - The interests accrued by general-purpose borrowings is capitalised by applying the average effective interest rate on this financing to the average cumulative investment qualifying for capitalisation, after deducting the investment financed with specific-purpose borrowings, provided that it does not exceed the total finance costs incurred in the year.

The average capitalisation rates used in 2016 and 2015 was 3.68% and 3.91%, respectively (Note 41).

2. Staff costs relating directly or indirectly to construction in progress (Note 35).

The IBERDROLA Group transfers property, plant and equipment in progress to property, plant and equipment in use at the end of the related trial period.

The costs of expansion or improvements leading to increased productivity, capacity or to a lengthening of the useful lives of the assets are capitalised.

Replacements or renewals of complete items are recorded as additions to property, plant and equipment, and the items replaced are derecognised.

Gains or losses arising on the disposal of items of property, plant and equipment are calculated as the difference between the amount received on the sale and the carrying amount of the asset disposed of.

4.e) Depreciation of property, plant and equipment in use

The cost of property, plant and equipment in use is depreciated on a straight-line basis, less any material residual value, at annual rates based on the following years of estimated useful life:

	Average years of estimated useful life
Conventional thermal power plants	25 - 50
Combined cycle plants	35
Nuclear plants	40
Wind farms (*)	
Structural components	40
Non structural components (rotative)	25
Gas storage facilities	25 - 40
Transmission facilities	40 - 56
Distribution facilities	30 - 54
Conventional meters and measuring devices	10-27
Electronic or smart meters	10
Buildings	50 - 75
Dispatching centres and other facilities	4 - 50

(*) In 2016 the IBERDROLA Group concluded the analysis it had been performing of the useful life of its wind farms, using internal and external sources of information. They concluded that, in the light of present circumstances, the best estimate of the useful life of civil works and the generator towers at onshore wind farms was 40 years, compared to the previous estimate of 25 years.

As a result, "Amortisation and provisions" in the 2016 Consolidated income statement includes the impact of this change in the estimate, which as per accounting regulations had been applied prospectively since 1 January 2016, and produced a lower depreciation of approximately EUR 148.1 million. The IBERDROLA Group has also estimated that, as of 2017, this adjustment to the useful life will give rise to an annual reduction in depreciation similar to that booked in 2016, and this amount at 1 January 2016 will gradually decrease as the useful life of the wind farms in use terminates.

As hydroelectric plants are operated under agreements (Note 11), the depreciation of civil engineering assets is performed over the life of the concession, while its electromechanical equipment is depreciated over the lower of the concession period or 35 years.

4.f) Leases

The IBERDROLA Group classifies as finance leases all arrangements under which the lessor transfers to the lessee substantially all the risks and rewards incidental to ownership of the asset. All other leases are classified as operating leases.

Assets acquired under finance leases are recognized as non-current assets in accordance with their nature and function. Assets are measured at the lower of the fair value of the leased asset and the present value of the future lease payments, and it is amortised by the useful life of each asset.

The expenses arising from operating leases are allocated to the Consolidated income statement on an accrual basis over the life of the lease agreement.

4.g) Nuclear fuel

The IBERDROLA Group measures its nuclear fuel stocks on the basis of the costs actually incurred in acquiring and subsequently processing the fuel.

Nuclear fuel costs include the finance costs accrued during construction, calculated as indicated in Note 4.d (Note 40).

The nuclear fuel consumed is recognised under "Procurements" in the Consolidated income statement from when the fuel loaded into the reactor starts to be used, based on the cost of the fuel and the degree of burning in each reporting period.

4.h) Inventories

Energy resources

Energy resources are measured at acquisition cost, calculated using the average weighted price method, or net realisable value, if the latter is lower.

No adjustments to the value of energy sources that are part of the production process are made if it is expected that the finished products into which they will be incorporated will be sold at above cost.

Real estate inventories

The real estate inventories were measured at acquisition cost, which includes both the acquisition cost of the land and plot and the costs of urban infrastructures and construction of real estate developments incurred until the year end. These costs include those incurred by the architecture and construction departments.

The acquisition cost also includes financial expenses to the extent that such expenses relate to the period of town planning permits, urbanisation or construction up until the time at which the land or plot is ready for operation, calculated using the method set out in Note 4.d (Note 41).

Commercial costs are charged to the Consolidated income statement on an accrual basis.

The IBERDROLA Group periodically compares the cost of acquisition of real estate inventories with their net realisable value, recognising the necessary impairment losses with a charge to the Consolidated income statement when the latter is lower. If the circumstance leading to the valuation adjustment no longer exists, it is reversed recognising the corresponding income.

For land, construction in progress and unsold units, net realisable value is used taking into account the appraisals by independent experts. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs to finish the production and the necessary costs to carry on with the sale of the element.

This value is determined using the residual method, where the estimated total cost of the work, is deducted from the gross value of the completed project, and the allowance for developer's risk and profit is added. The key variables of the residual method are:

- The total cost of the development, comprising the potential value of development at the valuation date based on the best estimates of independent valuers.
- The cost of the development, including all disbursements to be made by the developer of the work depending on the type (e.g. government-sponsored or private single-family dwellings) and quality of the construction. In addition to the cost of the work, it includes the cost of projects and licenses (10%-12% of the physical construction project), legal fees (1%-1.5% of the material implementation project), marketing and promotional expenses (2%-4% of income) and unforeseen contingencies (3% of income).
- The developer profit considered for each asset, depending on the zone state of the land, size and complexity of the development, ranging from 15% to 35% of total costs.

For land with licences, construction in progress and unsold units, the main difference with regard to unlicensed land is the developer profit, which in this case is lower given the stage of completion of the work and the decrease in risk as the completion of construction nears.

The heading "Net revenue" in the 2016 and 2015 Consolidated financial statements includes EUR 29,898 thousand and EUR 29,090 thousand, respectively, relating to sales of real state. These amounts represent the 0.10% and 0.09% of the IBERDROLA Group's total net revenue at those dates.

Emission allowances

Emission allowances inventories are valued at acquisition cost, calculated using the average weighted price method, or net realisable value, if the latter is lower.

Emission allowances which are incorporated into the production processes are not impaired if the finished products obtained as a result of those processes are sold over their cost.

Emission allowances acquired for the purpose of benefiting through fluctuations in their market price are measured at fair value with a credit or debit to the Consolidated income statement.

Emission allowances are derecognised from the Consolidated statements of financial position when they are sold to third parties, have been delivered or expire. When the allowances are delivered, they are derecognised with a charge to the provision made when the CO2 emissions were produced.

4.i) Non-Financial assets impairment

Each closing date at every accounting year, the IBERDROLA Group reviews the carrying amounts of its non-current assets to determine whether there is any indication that those assets have suffered an impairment loss. If such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss, if it is necessary. For this purpose, in the case of assets that do not generate cash flows independent from other assets, the IBERDROLA Group estimates the recoverable amount of the cash-generating unit to which belongs.

In the case of goodwill and other intangible assets which have not come into use or which have an indefinite useful life, the IBERDROLA Group performs the recoverability analysis systematically every year, except when there are indications of impairment in another moment, in which case recoverability analysis is performed at the same time.

For purposes of this recoverability analysis, goodwill is allocated to the cash generating units in which it is controlled for internal management purposes (Note 8).

Recoverable amount is the higher of fair value less selling cost and value in use, which is taken to be the present value of the estimated future cash flows. The assumptions used in assessing value in use, in making the estimates include discount rates, growth rates and expected changes in selling prices and direct costs. The discount rates reflect the time value of money and the risks specific to each cash-generating unit. The growth rates and the changes in prices and direct costs are based on contractual commitments that have already been signed, information in the public domain, sector forecasts and the experience of the IBERDROLA Group (Note 12).

If the recoverable amount of an asset is less than its carrying amount, the difference is registered as a charge to the "Amortisation and provisions" heading in the Consolidated income statement.

The IBERDROLA Group distinguishes between impairment allowances and write-offs depending on whether the impairment is reversible or not reversible. A write-off involves a decrease of the carrying amount of assets, either because the impairments are considered definitive and non-reversible, or because the accounting standards establish that, such as the case of goodwill, or when considering that the value of the asset is not going to be recovered for its use or disposal. Impairment losses are due to the fact that future expected earnings to be obtained are less than the carrying amount.

Impairment losses recognised for an asset are reversed with a credit to the "Amortisation and provisions" heading when there is a change in the estimates concerning the recoverable amount of the asset, increasing the carrying amount of the asset, but so the increased carrying amount does not exceed the carrying amount that would have been determined if no impairment loss had been recognised.

4.j) Associates and joint ventures

Investments in associates and joint ventures are accounted for using the equity method. Under this method, investments are measured initially at acquisition cost, subsequently adjusted for changes to each company's equity, taking into consideration the percentage of ownership and, if applicable, any valuation adjustments.

Some investments in associates and joint ventures which in the context of these Consolidated financial statements are immaterial are recorded at acquisition cost within "Non-current financial assets – Non-current equity investments" heading of the Consolidated statements of financial position for the years ended 31 December 2016 and 2015 (Note 13.b).

The IBERDROLA Group regularly analyses the existence of impairment at its associates and joint ventures by comparing the total carrying amount of the associate or joint venture, including goodwill, to its recoverable amount. If the carrying amount exceeds the recoverable amount, the IBERDROLA Group recognises the related impairment with a debit to the Consolidated income statement within the "Results of companies accounted for using the equity method - net of taxes" heading.

4.k) Joint operations

A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. These Consolidated financial statements include the proportional part of the assets, liabilities, income and expenses of the joint operation in which the IBERDROLA Group takes part in (Note 44).

4.l) Financial instruments

Financial assets

The IBERDROLA Group measures its current and non-current financial assets in accordance with the criteria described below:

1. Financial assets classified at fair value, registering changes through credits or charges in the Consolidated income statement. These are assets that meet any of the following requirements:

- They have been classified as held-for-trading financial assets, on the basis that the IBERDROLA Group intends to obtain a profit from fluctuations in their prices.
- They have been included in this asset category since initial recognition.

The assets included in this category are stated at fair value in the Consolidated statement of financial position, and changes in fair value are recognised as "Finance cost" or "Finance income" in the Consolidated income statement, as appropriate.

The IBERDROLA Group includes in this category the derivative financial instruments which do not satisfy the conditions necessary for hedge accounting based on the requirements established for this purpose in IAS 39: "Financial instruments" (Note 26).

2. Loans and receivables: these are initially recognised at fair value and are subsequently measured at amortised cost using the effective interest rate method.

The IBERDROLA Group records the related provisions for the difference between the amount of the receivables considered recoverable and the carrying amount of the receivables.

3. Held-to-maturity investments: are investments that the IBERDROLA Group has the intention and ability to hold to the date of maturity, which are also measured at amortised cost.
4. Available-for-sale financial assets: these are other financial assets that do not fall into any of the aforementioned three categories. These investments are recognised in the Consolidated statement of financial position at fair value at year end which, in the case of companies that are not listed, is obtained using a range of methods such as comparable company transactions or, if there is sufficient information, by discounting the expected cash flows. Changes in fair value are recognised with a charge or credit, as appropriate, to the "In unrealised asset and liability revaluation reserves" heading in the Consolidated statement of financial position (Note 20), until the disposal or impairment of these assets at which time the cumulative balance of this heading is recognised in the Consolidated income statement.

For those equity instruments of companies that are not publicly listed, the market value of which cannot be determined reliably are carried at cost of acquisition.

The IBERDROLA Group determines the most appropriate classification for each asset on acquisition and reviews the classification at each year end date.

The IBERDROLA Group recognises conventional financial asset purchases and sales on the date of operation.

Cash and cash equivalents

This heading in the Consolidated statement of financial position includes cash, current accounts and other highly liquid short-term investments that are readily convertible into cash and subject to insignificant risk of changes in value.

Impairment of financial assets at amortised cost

The IBERDROLA Group assesses, at least at each reporting date, whether there is any objective evidence that a financial asset or a group of financial assets is impaired. If it is determined that an impairment has occurred, the carrying amount of the financial asset is reduced by a debit to an impairment account in the Income statement for the period.

Impairment losses are reversed when the amount of the losses declines because of a subsequent event. Such reversals are recognised in the Consolidated income statement. An impairment loss may be reversed up to the carrying amount of the asset recognised at the date of reversal had no impairment loss been recognised previously.

The amount of impairment of debt instruments stated at amortised cost is calculated individually for material financial assets and collectively for financial assets which are not individually significant.

Impairment losses determined individually

The amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future expected credit losses that have not yet been incurred).

Impairment losses determined collectively

Financial assets are grouped on the basis of similarity of features relating to credit risk, which are indicative of the debtor's ability to pay all amounts due. The credit risk features considered for the purpose of grouping such assets are, among others: debtor's business sector, geographical area of activity, type of security or collateral, age of past-due amounts, and any other factor that may be relevant to estimate future cash flows.

To calculate an impairment loss on a group of financial assets, future cash flows are estimated on the basis of historical experience of losses for assets having credit risk features similar to those of the group in question.

Impairment of available-for-sale equity instruments

If there is objective evidence that the impairment losses on such assets are permanent, such losses are recognised in the Consolidated income statement.

The IBERDROLA Group considers objective evidence of impairment to be a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost. To this end, for available-for-sale financial instruments, a significant or prolonged decline in the fair value (stock market value for listed instruments) is considered to be a 40% fall for at least 3 months or a loss of value below purchase price for at least 18 months.

A recovery of an impairment loss is not recognised in the Consolidated income statement. Instead, it is recorded within "In unrealised asset and liability revaluation reserves" heading in the Consolidated statement of financial position.

Financial liabilities and equity instruments

Financial liabilities and equity instruments issued by the IBERDROLA Group are classified on the basis of the nature of their issue.

The IBERDROLA Group classifies as an equity instrument any contract that evidences a residual interest in the net assets of the Group.

Equity instruments having the substance of a financial liability

In the United States, the IBERDROLA Group has undertaken several transactions that bring minority shareholders as external partners of certain of its wind farms in exchange for cash and other financial assets primarily.

The main characteristics of these transactions are as follows:

- Regardless of the equity stake taken by the minority shareholders, the IBERDROLA Group retains ownership and management control of the wind farms; accordingly they are fully consolidated in these Consolidated financial statements.
- The minority shareholders have the right to a substantial portion of the profits and tax credits generated by these wind farms up to the return level established at the beginning of the contract.
- The minority shareholders remain in the equity of the wind farms until they achieve the stipulated returns.
- Once these returns have been obtained, the minority shareholders lose their entitlement to hold capital in the wind farms, simultaneously renouncing their claim on the profits and tax credits generated.
- Whether or not the minority shareholders of the IBERDROLA Group obtain the agreed upon returns depends on the economic performance of the wind farms. Although the IBERDROLA Group is bound to operate and maintain these facilities in an efficient manner and to take out the appropriate insurance policies, it is not obliged to deliver cash to the minority shareholders over and above the aforementioned profits and tax credits.

Following an analysis of the economic substance of these agreements, the IBERDROLA Group classifies the consideration received at the outset of the transaction under "Equity instruments having the substance of a financial liability" heading in the Consolidated statement of financial position. Subsequently, this consideration is measured at amortised cost (Note 21).

Debentures, bonds and bank borrowings

Loans, debentures and similar items are recorded initially at the amount received, net of transaction costs. In subsequent periods, all these financial liabilities are measured at amortised cost, using the effective interest rate method, except for hedged transactions, which are measured using the method described below in this same note.

Also, obligations under finance leases (Note 4.f) are recognised at the present value of the lease payments under "Bank borrowings and other financial liabilities – loans and others" in the Consolidated statement of financial position.

Trade and other payables

Accounts payables are caused by ordinary operations initially recognised at fair value and are subsequently measured at amortised cost.

Contracts to buy or sell non-financial items

The IBERDROLA Group performs a detailed analysis of all its contracts to buy or sell non-financial items to ensure they are classified correctly for accounting purposes.

As a general rule, those contracts that are settled net in cash or in another financial asset are classified as derivatives and are recognised and measured as described in this note, except for contracts entered into and held for the purpose of the receipt or delivery of a non-financial item in accordance with the IBERDROLA Group's purchase, sale, or usage requirements.

Contracts to buy or sell non-financial items to which the treatment described in IAS 39 is not applicable, are designated as own-use contracts and are recognised as the IBERDROLA Group receives or delivers the rights or obligations originating thereunder.

In the specific case of short-term contracts to buy or sell electricity and gas concluded on certain highly-liquid markets, the IBERDROLA Group adopts the following accounting treatment:

- Until the month preceding the supply date, the IBERDROLA Group classifies as own-use contracts only those contracts to buy or sell electricity and gas that reflect its best estimate of the actual purchase requirements of the IBERDROLA Group.
- In the month preceding the date of supply, and given that demand estimates become more and more accurate each day, the IBERDROLA Group assumes that all contracts written solely in response to changes in demand estimates, whether for purchase or sale, are own-use contracts, and not therefore derivatives.
- All contracts entered into with the intention of realising short-term gains on fluctuations in the market price of electricity and gas, as well as those that do not correspond to the situations described in the preceding two points are considered derivatives, and are therefore recognised on the Consolidated statement of financial position at their fair value.

Derivative financial instruments and hedge accounting

Financial derivatives are initially recognised at acquisition cost in the Consolidated statement of financial position and the required value adjustments are subsequently made to reflect their fair value at all times. Gains and losses arising from these changes are recognised in the Consolidated income statement, unless the derivative has been designated as a cash flow hedge or a hedge of a net investment in foreign countries.

For accounting purposes, hedges are classified as follows:

- Fair value hedges: where the hedged risk is a change in the fair value of an asset or liability or a firm commitment.
- Cash-flow hedges: where the hedged risk is the variation in cash flows attributable to a specific risk associated with an asset or liability or a likely transaction, or to exchange rate risk in a firm commitment.
- Hedge of a net investment in a foreign operation.

Each time a hedge transaction is entered, the IBERDROLA Group formally documents the transaction to be treated under hedge accounting. This documentation includes its identification as a hedge instrument, the item hedged, the nature of the risk the hedge is designed to cover and the way the effectiveness of the hedge is to be measured. In addition, hedges are reviewed periodically to ensure they are highly effective (between 80% and 125%).

The accounting treatment for hedging transactions is as follows:

- In the fair value hedges, changes in the fair value of the derivative financial instruments designated as a hedge and changes in the fair value of a hedged item due to the hedged risk are recognised with a debit or credit to the same heading of the Consolidated income statement.
- In cash flow hedges and hedges of a net investment in a foreign operation, changes in the fair value of the hedging derivative are recognised, in respective of the ineffective portion of the hedges, in the Consolidated income statement, while the effective portion is recognised under "In unrealised asset and liability revaluation reserves" and "Translation differences", respectively, in the Consolidated statement of financial position. The cumulative gain or loss recognised in these headings is transferred to the relevant heading of the Consolidated income statement as the hedged item affects net profit or loss.

If a hedge of a forecasted transaction results in the recognition of a non-financial asset or liability, its balance is taken into account in the initial measurement of the asset or liability arising from the hedged transaction.

If a hedge of a future transaction results in the recognition of a financial asset or liability, this balance is recognised in the "In unrealised asset and liability revaluation reserves" until the risk hedge in the future transaction impacts the Consolidated income statement.

If a future transaction does not result in the recognition of an asset or a liability, the amounts debited or credited, to "In unrealised asset and liability revaluation reserves" in the Consolidated statement of financial position will be recognised in the Consolidated income statement in the same period in which the hedge transaction is realised.

When hedge accounting is discontinued, the cumulative amount at that date recognised under "In unrealised asset and liability revaluation reserves" is retained under that heading until the hedged transaction occurs, at which time the gain or loss on the transaction will be adjusted. If a hedged transaction is no longer expected to occur, the gain or loss recognised under the aforementioned heading is transferred to the Consolidated income statement.

Derivatives embedded in other financial instruments are recognised separately when the IBERDROLA Group considers that their characteristics are not closely related to the financial instruments in which they are embedded and so long as the entire contract is not carried at fair value, registering changes in fair value with the gain or loss recognised in the Consolidated income statement.

The fair value of the derivative financial instruments is calculated as follows (Note 15):

- For derivatives quoted on an organised market corresponds to its market price at year end.
- To measure derivatives not traded on an organised market, the IBERDROLA Group uses assumptions based on market conditions at year end. Specifically, the fair value of the interest rate swaps is calculated as the value discounted at market interest rates of the interest rate swap contract spread. Currency futures are measured by discounting the future cash flows calculated using the forward exchange rates at year end. Finally, the fair value of contracts to trade non-financial items falling under the scope of IAS 39 is calculated on the basis of the best estimate of future price curves for the underlying non-financial items at the year end of the Consolidated financial statements, using, wherever possible, prices established on futures markets.

These measurement models take into account the risks of the asset or liability, among these, the credit risk of both the counterparty (Credit Value Adjustment) and the entity itself (Debit Value Adjustment). The credit risk is calculated according to the following parameters:

- Exposure at default: the amount of the risk arising at the time of non-payment by a counterparty, taking into account any collateral or compensation arrangements connected to the transaction.
- Probability of default: the probability that a counterparty will breach its obligations to pay the principal and/or interests, depending mainly on the features of the counterparty and its credit rating.
- Loss given default: the estimated loss in the event of default.

Derecognition of financial assets and liabilities

A financial asset is derecognised when:

- The rights to receive cash flows from the asset have expired.
- The IBERDROLA Group retains the rights to receive cash flows from the asset, but has assumed an obligation to pay them in full to a third party and has transferred substantially all the asset's benefits and risks or does not retain them substantially.
- The IBERDROLA Group has transferred its rights to receive cash flows from the asset and either has transferred substantially all the risks and benefits of the asset, or has neither transferred nor retained them, but has transferred the control of the asset.

Financial liabilities are derecognised when the obligation under the liability is discharged or cancelled or expires.

Offsetting of financial instruments

The financial assets and liabilities can be offset: the corresponding net amount must be shown in the Statement of financial position if the company currently has a legally enforceable right to offset the recognised amounts and the intention of settling them for the net amount or realising the assets and settling the liabilities simultaneously.

4.m) Treasury shares

At year end, the IBERDROLA Group's treasury shares are included under the heading "Treasury shares" in the Consolidated statement of financial position and are measured at acquisition cost.

The gains and losses obtained on disposal of treasury shares are recognised in "Other reserves" in the Consolidated statement of financial position.

4.n) Deferred income

Government Grants

This heading includes any non-reimbursable grants provided by the Administration whose purpose is to finance property, plant and equipment, including the cash received from the US Administration in the form of Investment Tax Credits as a result of setting up wind power facilities. All the capital grants are taken to the profit and loss statement under the "Other operating income" heading of the Consolidated income statement as the financed wind farms are depreciated (Note 2.a).

Facilities transferred or financed by third parties

According to the regulation applicable to electricity distribution in the countries in which it is active, the IBERDROLA Group occasionally receives cash payments from third parties for the construction of electricity grid connection facilities or direct assignment of such facilities. Both the cash received and the fair value of the facilities received are credited to "Deferred income" heading in the Consolidated statement of financial position.

These amounts are subsequently recognised under “Other operating income” in the Consolidated income statement as the facilities are depreciated.

Other deferred income

“Deferred income” heading also includes amounts received from third parties in relation to the assignment of the right to use certain facilities, which connect to the electricity grid the IBERDROLA Group’s optic fibre network and other owned assets. These amounts are taken to profit or loss on a straight-line basis over the term of each contract under “Other operating income” heading in the Consolidated income statement.

4.o) Post-employment and other employee benefits

The contributions to be made to the defined contribution post-employment benefit plans are expensed under the “Staff costs” heading in the Consolidated income statement on an accrual basis.

In the case of the defined benefit plans, the IBERDROLA Group recognises the expenditure relating to these obligations on an accrual basis over the working life of the employees by commissioning the appropriate independent actuarial studies using the projected unit credit method to measure the obligation accrued at the year end, and the positive or negative actuarial differences are recognised under “Other reserves” heading when they arise. The provision recognised under this concept represents the present value of the defined benefit obligation reduced by the fair value of the related plans.

If the fair value of the assets exceeds the present value of the obligation, the net asset is not recognised in the Consolidated statement of financial position unless it is virtually certain that it belongs to IBERDROLA Group.

The IBERDROLA Group determines the discount rate with reference to the market yields at the end of the reporting period, corresponding to the bonds or business obligations of high credit quality (rating equivalent to AA/Aa). In the countries in which does not exist a deep market to such bonds and obligations, the discount rate is determined with reference to Government bonds.

For the Eurozone, United Kingdom and the United States of America, there is a deep bond market with a sufficient period of maturity to cover all payments expected. In reference to the countries related to the Eurozone, the depth of the bond or obligation market is evaluated at the level of the monetary union and not for the particular country. In the case of Brazil, the discount rate has been determined taking into account the Brazilian sovereign credit, because a deep corporative market does not exist as they don’t satisfy the indicated credit qualifications.

The IBERDROLA Group applies a weighted average discount rate that reflects the estimate timing and amount of benefit payment, as well as the currency in which the benefits are to be paid.

The calculation methodology is mainly based on the following principles:

- The universe and spectrum of the outstanding bonds that meet the criteria of an AA/Aa rating is generated. The source of information corresponds with Bloomberg. The IBERDROLA Group has adopted the notional issues that are higher than EUR 50 million or its equivalent in local currency as the selection criteria.
- Once the bonds' database is obtained, the result is screened and the bonds that show any deficiencies are eliminated.
- The sample is grouped based on the bonds' duration and the return on each duration and outstanding nominal amount of the issue is shown. As far as possible, the price return is based on the midpoint of the bid/ask spread.

- The benefit payment is calculated using a mathematical formula, i.e., the discrete minimum approximation of the quadratic function, resulting in a market return curve based on the duration. The market curve result will provide the discount factors for each future maturity date of the bonds.
- For markets in which government bonds or corporate bonds with maturity dates beyond 25/30 years are not available, it is assumed that they will remain at the same level from the latest maturity date for which there is information available.

The discount rate reflects the time value of money and estimated schedule for the benefit payments. However, it does not reflect the actuarial risk, investment, credit or deviation in compliance with the actuarial assumptions risk.

4.p) Collective redundancy procedure and other early retirement plans for employees

The IBERDROLA Group recognises termination benefits, when there is an agreement with the employees or a certain expectation that such an agreement will be reached that will enable the employees to be terminated in exchange for indemnity payment.

The IBERDROLA Group recognises the full amount of the expenditure relating to these plans when the obligation arises by performing the appropriate actuarial studies to calculate the present value of the actuarial obligation at year end. The actuarial gains and losses are recognised in the Consolidated income statement.

4.q) Provision for emission allowances

The IBERDROLA Group records a provision for contingencies and expenses in order to recognise the obligation to deliver CO2 emission allowances, in accordance with the methods provided for in the national assignment plans (Notes 3 and 24).

For the portion of emissions covered by the allowances granted under these plans or by allowances acquired by the Group, the provision is recognised at the carrying amount of the allowances. If it is estimated that it will be necessary to deliver more emission allowances, the provision for this shortfall is calculated based on the market price of the allowances at the date of year end.

Under the "Procurements" heading in the 2016 and 2015 Consolidated income statements include EUR 55,275 thousand and EUR 122,773 thousand, respectively (Note 24).

4.r) Production facility closure costs

The IBERDROLA Group will incur in several decommissioning costs of its production plants, among which include those arising from necessary tasks to fit the land where they are located. Additionally, in accordance with the current legislation, the Group must perform certain tasks prior to the decommissioning of its nuclear plants, of which *Empresa Nacional de Residuos Radioactivos, S.A.* (hereinafter, ENRESA) is responsible for.

The estimated present value of these costs is capitalised with a credit to "Provisions – Other provisions" at the beginning of the useful life of the related asset (Note 24).

This estimate is subject to annual revision so that the provision reflects the present value of the full amount of the estimated future costs. The value of the asset is only adjusted for variances with respect to the initial one.

The IBERDROLA Group applies a risk-free rate to financially update the provision because the estimated future cash flows to satisfy the obligation reflect the specific risks of the corresponding liability. The risk-free rate used corresponds to the yield at year end on which reports, government bonds with enough depth and solvency in the same currency and similar due date to the obligation.

Any change in the provision as a result of its discounting is recognised in "Finance cost" in the Consolidated income statement.

4.s) Other provisions

The IBERDROLA Group recognises provisions to cover present obligations, whether these are legal or implied, which arise as a result of past events, provided that it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation (Note 24). A provision is recognised when the liability or obligation arises, with a charge to the relevant heading in the Consolidated income statement depending on the nature of the obligation, for the present value of the provision when the effect of discounting the value of the obligation to present value is material. The change in the provision due to its discounting each year is recognised under "Finance cost" in the Consolidated income statement.

These provisions include those recorded to cover environmental damage, which were determined on the basis of a case-by-case analysis of the situation of the polluted assets and the cost of decontaminating them.

On the other hand, according to labour regulations in force, the IBERDROLA Group is obliged to pay compensations to employees who, under certain conditions, terminate their employment relationship. At the date of authorization for issue of these Consolidated financial statements, the IBERDROLA Group does not expect to start any different plan from that mentioned in Note 23.

4.t) Current and non-current debt classification

In the Consolidated statement of financial position debts are classified by their maturity date at year end. Debts that are due within twelve months are classified as current items and those due within more than twelve months as non-current items.

4.u) Revenue recognition

Revenues from sales is measured at the fair value of the assets or rights received as consideration for the goods and services provided in the normal course of the Group companies' business, net of discounts and applicable taxes.

Income from regulated activities where remuneration is based on a fixed margin is booked by the IBERDROLA Group under the "Net revenue" heading in the Consolidated income statement for the corresponding year.

In the case of some regulated activities carried out by the IBERDROLA Group, any discrepancies between costs estimated when setting the annual tariff and costs actually incurred are corrected in the following years' tariffs. These discrepancies are recognised as income or expense for the year in which they arise only if its proceed or payment is certain, regardless of future sales.

Revenues from service agreements in which the results can be reliably measured are recognised in accordance with the percentage of completion method.

The IBERDROLA Group has electricity generation capacity assignment agreements with the *Comisión Federal de la Electricidad* (hereinafter, CFE) in Mexico for a term of 25 years from the date on which each combined cycle plant enters into commercial operation. These contracts set a pre-established payment timetable for assignments of electricity supply capacity and for plant operation and maintenance. IBERDROLA considered the question whether these contracts constitute a lease or service provision in accordance with the requirements of IFRIC 4: "Determining whether an arrangement contains a lease". Given that only IBERDROLA can operate or manage the plant and that operating revenue is not transferred solely to CFE as these plants generate additional revenue that is sold to third parties and, further, due to the price of the products being linked to market rates, it was concluded that these contracts are a service to be recognised in accounting with the percentage of completion method.

Revenue from construction contracts is recognised in accordance with the accounting policy described in Note 4.v.

As to housing sales, the IBERDROLA Group follows the principle of recognising income at the time when legal title is transferred to the purchaser, which usually matches the date of notarisation of the respective contracts.

Interest income is accrued on a time proportional basis, by reference to the outstanding principal and the applicable effective interest rate, which is the rate that exactly discounts estimated future cash receipts through the expected life of the asset to that asset's carrying amount.

Dividend income is recognised when the IBERDROLA Group companies are entitled to receive them.

4.v) Construction contracts

If the income and expenses related to a construction contract can be estimated reliably, the income is recognised according to the degree of completion of the construction project by measuring the contract costs incurred to date as a proportion of the total estimated construction costs.

When the income from a contract cannot be reliably estimated, all such income is recognised to the extent that costs are incurred, provided that such costs are recoverable. No contract margin is recognised until it can be estimated reliably.

If the estimated costs of a contract exceed revenue from that contract, the loss is recognised immediately in the Consolidated income statement.

Changes to construction work and any claims are included within contract revenue if negotiations are at an advanced stage of maturity so that it is probable that the client will accept the claim and the amount can be measured reliably.

4.w) Settlements relating to regulated activities and receivables due to the financing of revenue shortfall

Below, there is a description of the accounting impact on the Consolidated financial statements of certain regulatory issues arising in Spain in 2016 and 2015.

a) Electricity distribution

The Order IET/980/2016, by which the remuneration for electrical energy distribution companies is established for 2016, in accordance with the methodology regulated by Royal Decree 1048/2013, which recognized a remuneration for the electrical energy distribution activity carried out by the IBERDROLA Group in Spain during 2016 which amounts to EUR 1,661,639 thousand, amount which has been registered with a credit to the "Net revenue" heading in the Consolidated income statement for 2016.

The Order IET/2444/2014, by which access tolls of electricity for 2015 are determined, established compensation to the distribution of electricity activity carried out by the IBERDROLA Group in Spain amounting to EUR 1,589,345 thousand, which was recorded as a credit to the "Net revenue" heading in the Consolidated income statement for the 2015 year end.

b) Revenue shortfall

The Law 24/2013 of the Electricity Sector establishes that, in the case that an imbalance occurs due to revenue shortfalls in the settlement of the electricity sector, the amount may not exceed 2% of the estimated revenue of the system for that year. In addition, the accumulated debt by imbalances from previous years may not exceed 5% of the estimated revenue of the system. If these limits are exceeded, access tolls will be reviewed at least in an amount equivalent to the total excess of those limits. This law additionally states that the part of the imbalance due to revenue shortfall, without exceeding the limits, and that is not compensated by raising tolls and fees, will be covered by the subjects of the settlements system proportionally to their remuneration for the activities they perform.

The IBERDROLA Group has estimated that the outcome of the settlements of the Spanish electrical system corresponding to 2016 will have a surplus. However, the provisional settlements made until 31 December 2016 present a revenue shortfall. The amount of the deficit covered by the IBERDROLA Group amounted to EUR 240,917 thousand, which is recognized under the "Other current financial assets" heading in the Consolidated statement of financial position (Note 13.c).

The IBERDROLA Group estimated that the outcome of the settlements of the Spanish electrical system corresponding to 2015 would have a surplus. However, the provisional settlements made until 31 December 2015 presented a revenue shortfall. The amount of the deficit covered by the IBERDROLA Group amounted to EUR 150,473 thousand, which were recognized under the "Other current financial assets" heading in the Consolidated statement of financial position (Note 13.c). These amounts were received during 2016.

4.x) Onerous contracts

The IBERDROLA Group defines an onerous contract as a contract in which the unavoidable costs for meeting the corresponding obligations exceed the economic benefits expected to be received according to the contract.

The IBERDROLA Group records a provision for the present value of the difference between the direct costs and the economic benefits of the contract.

No provision was deemed necessary under this heading at 31 December 2016 and 2015.

4.y) Transactions in foreign currency

Transactions carried out in currencies other than the functional currency of the Group companies are recorded at the exchange rates prevailing at the transaction date. During the year, the differences arising between the exchange rates at which the transactions were recorded and those in force at the date on which the related proceeds or payments are made are charged or credited, as appropriate, to the Consolidated income statement.

Also, debt instrument and receivables and payables denominated in foreign currencies are converted at the year end exchange rates at 31 December of every year. Exchange differences are charged to "Finance cost" or credited to "Finance income" in the Consolidated income statement, as appropriate.

Those foreign currency transactions in which the IBERDROLA Group has decided to mitigate translation risk through the use of financial derivatives or other hedging instruments are recorded as described in Note 4.I.

4.z) Income Tax

Since 1986, IBERDROLA has filed Consolidated Tax Returns with certain Group companies.

Foreign companies are taxed according to the current legislation of their respective jurisdiction.

Income Tax is accounted for using the general balance liability method, which consists of determining deferred tax assets and liabilities on the basis of the carrying amounts of assets and liabilities and their tax base, using the tax rates that can objectively be expected to be in force when the assets or liabilities are realised or settled. Deferred tax assets and liabilities arising as a result of direct charges or credits to equity are also accounted for with a debit or credit to equity.

The IBERDROLA Group recognises deferred tax assets as long as future taxable profits are expected against which the said assets can be recovered.

Deductions in order to avoid double taxation and other tax credits as well as tax relief earned as a result of economic events occurring in the year are deducted from the Income Tax expense, unless there are doubts as to whether they can be realised.

4.aa) Final radioactive waste management costs

On 8 November 2003, the Royal Decree 1349/2003 was published regulating the ENRESA activities and its financing. This royal decree grouped together the previous legislation regulating the activities that ENRESA develops as well as its financing, and repeals, inter alia, the Royal Decree 1899/1984, of 1 August.

Meanwhile, the Royal Decree-law 5/2005 and the Law 24/2005 establish that the costs relating to the management of radioactive waste and spent fuel from nuclear plants, and to the dismantling and closure of the plants attributable to their operation and incurred after 31 March 2005, will be financed by the owners of the nuclear plants in use.

On the other hand, on 7 May 2009, the Royal Decree-law 6/2009 was published, adopting various energy sector measures and approving the Social tariff. The principal measures introduced are as follows:

- Necessary costs incurred in the management of radioactive waste and nuclear fuel at nuclear power stations that are definitively dismantled before the state-owned radioactive waste management company ENRESA begins operating, which had not yet been done at the date of these Consolidated financial statements, and all necessary costs incurred in dismantling and closing these power stations, will be treated as diversification and capacity guarantee costs.

Amounts used to cover the cost of managing radioactive waste generated by research activities directly related to nuclear electricity generation and the costs deriving from the reprocessing of spent fuel sent overseas prior to the entry into force of the Electricity Industry Law 54/1997, and all other costs that may be specified by the royal decree, shall also be considered diversification and capacity guarantee costs.

- Amounts used to register provisions to cover the costs incurred in managing radioactive waste and spent fuel generated at operational nuclear power stations after the establishment of ENRESA as well as dismantling and closure costs will not be treated as supply diversification and security costs, since these will be financed by the owners of the nuclear power stations while they are operational, irrespective of the date on which they are generated.
- The balance of ENRESA's provision remaining after deduction of the amounts needed to cover the supply security and diversification costs will be used to cover costs not included in this category.
- To cover the costs associated with nuclear power plants in operation, the companies owning the stations must pay a charge directly proportional to the volume of energy generated at each plant. The definitive method used to calculate this charge will be approved by the resolution of the Council of Ministers. This fact has not taken place yet as of the date of issue of these Consolidated financial statements.

After a detailed analysis of the impact of the Royal Decree-law 6/2009, the IBERDROLA Group considers that the rate is the best estimate available of the accrued expenses originated for that royal decree-law.

The "Taxes other than income tax" heading of the Consolidated income statements for 2016 and 2015 includes EUR 174,499 thousand and EUR 164,766 thousand, respectively.

4.ab) Earnings per share

Basic earnings per share are calculated by dividing the net profit for the year attributable to the Parent company by the weighted average number of ordinary shares outstanding during the year, excluding the average number of shares of the parent company held by Group companies (Notes 20 and 52).

Meanwhile, diluted earnings per share are calculated by dividing the net profit for the year attributable to ordinary shareholders by the weighted average number of ordinary shares outstanding during the year, adjusted by the weighted average number of ordinary shares that would have been outstanding assuming the conversion of all the potential ordinary shares into ordinary shares of IBERDROLA. For these purposes, it is considered that shares are converted at the beginning of the year or at the date of issue of the potential ordinary shares, if the latter were issued during the current period.

In the Consolidated financial statements of the IBERDROLA Group for the years ended 31 December 2016 and 2015, basic earnings per share coincide with diluted earnings per share, since there were no potential shares outstanding during these years that could be converted into ordinary shares (Note 52).

4.ac) Dividends

The dividend proposed by the Board of Directors of IBERDROLA to the General Shareholders' Meeting is not deducted from equity until it is approved by the latter.

4.ad) Non-current assets held for sale and discontinued operations

If the carrying amount of a non-current asset (or a disposable group of assets) is recovered principally through its sale rather than through its continued use, the IBERDROLA Group classifies it as held for sale and values it at the lower of its carrying amount and its fair value less the costs of sale.

A discontinued operation is a component of the entity that either has been sold or disposed of by other means, or is classified as held for sale and:

- represents a business line or geographical area that is significant and can be considered separately from the rest;
- is part of a single and coordinated plan to sell or dispose by other means a business line or geographical area that can be considered separately from the rest; or
- is a subsidiary acquired exclusively with intention to resale.

If the existence of discontinued operations is considered, the IBERDROLA Group recognizes a single amount in the Consolidated statement of comprehensive income that includes the total amount of:

- profit or loss after tax from discontinued operations, and
- profit or loss after tax recognized by measurement at fair value less costs of sale, or sale or disposal by other means of the assets or disposable groups of assets that constitutes the discontinued operation.

The IBERDROLA Group considers that there are no assets or cash generating units that meet the conditions for their presentation as assets held for sale or discontinued operations at 31 December 2016.

4.ae) Consolidated statements of cash flow

In the Consolidated statements of cash flow, which were prepared using the indirect method, the following terms are considered:

- Operating activities: the typical activities of the Group companies, as well as other activities that are not investing or financing activities.
- Investing activities: the acquisition, sale or disposal by other means of long-term assets and other investments not included in cash and cash equivalents.
- Financing activities: activities that result in changes in the size and composition of the equity and liabilities of the company that are not operating activities.

4.af) Share-based employee compensation

The delivery of IBERDROLA shares to employees as compensation for their services is recognised under "Staff costs" in the Consolidated income statement as the employees perform the remunerated services, with a credit to equity under "Equity – Other reserves" in the Consolidated statement of financial position at the fair value of the equity instruments on the delivery date, defined as the date the IBERDROLA Group and its employees reach an agreement establishing the terms of the share delivery.

If remuneration based on equity instruments is paid in cash, the amount booked as "Staff costs" in the Consolidated income statement is credited to "Other non-current payables" or "Trade and other payables - Other current liabilities" on the liabilities side of the Consolidated statement of financial position, as appropriate. The fair value of the cash-settled compensation is remeasured at each reporting date.

5. FINANCING AND FINANCIAL RISK POLICY

The IBERDROLA Group is exposed to risks inherent to the different countries, industries and markets in which it operates and in the businesses it carries out, which could prevent it from achieving its objectives and executing its strategies successfully.

In particular, the financing and financial risk policy of the IBERDROLA Group approved by the Board of Directors identifies the risk factors described below. The IBERDROLA Group has an organisation and systems, which allow the financial risks to which the Group is exposed to be identified, measured and controlled.

Interest rate risk

The IBERDROLA Group is exposed to the risk of fluctuations in interest rates affecting cash flows and fair value in respect of items in the Statement of financial position (debt and derivatives).

In order to adequately manage and limit this risk, the IBERDROLA Group yearly determines the desired structure of the debt between fixed and floating interest rate, taking into account the indexing of income at a certain indicator, either interest rate or price index. On a yearly basis, actions to be carried out are determined throughout the year: new sources of financing (at a fixed, floating or indexed rate) and/or the use of interest rate derivatives.

The debt structure at 31 December 2016 and 2015, after considering the effect of hedge derivatives, is the following:

Thousands of euros	12.31.2016	12.31.2015
Fixed interest rate	15,399,855	13,465,002
Floating interest rate	15,770,827	15,928,049
Limited floating interest rate (*)	50,000	51,424
Total	31,220,682	29,444,475

(*) Relating to certain borrowing agreements whose exposure to interest rate fluctuations is limited by caps and floors.

The reference interest rates for the floating rate borrowings are basically Euribor, Libor- sterling pound, Libor-dollar and the most liquid local reference indexes in the case of the debt of the Latin American subsidiaries.

Exchange rate risk

As the IBERDROLA Group's functional currency is the euro, fluctuations in the value of the foreign exchange rate in which borrowings are instrumented and transactions are made (mainly the sterling pound, the US dollar and the Brazilian real) with respect to the euro may have an impact on the finance costs, on the profit for the year and on the Group's equity.

The following items could be affected by exchange rate risk:

- Proceeds and payments for supplies, services or equipment acquisition in currencies other than the local or functional currencies.
- Income and expenses incurred by certain foreign subsidiaries indexed to currencies other than the local or functional currencies.
- Debt denominated in currencies other than the local or functional currency arranged by the IBERDROLA Group companies.
- Profit or loss in consolidation of the foreign subsidiaries.
- Consolidated carrying amount of investments in foreign subsidiaries.

The IBERDROLA Group reduces this risk by ensuring that all its economic flows are denominated in the functional currency of each Group company, provided that this is possible and economically practicable and efficient. The resulting open positions are integrated and managed through the use of derivatives within the approved limits and holding net borrowings in foreign currencies.

Note 6.c of these Consolidated financial statements includes information on the potential impact of the Brexit on the IBERDROLA Group.

Commodity price risk

The IBERDROLA Group's activities require the acquisition and sale of raw materials (natural gas, coal, fuel oil, gas oil, emission allowances, etc.), whose price is subject to the volatility of international markets (global and regional) where those raw materials are traded.

Likewise, the prices for such raw materials are linked to the price indexes of other raw materials (mainly oil) and, therefore, they also depend on the volatility of the global oil market.

The margin obtained in the operations depends on the relative competitiveness of the IBERDROLA Group's plants compared to its competitors. This relative competitiveness also depends on raw material prices.

Inherent business risk

The activities of the IBERDROLA Group are exposed to a range of business risks related to the uncertainty of the main variables affecting it, such as the evolution of the demand for electricity and gas, the availability of hydroelectric and wind power resources in the electricity production (both for IBERDROLA's and the rest of the competitors that operate in the same market) and the availability of the electricity production plants.

Liquidity risk

Exposure to adverse situations in the debt or capital markets or the IBERDROLA Group's economic and financial situation can hinder or prevent the IBERDROLA Group from obtaining the financing required to properly carry on its business activities.

IBERDROLA Group's liquidity policy is designed to ensure that it can meet its payment obligations without having to obtain financing under unfavourable terms. For this purpose, it uses various management measures such as the arrangement of committed credit facilities of sufficient amount, term and flexibility, diversification of the coverage of financing needs through access to different markets and geographical areas, and diversification of the maturities of the debt issued (Notes 25 and 50).

The balances for cash, liquid assets and available committed credit facilities are sufficient for meeting the Group's liquidity needs for more than 24 months, not including the new financing facilities.

The figures relating to the IBERDROLA Group's debt performance are included in Notes 25 and 50 of the Financial statements.

Credit risk

The IBERDROLA Group is exposed to the credit risk arising from the possibility that counterparties (customers, suppliers, financial institutions, partners, etc.) might fail to comply with contractual obligations. This exposure may arise with regard to unsettled amounts, to the cost of replacing products that are not supplied, as well as, in the case of dedicated plants, to amounts on which depreciation is pending, of said plants.

Credit risk is managed and limited in accordance with the type of transaction and the credit worthiness of the counterparty. Specifically, there is a corporate credit risk policy which establishes criteria for admission, approval systems, authorisation levels, qualification tools, exposure measurement methodologies, exposition limits, mitigation tools, etc.

With regard to credit risk on trade receivables, the historical cost of defaults has remained moderate and stable at close to 1% of total turnover of this activity, despite the current difficult economic environment.

Regarding other exposure (counterparties in transactions with derivatives, placement of cash surpluses, sale transactions involving energy and guarantees received from third parties), in 2016 and 2015 there have been no material non-payments or losses.

At 31 December 2016 and 2015, there was no significant concentration of credit risk for the IBERDROLA Group.

Sensitivity analysis

The following sensitivity analyses show, for each type of risk (without reflecting the interdependence among risk variables), how income for the year and equity might be affected by reasonably possible changes in each risk variable at 31 December 2016 and 2015. Therefore, the sensitivity analysis does not show the effect on income for the year and equity that might have arisen if during 2016 and 2015 the risk variables had been different.

- Financial:

The sensitivity of the consolidated profit and the equity to the variation of the interest rates is as follows:

Thousands of euros	Increase/ decrease in interest rate (basis points)	Impact on profit before taxes Income/(Expense)	Direct impact on equity before taxes	Impact on equity before taxes
2016	+25	1,200	53,070	54,270
	- 25	(1,200)	(53,070)	(54,270)
2015	+25	1,620	75,435	77,055
	- 25	(1,620)	(75,304)	(76,924)

The sensitivity of the consolidated profit and equity of the IBERDROLA Group to changes in the dollar/euro, sterling pound/euro and Brazilian real/euro exchange rate is as follows:

Thousands of euros	Change in the dollar/euro exchange rate	Impact on profit before taxes Income/(Expense)	Direct impact on equity before taxes	Impact on profit before taxes
2016	Depreciation 5%	752	(725,927)	(725,175)
	Appreciation 5%	(831)	802,341	801,510
2015	Depreciation 5%	222	(664,396)	(664,174)
	Appreciation 5%	(245)	734,332	734,087

Thousands of euros	Change in the sterling pound /euro exchange rate	Impact on profit before taxes Income/(Expense)	Direct impact on equity before taxes	Impact on equity before taxes
2016	Depreciation 5%	3,823	(438,573)	(434,750)
	Appreciation 5%	(4,225)	484,738	480,513
2015	Depreciation 5%	13,893	(477,872)	(463,979)
	Appreciation 5%	(15,356)	528,175	512,819

Thousands of euros	Change in the Brazilian real /euro exchange rate	Impact on profit before taxes Income/(Expense)	Direct impact on equity before taxes	Impact on profit before taxes
2016	Depreciation 5%	–	(102,277)	(102,277)
	Appreciation 5%	–	113,043	113,043
2015	Depreciation 5%	–	(83,307)	(83,307)
	Appreciation 5%	–	92,076	92,076

- Raw materials:

The sensitivity of the consolidated profit and the equity to changes in the market prices of the main raw materials is as follows:

Thousands of euros				
Year 2016	Change in price	Impact on profit before taxes Income/ (Expense)	Direct impact on equity before taxes	Impact on equity before taxes
Gas	+ 5%	1,135	15,574	16,709
	- 5%	(1,163)	(15,090)	(16,253)
Electricity	+ 5%	7,574	8,493	16,067
	- 5%	(7,572)	(8,493)	(16,065)
CO2	+ 5%	(64)	404	340
	- 5%	64	(404)	(340)
Coal	+ 5%	(115)	172	57
	- 5%	115	(172)	(57)

Thousands of euros				
Year 2016	Change in price	Impact on profit before taxes Income/ (Expense)	Direct impact on equity before taxes	Impact on equity before taxes
Gas	+ 5%	(6,426)	15,548	9,122
	- 5%	5,523	(15,548)	(10,025)
Electricity	+ 5%	(138)	5,046	4,908
	- 5%	162	(5,046)	(4,884)
CO2	+ 5%	–	2,023	2,023
	- 5%	–	(2,023)	(2,023)
Coal	+ 5%	–	837	837
	- 5%	–	(837)	(837)

6. F ESTIMATES AND SOURCES OF UNCERTAINTY

6.a) Accounting estimates

The most significant estimates made by the IBERDROLA Group in these Consolidated financial statements are as follows:

- Unbilled power supplied:

The revenue figure for each year includes an estimate of the power supplied to customers of deregulated markets but not billed because it had not been measured at year end for reasons relating to the regular meter-reading period. The estimated unbilled power at 31 December 2016 and 2015, amounted to EUR 1,821,047 thousand and EUR 2,218,602 thousand, respectively. This amount is included under "Current assets – Other current trade and other receivables" on the Consolidated statements of financial position at 31 December 2016 and 2015.

- Settlements relating to regulated activities in Spain:

At the end of each year, the IBERDROLA Group estimates the definitive settlements relating to regulated activities in Spain for that year, establishing the shortfall in revenue, if any, that corresponds together with the amount that will be recovered in the future on the basis of the announcements made by the authorities and the periods during which this recovery will take place (Note 4.w).

These estimates are made on the basis of the provisional settlements published up to the date of authorization for issue of the Consolidated financial statements and all available information on the sector.

- Contracts to trade energy supplies:

As mentioned in Note 4.l, the IBERDROLA Group analyses its contracts to trade energy supplies to ensure they are properly classified for accounting purposes. This analysis involves estimating final customer demand and other variables. These estimates are revised at regular intervals.

- Provisions for contingencies and expenses:

As indicated in Note 4.s, the IBERDROLA Group recognises provisions to cover present obligations arising from past events. For this purpose, it must assess the outcome of certain of legal or other nature procedures that are ongoing at the date of authorization for issue of these Consolidated financial statements based on the best information available.

- Useful lives:

The IBERDROLA Group's tangible assets operate over very prolonged periods of time. The Group estimates their useful lives for accounting purposes (Note 4.e) taking into account each asset's technical characteristics, the period over which they are expected to generate economic benefits and the applicable legislation in each case.

- Costs incurred in closing and dismantling electricity production and distribution facilities:

The IBERDROLA Group periodically revises the estimates made concerning the costs to be incurred in the dismantling of its facilities.

- Provision for pensions and similar commitments and restructuring plans:

At each year end, the IBERDROLA Group estimates the current actuarial provision required to cover obligations relating to restructuring plans, pensions and other similar obligations to its employees. In several cases, it involves the valuation of the assets affected to certain plans. In making these estimates, the IBERDROLA Group receives advice from independent actuaries and expert appraisers (Notes 4.o, 4.p and 23).

- Fair value of investment property:

The IBERDROLA Group appraises its investment property each year. While these appraisals are particularly important given the current situation of the real estate market, the IBERDROLA Group considers that its appraisals, commissioned by independent valuers, appropriately reflect this situation.

- Impairment of assets:

As described in Notes 4.i and 12, the IBERDROLA Group, in accordance with applicable accounting regulations, tests the cash-generating units that require testing for impairment each year. Specific tests are also conducted if indications of impairment are detected. These impairment tests require estimating the future cash flows of the businesses and the most appropriate discount rate in each case. The IBERDROLA Group believes its estimates in this respect are appropriate and consistent with the current market situation and reflect its investment plans and the best available estimate of its future expense and income. Also, the discount rates reflect the risk of cash-generating units.

- Other intangible assets:

As disclosed in Note 4.b of these Consolidated financial statements, the "Other intangible assets" heading on the Consolidated statement of financial position includes wind farm projects and gas storage facilities in the development phase. The IBERDROLA Group estimates that these projects meet the identifiability requirement under IAS 38 for them to be capitalised, and that the Group's future investment plans will include the construction of the facilities proposed in these projects.

- Deferred tax assets:

As mentioned in Note 4.z, the IBERDROLA Group only recognizes deferred tax assets when future taxable profits are expected against which the recovery of those assets is possible. In this sense, the IBERDROLA Group performs projections of its taxable earnings to reach a final conclusion, projections that are consistent with the impairment tests mentioned earlier in this Note.

- Assets held for sale and discontinued operations:

The IBERDROLA Group, at each year end, estimates the existence of specific assets or cash-generating units that meet the conditions for their classification as assets held for sale or discontinued operations. The IBERDROLA Group considers that there not assets or generating units that meet the conditions for this presentation as assets held for sale or discontinued operations at 31 December 2016.

6.b) Sources of uncertainty

There are certain aspects that, at the date of the authorization for issue of these Consolidated financial statements, constitute a source of uncertainty concerning the accounting effect:

- Section 12.5 of the Corporate Income Tax Law (*Ley del Impuesto sobre Sociedades*) introduced under the Royal Decree 4/2004, stated that financial goodwill arising from the acquisition of foreign companies was deductible for tax purposes. IBERDROLA is applying said deductibility for the financial goodwill arising from the acquisitions of Scottish Power Plc. (now Scottish Power Ltd.), and Energy East Inc. (now AVANGRID).

In October 2007, the European Commission decided to initiate a formal investigation of the aforementioned tax measure to examine whether it was compatible with the internal market.

In 2009 and 2011 the European Commission issued two Decisions (named First Decision and Second Decision) stating that article 12.5 constituted a forbidden State aid and should be removed. However, deductions could remain in place for acquisitions transacted or agreed before December 2007 (this being the case of the acquisitions made by the IBERDROLA Group) due to the fact that the entities applying them had acted on the ground of legitimate expectations.

In February 2014, the Spanish National High Court (*Audiencia Nacional*) issued a resolution stating that article 12.5 does not apply to indirect acquisitions (i.e. second and lower-level tier subsidiaries). This decision has been appealed against by the IBERDROLA Group and other parties concerned.

In October 2014, the European Commission issued a third decision (named Third Decision) in which it determined that, as the Spanish tax authorities answered in 2012 to several "binding consultations" as to whether indirect acquisitions are deductible under article 12.5, it cannot be understood that the companies that made indirect acquisitions acted on the ground of legitimate expectations. Furthermore, as this was a measure subsequent to the date on which it was disclosed that the formal investigation process had begun, the Commission considered that, for companies which made indirect acquisitions prior to 21 December 2007, no legitimate expectations had been generated, since they were aware of the administrative practice which excluded indirect acquisitions from the scope of application of the tax measure. Therefore, the Commission requested to the Kingdom of Spain, which has appealed against that decision, to recover the aid given.

On 7 November 2014, the General Court of the European Union (TGUE) set aside the two Commission Decisions referred earlier on the ground that the deduction under article 12.5 is not State aid because it is not selective. This Decision has been appealed against by the European Commission.

- On 27 February 2015, the General Court of the European Union issued a resolution rejecting the interim suspension of the Third Decision, which means that Spanish tax authorities should have to recover the aid. However, this Resolution mentions a writing that was sent to the Spanish Kingdom by the General Director for Competition of the Commission, in which it is declared that the recovery of the aid won't be actively pursued until the European Court of Justice does not conclude on the appeals of the Commission against the General Court Resolutions of 7 November 2014.

Furthermore, on the same date it was published the third Decision in the Official Journal of the European Union, against which the IBERDROLA filed the corresponding appeal before the General Court on 22 May 2015.

On 21 December 2016 the Court of Justice of the European Union issued a resolution resolving the appeals submitted by the European Commission against the General Court rulings of 7 November 2014, dismissing said rulings and agreeing to refer the issue back to the Court to rule on the selectivity of the measure and examine the reasons for an appeal stated by the parties concerned, which had not been examined in these rulings. This resolution confirmed the validity of the First and Second Decisions. Consequently, the European Commission declared it will work with the Spanish authorities to implement the refund of the aid granted, including aid that had been declared incompatible with the domestic market by the Third Decision.

Actual recovery of the aid will be provisional, subject to the final outcome of the appeals submitted against the three decisions.

At the date of these Consolidated financial statements, the appeal submitted had not been resolved.

- In 2009, a series of incentives were established to promote renewable energies in the United States that were initially applicable only to wind farms that were brought onstream prior to 31 December 2012. Part of these, specifically, the *Production Tax Credits* (PTC) measured in USD/MWh produced, were extended to wind farms whose construction has begun before 1 January 2015 (Note 3).

In December 2015 PTC were extended to those wind farms which construction will begin before 31 December 2019, but the unitary amount is gradually reduced for those wind farms which construction is initiated from 1 January 2017 onwards.

The IBERDROLA Group considers that this extension of PTC ensures an adequate profitability for the facilities put in use until 2019. Furthermore, the IBERDROLA Group considers that the wind farms, of which construction begins after 2019, would benefit from a remuneration system that will exceed the return required by the IBERDROLA Group for its investments. Therefore, the IBERDROLA Group believes that they will be able to recover its tangible and intangible assets in the United States related to renewable energy sources at the value stated in the Consolidated Statement of financial position at 31 December 2016.

- The IBERDROLA Group has stakes in several nuclear plants, all of which are located in Spain. The Santa María de Garoña nuclear plant, in which the IBERDROLA Group has a 50% stake, came into operation in 1971. It was disconnected from the electricity grid in 2012. The Royal Decree 102/2014, for the responsible and safe management of spent nuclear fuel and radioactive waste, authorises Nuclenor, S.A. (hereinafter "NUCLENOR"), the company that owns the plant, to apply for an extension of the operating licence for the plant for an indefinite period. On 2 June 2014, NUCLENOR applied to the Nuclear Safety Council (*Consejo de Seguridad Nuclear*, hereinafter "CSN") for a new operating licence valid until 2031. On 8 February 2017, the plenary of the CSN has agreed to set the limits and conditions related to the application for renewal of operating authorization of the Santa María de Garoña nuclear power plant. The evaluations conclude that the proposals by NUCLENOR are acceptable, while, from the point of view of safety and radiation protection it is necessary for the holder to carry out additional actions that are identified within limits and conditions on nuclear safety and radiation protection and which are included in the proposal that the CSN has sent to the Ministry of Energy, Tourism and Digital Agenda, which will have six months to issue its resolution. At the date of authorization for issue of these Consolidated financial statements neither the proposal of the CSN nor the resolution of the Ministry of Energy, Tourism and Digital Agenda are available.

The operating licences in effect for the rest of nuclear plants have a term of 30 to 40 years from their coming into operation. Those plants are governed by the Sustainable Economy Law (*Ley de Economía Sostenible*), enacted on 15 February 2011, which provides, with no time limit, that the share of nuclear power in the production mix must be determined in accordance with its production timetable and the licence renewals requested by nuclear plant owners within the framework of the prevailing law.

Taking this into account, as well as the investment and maintenance policies followed at its nuclear plants, the IBERDROLA Group considers that the corresponding operating licences will be renewed at least until those plants are 40 years old. Accordingly, for accounting purposes the plants will be depreciated over the resulting period (Note 4.e).

- The Notes 28 and 43 of these Consolidated financial statements describe the principal contingent liabilities of the IBERDROLA Group, the majority of which have arisen in ongoing litigation, the future course of which cannot be determined with certainty at the date of authorization for issue of these Consolidated financial statements.
- The IBERDROLA Group is currently involved in negotiations and/or arbitration regarding some of its long-term contracts to supply or sell raw materials and believes that their outcomes will not have a significant change on the amounts shown in the Consolidated financial statements.

The IBERDROLA Group and its legal and tax advisors consider that no losses of assets and no significant liabilities will arise for the IBERDROLA Group as a result of the matters detailed in the paragraphs above.

6.c) IBERDROLA and the United Kingdom's referendum result – European Union (BREXIT)

The outcome of the referendum that took place on 23 June 2016 whereby the British people voted for the United Kingdom to leave the European Union (EU) ushered in a period of political and economic uncertainty that could lead to some volatility on finance markets.

At the date of these Consolidated financial statements it is unknown of how the process of negotiations to take the United Kingdom out of the EU will be; the result of the referendum, however, will not entail any immediate changes concerning the status of the United Kingdom's transnational relations. The procedure regulated in article 50 of the Treaty on European Union (TEU) stipulates that negotiations may be conducted over a period of up to two years once the United Kingdom has notified the European Council of its intention to leave the EU, and this period may be extended by mutual agreement between both parties.

However, IBERDROLA believes that there will be no significant short-term impact for the following reasons:

- Currency diversification offsets the potential impact of the Brexit in that the expected trend in the US dollar partially compensates for the impact of Brexit on the sterling pound.
- Approximately 80% of total EBITDA generated by the IBERDROLA Group in the United Kingdom is accounted for by Regulated (Transmission - Distribution) and Renewables businesses. Both these areas of business have stable predictable regulation. In general, British regulatory frameworks set values in real terms in the long term, and therefore any future inflationary tensions would not affect the expected returns.
 - o Distribution: Remuneration guaranteed up to 2023 by the RIIOD-1 regulatory framework.
 - o Transmission: Remuneration guaranteed up to 2021 by the RIOT1 regulatory framework.
 - o Renewables: existing facilities and new projects, such as the East Anglia offshore wind power project, have the backing of the approved remuneration mechanisms: Renewables Obligation Certificates (ROCs) and Contracts for Differences (CfDs), respectively; which affect the first 15-20 years of asset useful life.

The IBERDROLA Group's EBITDA (gross operating profit) and Net profit for 2016 from the sterling pound and the US dollar are as follows:

2016	EBITDA	Net profit
Sterling pound	20.0%	20.8%
US dollar	29.8%	26.3%

- The strategy of funding in the same currency as the currency in which earnings and funds from operations are generated protects solvency ratios (Net Debt/EBITDA or Funds From Operations (FFO)/Net Debt).
 - o Solvency ratios: Solvency ratios are practically immune to major EUR/GBP exchange rate fluctuations. Changes in the EUR/GBP exchange rate would also have a similar effect on debt and FFO/EBITDA ratios.

2016	EBITDA	FFO	Net debt and derivatives
Sterling pound	20.0%	20.6%	21.2%

- Exchange rate: For the 2016 year end, the contribution by the Sterling pound to the IBERDROLA Group's net profit is fully hedged by derivatives or other financial instruments.
- 75% of 2016-2020 investment projects in the United Kingdom included in the strategic plan (GBP 6,400 million) do not entail any currency risk, and a further 21% have price review clauses.

The IBERDROLA Group therefore believes that, since most of its businesses in the United Kingdom are regulated and since the supplies of electricity constitute an essential service, the sensitivity analyses performed demonstrate that none of its British cash-generating units are showing any signs of impairment at the date of these Consolidated financial statements.

7. GEOGRAPHICAL AND BUSINESS SEGMENT REPORTING

IFRS 8: "Operating segments" provides that an operating segment is a component of an entity:

- that engages in business activities from which it may earn revenues and incur expenses (including revenues and expenses relating to transactions with other components of the same entity),
- which operating results are reviewed regularly by the entity's chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance, and
- for which discrete financial information is available.

Transactions among different segments are carried out on market basis.

The operating segments identified by the IBERDROLA Group are as follows:

- Network business: including all the energy transmission and distribution activities, and any other regulated activity originated in Spain, the United Kingdom, the United States and Brazil.
- Deregulated business: including electricity generation and sales businesses as well as gas trading and storage businesses carried on by the Group in Spain, Portugal, the United Kingdom and North America.
- Renewable business: activities related to renewable energies in Spain, the United Kingdom, the United States and the rest of the world.
- Other businesses: including the engineering and construction businesses and the non-power businesses.

Additionally, Corporation includes the costs of the Group's structure (Single Corporation), of the administration services of the corporate areas that are subsequently invoiced to the other companies through specific service agreements.

The IBERDROLA Group manages globally not only the financial activities but also the effects of taxation on profits. Consequently, financial income and expenses and Income Tax have not been allocated to operating segments.

The key figures for the operating segments identified are as follows:

Business segment reporting for 2016

Thousands of euros	Desregulated				Renewable					Network					Other businesses	Total segments	Corporation and adjustments	
	Spain and Portugal	United Kingdom	North America	Total	Spain	United Kingdom	United States	Rest of the world	Total	Spain	United Kingdom	United States	Brazil	Total	Total	Total	Total	Total
NET REVENUE																		
External revenues	12,004,791	5,361,763	1,568,422	18,934,976	44,543	56,374	963,971	235,365	1,300,253	1,909,088	1,106,035	3,979,421	1,458,544	8,453,088	751,868	29,440,185	(224,803)	29,215,382
Inter-segment revenues	(124,258)	106,566	46,263	28,571	732,700	367,240	–	(560)	1,099,380	140,588	213,058	–	–	353,646	1,740	1,483,337	20,076	1,503,413
Intercompany eliminations	–	–	–	(240,175)	–	–	–	–	–	–	–	–	–	–	–	(240,175)	(1,263,238)	(1,503,413)
Total revenues	–	–	–	18,723,372	–	–	–	–	2,399,633	–	–	–	–	8,806,734	753,608	30,683,347	(1,467,965)	29,215,382
INCOME STATEMENT																		
Segment operating profit	986,453	17,161	309,516	1,313,130	250,626	126,788	218,225	107,143	702,782	1,100,314	692,426	729,464	126,991	2,649,195	(124,878)	4,540,229	13,807	4,554,036
Share in net profit of companies accounted for using the equity method	(25,693)	(100)	19,591	(6,202)	366	1,139	(9,406)	(5,505)	(13,406)	1,808	95	11,728	41,779	55,410	58,064	93,866	(45,143)	48,723
ASSETS																		
Segment assets	9,405,437	6,777,831	4,352,599	20,535,867	4,395,626	5,533,538	11,873,056	1,650,603	23,452,823	10,991,733	11,502,554	20,631,805	1,552,638	44,678,730	1,816,222	90,483,642	821,795	91,305,437
Investments in companies accounted for using the equity method	5,953	1,825	438,914	446,692	61,879	7,908	144,788	110,010	324,585	51,395	92	143,107	657,082	851,676	616,793	2,239,746	(91)	2,239,655
LIABILITIES																		
Segment liabilities	2,286,718	757,531	632,484	3,676,733	468,475	453,827	1,949,411	165,334	3,037,047	5,778,964	1,698,568	3,329,316	431,133	11,237,981	462,722	18,414,483	1,051,839	19,466,322
OTHER INFORMATION																		
Total cost incurred during the period in the acquisition of property, plant and equipment and non-current intangible assets	224,701	134,839	413,818	773,358	15,989	961,540	690,925	120,680	1,789,134	512,916	792,534	843,808	83,707	2,232,965	1,847	4,797,304	(51,244)	4,746,060
Depreciation and amortisation expenses	534,056	276,432	129,693	940,181	246,807	140,186	345,419	65,055	797,467	502,755	283,813	540,173	105,762	1,432,503	13,585	3,183,736	69,970	3,253,706
Expenses of the period other than depreciation and amortisation that did not result in cash outflows	22,556	5,567	964	29,087	3,025	–	8,563	–	11,588	26,582	21,607	63,609	840	112,638	3,077	156,390	104,640	261,030

Business segment reporting for 2015 (Restated Note 2.c)

	Desregulated				Renewable					Network					Other businesses	Total Segment s	Corporation and adjustments	
	Spain and Portugal	United Kingdom	North America	Total	Spain	United Kingdom	United States	Rest of the world	Total	Spain	United Kingdom	United States	Brazil	Total	Total	Total	Total	Total
NET REVENUE																		
External revenues	12,752,414	7,528,930	1,537,721	21,819,065	12,041	253,895	1,008,341	219,026	1,493,303	1,790,993	1,266,694	2,674,947	1,735,404	7,468,038	865,548	31,645,954	(227,261)	31,418,693
Inter-segment revenues	26,695	32,865	52,582	112,142	752,500	543,897	(31)	897	1,297,263	174,030	266,910	8	–	440,948	4,745	1,855,098	(42,263)	1,812,835
Intercompany eliminations	–	–	–	(314,105)	–	–	–	–	–	–	–	–	–	–	–	(314,105)	(1,498,730)	(1,812,835)
Total revenues	–	–	–	21,617,102	–	–	–	–	2,790,566	–	–	–	–	7,908,986	870,293	33,186,947	(1,768,254)	31,418,693
INCOME STATEMENT																		
Segment operating profit	969,553	(283,006)	275,398	961,945	194,029	248,113	125,306	91,660	659,108	1,014,108	828,631	497,087	145,483	2,485,309	(30,111)	4,076,251	(246,964)	3,829,287
Share in net profit of companies accounted for using the equity method	(29,920)	(603)	(4,691)	(35,214)	2,910	(5,178)	(2,636)	5,043	139	212	–	486	56,040	56,738	46,633	68,296	(12,978)	55,318
ASSETS																		
Segment assets	10,095,990	8,015,713	3,891,452	22,003,155	4,848,182	5,685,573	10,934,171	904,955	22,372,881	10,743,395	12,487,333	18,761,795	1,324,076	43,316,599	1,856,121	89,548,756	762,163	90,310,919
Investments in companies accounted for using the equity method	17,352	2,210	307,305	326,867	57,430	14,931	155,217	161,201	388,779	51,845	–	100,718	587,294	739,857	594,781	2,050,284	(101)	2,050,183
LIABILITIES																		
Segment liabilities	2,673,880	909,920	616,415	4,200,215	461,633	417,283	1,989,644	122,262	2,990,822	5,938,202	1,834,208	2,989,898	451,212	11,213,520	426,846	18,831,403	932,875	19,764,278
OTHER INFORMATION																		
Total cost incurred during the period in the acquisition of property, plant and equipment and non-current intangible assets	265,694	104,305	373,486	743,485	113,998	566,194	173,374	184,476	1,038,042	481,429	1,004,739	559,561	76,024	2,121,753	1,191	3,904,471	(74,348)	3,830,123
Depreciation and amortisation expenses	535,005	704,754	121,535	1,361,294	279,198	189,973	445,640	73,287	988,098	442,627	309,383	283,451	107,034	1,142,495	19,562	3,511,449	56,659	3,568,108
Expenses of the period other than depreciation and amortisation that did not result in cash outflows	23,314	63,815	3,116	90,245	3,770	3,075	7,460	204	14,509	34,102	48,496	43,863	1,521	127,982	9,753	242,489	46,672	289,161

Additionally the net revenue and non-current assets by geographical area is as follows:

Thousands of euros	12.31.2016	12.31.2015
Net revenue		
Spain	13,453,880	14,470,382
United Kingdom	6,627,660	9,119,973
North America	6,863,387	5,710,284
Brazil	1,578,281	1,829,692
Rest of the world	692,174	288,362
Total	29,215,382	31,418,693

Thousands of euros	12.31.2016	12.31.2015
Non-current assets (*)		
Spain	23,537,117	23,875,710
United Kingdom	21,898,039	24,181,832
North America	35,837,302	32,666,875
Brazil	1,444,265	1,197,105
Rest of the world	1,514,166	1,107,415
Total	84,230,889	83,028,937

(*) Excluding non-current financial assets, deferred tax assets and non-current trade and other receivables.

In addition, the reconciliation between segment assets and liabilities and the total assets and liabilities in the Consolidated statement of financial position is as follows:

Thousands of euros	12.31.2016	12.31.2015
Segment assets	91,305,437	90,310,919
Non-current financial assets	3,903,994	3,711,006
Deferred tax assets	6,958,154	6,629,508
Current trade and other receivables	984,377	893,891
Current financial investments	1,474,790	1,287,623
Income tax receivables	503,403	411,322
Other tax receivables	143,379	266,640
Cash and cash equivalents	1,432,686	1,153,273
Total Assets	106,706,220	104,664,182

Thousands of euros	12.31.2016	12.31.2015
Segment liabilities	19,466,322	19,764,278
Equity	40,687,389	40,956,053
Non-current equity instruments having the substance of a financial liability	43,664	117,209
Non-current bank borrowings	26,926,882	24,899,010
Deferred tax liabilities	12,740,661	11,896,477
Other non-current payables	737,269	689,694
Current equity instruments having the substance of a financial liability	93,390	99,221
Current bank borrowings	5,404,119	5,662,019
Other current liabilities	606,524	580,221
Total Equity and Liabilities	106,706,220	104,664,182

8. INTANGIBLE ASSETS

The changes in 2016 and 2015 in intangible assets accounts and in the related accumulated amortisation and provisions were as follows:

Thousands of euros	Balance at 01.01.15	Translation differences	Modification of the consolidation perimeter (Note 42)	Additions or (charges) / reversals	Capitalised staff costs (Note 35)	Transfers	Disposals, derecognition and reductions	Balance at 12.31.15	Translation differences	Modification of the consolidation perimeter (Note 42)	Additions or (charges) / reversals	Capitalised staff costs (Note 35)	Transfers	Disposals, derecognition and reductions	Balance at 12.31.16
Cost:															
Goodwill	8,354,186	515,900	482,703	–	–	–	–	9,352,789	(605,188)	(35,351)	–	–	–	(1,197)	8,711,053
Concessions, patents, licenses, trademarks and others	5,400,539	234,755	1,896,685	11,161	–	2,854	(110)	7,545,884	29,993	104,888	15,553	–	92	(1)	7,696,409
Intangible assets classified under IFRIC 12	837,519	(199,511)	–	78,412	23,589	(6,647)	(6,854)	726,508	179,979	–	84,089	23,696	(32,512)	(14,986)	966,774
Computer software	1,270,190	44,970	235,774	124,405	5,350	340,573	(151,774)	1,869,488	(32,150)	–	143,269	7,377	24,234	(52,201)	1,960,017
Emission allowances	88	–	–	–	–	–	(88)	–	–	–	–	–	–	–	–
Other intangible assets	4,417,688	407,322	838,576	20,062	–	(755,372)	(66,575)	4,861,701	(17,649)	25,639	10,678	–	(371,402)	(4,542)	4,504,425
Total cost	20,280,210	1,003,436	3,453,738	234,040	28,939	(418,592)	(225,401)	24,356,370	(445,015)	95,176	253,589	31,073	(379,588)	(72,927)	23,838,678
Accumulated amortisation and provisions															
Concessions, patents, licenses, trademarks and others	651,522	(5,712)	–	95,381	–	1,358	–	742,549	(43,632)	–	80,930	–	–	–	779,847
Intangible assets classified under IFRIC 12	178,159	(50,199)	–	51,067	–	36,141	(5,902)	209,266	55,604	–	51,505	–	–	(5,877)	310,498
Computer software	871,545	32,285	105,014	158,253	–	245,881	(150,440)	1,262,538	(12,634)	–	164,905	–	1,691	(52,003)	1,364,497
Other intangible assets	928,254	73,921	–	30,738	–	(461,442)	(16,481)	554,990	(47,291)	–	146,688	–	–	(3,173)	651,214
Total accumulated amortisation	2,629,480	50,295	105,014	335,439	–	(178,062)	(172,823)	2,769,343	(47,953)	–	444,028	–	1,691	(61,053)	3,106,056
Impairment allowances (Note 12)	788,500	88,449	–	(49,528)	–	–	–	827,421	39,220	–	(68,182)	–	–	–	798,459
Total accumulated amortisation and provisions	3,417,980	138,744	105,014	285,911	–	(178,062)	(172,823)	3,596,764	(8,733)	–	375,846	–	1,691	(61,053)	3,904,515
Total carrying amount	16,862,230	864,692	3,348,724	(51,871)	28,939	(240,530)	(52,578)	20,759,606	(436,282)	95,176	(122,257)	31,073	(381,279)	(11,874)	19,934,163

The fully amortised intangible assets in use at 31 December 2016 and 2015 amounted to EUR 384,669 thousand and EUR 323,129 thousand, respectively.

The IBERDROLA Group maintains at 31 December 2016 and 2015 commitments to acquire intangible assets for EUR 44,655 and EUR 8,814 thousand.

In addition, at 31 December 2016 and 2015, there were no significant restrictions on the ownership of intangible assets, except for the regulated businesses that may require authorisation of the corresponding regulator for specific transactions.

The allocation of goodwill to the cash generating units at 31 December 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Electricity and gas generation and supply in the UK	4,391,911	5,052,019
Regulated activities in the UK	677,949	779,845
Renewable energies in the UK	428,179	492,535
Renewable energies in the USA	1,460,337	1,386,866
Regulated activities in the USA	1,143,048	1,120,892
Regulated activities in Brazil	175,224	141,688
Corporate activities and others	434,405	378,944
Total	8,711,053	9,352,789

The allocation of indefinite life and in-progress intangible assets at 31 December 2016 and 2015 to the various cash generating units is as follows:

2016			
Thousands of euros	Intangible assets with indefinite useful lives	Intangible assets in progress	Total
Electricity distribution in Scotland	781,646	–	781,646
Electricity distribution in Wales and England	752,279	–	752,279
Electricity transmission in the UK	297,082	–	297,082
Renewable energies in the USA	–	257,681	257,681
Electricity and gas distribution in New York (NYSEG)	1,139,094	–	1,139,094
Electricity and gas distribution in New York (RG&E)	1,026,721	–	1,026,721
Electricity transmission and distribution in Maine (CMP)	282,876	20,960	303,836
Electricity transmission and distribution in Connecticut (UI)	1,186,251	–	1,186,251
Gas distribution in Connecticut (CNG)	299,325	–	299,325
Gas distribution in Connecticut (SCG)	587,610	–	587,610
Gas distribution in Massachusetts (BGC)	40,076	–	40,076
Others	–	367,121	367,121
Total	6,392,960	645,762	7,038,722

2015			
Thousands of euros	Intangible assets with indefinite useful lives	Intangible assets in progress	Total
Electricity distribution in Scotland	899,128	–	899,128
Electricity distribution in Wales and England	865,347	–	865,347
Electricity transmission in the UK	341,734	–	341,734
Renewable energies in the UK	–	382,333	382,333
Renewable energies in the USA	–	201,809	201,809
Electricity and gas distribution in New York (NYSEG)	1,081,786	–	1,081,786
Electricity and gas distribution in New York (RG&E)	975,066	–	975,066
Electricity transmission and distribution in Maine (CMP)	268,644	35,193	303,837
Electricity transmission and distribution in Connecticut (UI)	1,023,797	–	1,023,797
Gas distribution in Connecticut (CNG)	282,152	–	282,152
Gas distribution in Connecticut (SCG)	558,047	–	558,047
Gas distribution in Massachusetts (BGC)	38,061	–	38,061
Others	–	355,735	355,735
Total	6,333,762	975,070	7,308,832

9. INVESTMENT PROPERTY

The changes in 2016 and 2015 in the IBERDROLA Group's investment property were as follows:

Thousands of euros	Balance at 01.01.15	Additions/ (charge)/ reversals	Transfers	Decreases, disposals or reductions	Balance at 12.31.15	Additions/ (charge)/ reversals	Transfers	Decreases, disposals or reductions	Balance at 12.31.16
Investment property	560,547	4,713	(2,188)	(1,199)	561,873	7,321	(9,683)	(14,396)	545,115
Impairment provision	(38,064)	–	6,111	–	(31,953)	–	4,118	–	(27,835)
Accumulated depreciation	(40,138)	(7,516)	(1,716)	191	(49,179)	(7,446)	1	1,686	(54,938)
Total carrying amount	482,345	(2,803)	2,207	(1,008)	480,741	(125)	(5,564)	(12,710)	462,342

The fair value of the investment properties in use at 31 December 2016 and 2015 was EUR 530,112 thousand and EUR 540,018 thousand, respectively. This fair value was generally calculated as described in Note 4.c., and it would be considered as Level 3.

At 31 December 2016 and 2015, none of the investment properties had been fully depreciated and there were no restrictions on their realisation. Moreover, there were no contractual obligations to acquire, build, develop, repair or maintain investment property.

10. PROPERTY, PLANT AND EQUIPMENT

The changes in 2016 and 2015 in property, plant and equipment accounts and in the related accumulated amortised and provisions were as follows:

Thousands of euros	Balance at 01.01.15	Translation differences	Modification of the consolidation perimeter (Note 42)	Additions and charges / (reversals)	Transfers	Decreases, disposals or reductions	Write-offs	Balance at 12.31.15	Translation differences	Modification of the consolidation perimeter (Note 42)	Additions and charges / (reversals)	Transfers	Decreases, disposals or reductions	Write-offs	Balance at 12.31.16
Cost:															
Land and buildings	1,296,046	54,339	–	59,468	457,033	(18,167)	–	1,848,719	25,707	(4,904)	65,379	375,359	(10,673)	–	2,299,587
Operating plants															
Hydroelectric plants	6,319,578	45,121	–	–	438,415	(119)	–	6,802,995	(36,321)	–	–	77,458	(797)	–	6,843,335
Thermal power plants	2,710,268	88,721	–	20,035	3,016	(3,132)	–	2,818,908	(151,000)	–	544	15,414	(1,467,171)	–	1,216,695
Combined cycle plants	7,147,320	377,042	–	16,008	135,457	(94,789)	–	7,581,038	(8,272)	–	25,652	396,373	(19,667)	–	7,975,124
Nuclear plants	7,366,231	–	–	47,707	105,801	(60,437)	–	7,459,302	–	–	(5,017)	109,408	(55,363)	–	7,508,330
Wind-powered facilities	21,335,182	1,356,647	–	178,750	497,769	(65,893)	–	23,302,455	73,997	–	(92,938)	(197,529)	(82,026)	–	23,003,959
Facilities including:															
Gas storage facilities and other alternative plants	1,329,458	91,883	–	194	3,464	(32)	–	1,424,967	73,332	–	140	49,336	(290)	–	1,547,485
Electricity transmission facilities	5,269,626	456,777	–	–	622,324	(12,950)	–	6,335,777	(173,212)	–	–	1,270,828	(38,545)	–	7,394,848
Gas transmission facilities	45,682	4,008	–	–	(303)	–	–	49,387	2,775	–	–	–	–	–	52,162
Electricity distribution facilities	26,059,718	826,139	2,107,027	102,366	953,595	(50,953)	–	29,997,892	(657,281)	–	73,502	811,803	(39,868)	–	30,186,048
Gas distribution facilities	1,260,051	145,990	1,621,957	–	(90,685)	(2,988)	–	2,934,325	143,087	–	–	(180,454)	(11,107)	–	2,885,851
Meters and measuring devices	1,652,283	65,211	–	134,770	114,658	(130,906)	–	1,836,016	(29,048)	–	199,700	285,569	(186,300)	–	2,105,937
Dispatching centres and other facilities	1,604,182	27,328	41,931	3,626	85,197	(33,263)	–	1,729,001	(8,370)	–	3,451	136,386	(1,844)	–	1,858,624
Total operating plants in use	82,099,579	3,484,867	3,770,915	503,456	2,868,708	(455,462)	–	92,272,063	(770,313)	–	205,034	2,774,592	(1,902,978)	–	92,578,398
Other items of property, plant and equipment in use	1,953,551	113,152	–	93,577	(589,685)	(128,871)	–	1,441,724	19,127	–	133,516	214,981	(102,288)	–	1,707,060
Plants in progress	3,793,113	223,685	249,387	3,355,040	(2,697,013)	(13,684)	(26,858)	4,883,670	(158,301)	–	4,401,277	(2,918,251)	(13,648)	(29,245)	6,165,502
Advances and other items of property, plant and equipment in progress(*)	331,195	20,349	–	147,519	(92,783)	(83,550)	(19,403)	303,327	22,791	–	397,330	(85,042)	(77,235)	–	561,171
Total cost	89,473,484	3,896,392	4,020,302	4,159,060	(53,740)	(699,734)	(46,261)	100,749,503	(860,989)	(4,904)	5,202,536	361,639	(2,106,822)	(29,245)	103,311,718

(*) Advances at 31 December 2016 and 2015 were EUR 306,178 thousand and EUR 60,249 thousand, respectively.

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	Balance at 01.01.15	Translation differences	Modification of the consolidation perimeter (Note 42)	Additions and charges / (reversals)	Transfers	Decreases, disposals or reductions	Write-offs	Balance at 12.31.15	Translation differences	Modification of the consolidation perimeter (Note 42)	Additions and charges / (reversals)	Transfers	Decreases, disposals or reductions	Write-offs	Balance at 12.31.16
Thousands of euros															
Accumulated depreciation and provisions:															
Buildings	288,461	12,770	–	33,666	90,851	(8,594)	–	417,154	1,621	–	35,695	53,603	(7,039)	–	501,034
Plants in use															
Hydroelectric plants	3,560,719	13,969	–	117,335	(2,058)	(71)	–	3,689,894	(19,912)	–	128,464	(15,996)	(558)	–	3,781,892
Thermal power plants	1,832,690	46,362	–	155,263	(21,931)	–	–	2,012,384	(92,123)	–	25,813	(1,683)	(915,795)	–	1,028,596
Combined cycle plants	2,468,728	133,706	–	271,929	8,847	(77,900)	–	2,805,310	(29,667)	–	275,084	–	(17,356)	–	3,033,371
Nuclear plants	5,093,605	–	–	272,937	–	(60,437)	–	5,306,105	–	–	261,859	–	(54,102)	–	5,513,862
Wind-powered facilities	5,450,539	290,028	–	893,100	9	(20,214)	–	6,613,462	44,137	–	730,544	(247,842)	(9,601)	–	7,130,700
Facilities including:															
Gas storage facilities and other alternative plants	258,243	14,283	–	26,023	396	–	–	298,945	15,775	–	26,985	19,629	(236)	–	361,098
Electricity transmission facilities	1,274,407	111,838	–	128,962	(95,685)	(11,660)	–	1,407,862	(38,940)	–	132,617	127,942	(17,233)	–	1,612,248
Gas transmission facilities	10,928	895	–	303	–	–	–	12,126	707	–	298	–	–	–	13,131
Electricity distribution facilities	9,466,813	279,978	466,199	619,888	87,457	(35,458)	–	10,884,877	(123,233)	–	694,741	15,033	(29,209)	–	11,442,209
Gas distribution facilities	465,475	53,176	738,257	23,543	(42,802)	(2,629)	–	1,235,020	61,394	–	46,165	(102,736)	(5,625)	–	1,234,218
Meters and measuring devices	1,016,149	33,844	–	98,114	30,912	(128,622)	–	1,050,397	(40,835)	–	125,020	51,132	(186,200)	–	999,514
Dispatching centres and other facilities	803,271	22,760	9,659	16,173	(368)	(32,600)	–	818,895	(13,661)	–	46,247	17,485	(1,690)	–	867,276
Total	31,701,567	1,000,839	1,214,115	2,623,570	(35,223)	(369,591)	–	36,135,277	(236,358)	–	2,493,837	(137,036)	(1,237,605)	–	37,018,115
Other items of property, plant and equipment in use	1,286,283	66,185	–	93,244	(346,061)	(126,846)	–	972,805	4,510	–	106,886	75,431	(88,627)	–	1,071,005
Total accumulated amortisation	33,276,311	1,079,794	1,214,115	2,750,480	(290,433)	(505,031)	–	37,525,236	(230,227)	–	2,636,418	(8,002)	(1,333,271)	–	38,590,154
Impairment provisions (Note 12)	1,089,871	63,114	–	282,692	–	–	–	1,435,677	(22,869)	–	–	–	(525,628)	–	887,180
Total accumulated amortisation and provisions	34,366,182	1,142,908	1,214,115	3,033,172	(290,433)	(505,031)	–	38,960,913	(253,096)	–	2,636,418	(8,002)	(1,858,899)	–	39,477,334
Total carrying amount	55,107,302	2,753,484	2,806,187	1,125,888	236,693	(194,703)	(46,261)	61,788,590	(607,893)	(4,904)	2,566,118	369,641	(247,923)	(29,245)	63,834,384

The breakdown by business of the main investments made in property, plant and equipment in 2016 and 2015, additional to the ones included in the acquisition of UIL (Note 42) and not including the capitalization of financial (Note 40) nor staff costs (Note 35) is as follows:

Thousands of euros	12.31.2016	12.31.2015
Spain and Portugal deregulated	219,697	263,707
United Kingdom deregulated	109,428	75,186
North America deregulated	398,560	364,594
Spain renewables	8,293	113,234
United Kingdom renewables	909,740	563,421
United States renewables	689,475	21,561
Rest of the world renewables	91,379	178,894
Spain networks	498,322	457,758
United Kingdom networks	779,772	1,001,471
United States networks	792,963	539,007
Brazil networks	–	223
Corporation and others	10,342	30,061
Total	4,507,971	3,609,117

The "Amortisation and provisions" heading, in the Consolidated income statement for 2016 includes EUR 29,245 thousand for impairment and write-offs of property, plant and equipment of the IBERDROLA Group. In 2015 this heading included a debit of EUR 328,953 thousand. (Note 12).

The breakdown by asset type of impairment charges/(reversals) recognised in 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Thermal power plant (Note 12)	–	274,617
Wind-powered facilities	–	8,075
Total Additions/ Reversals	–	282,692

In 2016 the Longannet coal-fired power plant in the United Kingdom was closed, resulting in a decrease in the "Property, plant and equipment" heading of EUR 1,348,124 thousand gross cost, EUR 842,929 thousand of accumulated depreciation and EUR 505,195 thousand of provision for impairment (Note 12).

The value of fully depreciated items of property, plant and equipment in use at 31 December 2016 and 2015 was EUR 2,909,361 thousand and EUR 3,174,597 thousand, respectively.

The IBERDROLA Group maintains, at 31 December 2016 and 2015, commitments to acquire property, plant and equipment amounted to EUR 5,275,933 and EUR 3,652,397 thousand, respectively.

At 31 December 2016 and 2015, the heading "Property, plant and equipment – Property, plant and equipment in use" included EUR 193,044 and EUR 171,856 thousand, respectively, for assets held under finance leases corresponding primarily to IBERDROLA Group's corporate offices in Madrid, among other assets. The minimum payments on the lease contracts at 31 December 2016 is as follows:

Thousands of euros	12.31.2016
2017	33,899
2018-2021	48,721
From 2022 on	129,230
Total amounts payable	211,850
Finance cost	43,493
Present value of the payments	168,357
Total	211,850

11. CONCESSION ARRANGEMENTS

A description is set out below of electricity distribution service concession arrangements in Brazil within the scope of IFRIC 12: "Service Concession Arrangements" (Note 4.b):

Company	Nº of towns	Address	Grant date	Due date	Tariff cycle	Last review
ELEKTRO	223	Estado do Sao Paulo	08/27/1998	08/26/2028	4 years	August 2015
ELEKTRO	5	Mato Grosso do Sul	08/27/1998	08/26/2028	4 years	August 2015

The duration of each concession is 30 years, and they may be extended for up to 30 years upon application by the concession holder and at the discretion of the concession grantor, which is the *Agência Nacional de Energia Elétrica* (ANEEL). The main duties and obligations of the concession holder within the terms of the concession contract are to supply electricity to clients within its concession area, carry out construction work as necessary to provide service, and maintain the assets relating to the concession (Note 4.b).

The concession holder may not transfer such assets or use them as collateral without the prior written consent of the regulatory body.

At the end of a concession the property reverts automatically to the concession grantor and the amount of indemnification due to the concession holder is assessed and determined.

The price of services provided to consumers is regulated, and is composed as follows: Parcel A (non-controllable costs, such as energy purchases, transmission and sector charges, among others) and Parcel B (efficient operating costs and capital costs – return on the investment and the regulatory reimbursement). The adjustment mechanisms are the annual tariffs and the ordinary tariff review conducted every four years.

In late 2014, ELEKTRO's concession arrangements described above as well as the dealership distribution agreements of electricity in Brazil belonging to NEOENERGIA (Notes 13.c and 27) was edited to ensure that at the end of the concession period they are considered for the calculation of compensation remaining balances (assets or liabilities) for the eventual failure of recognition or payment for the rate of Parcel A and other financial components.

12. IMPAIRMENT OF NON-FINANCIAL ASSETS

Methodology of impairment tests

At least yearly, the IBERDROLA Group analyses its assets for indications of impairment. If such indications are found, an impairment test is conducted.

In addition, the IBERDROLA Group conducts a systematic analysis of the impairment of cash-generating units that include goodwill or intangible assets which have not come into use or with indefinite useful life.

The projections used in the impairment tests are based on the best forecast information held by the IBERDROLA Group and include the investment plans for each country prevailing at that time.

a) Assumptions used in deregulated business:

- Production of the facilities: the hours of operation used are consistent with those in previous years, and in line with the expected evolution of the energy mix of the countries where the IBERDROLA Group operates.
- Selling prices of electricity and gas: the selling prices used are the ones agreed upon in the signed price purchase agreements. For unsold production, future prices in the market where the IBERDROLA Group operates are used. With reference to the gas storage activity in the United States and Canada, futures prices from the North American gas market have been used for the period presenting liquidity, while prices for subsequent periods have been taken from external sources.
- Gas purchase prices: the prices used are taken from long-term purchase agreements signed by the IBERDROLA Group, estimating the variables included in them according to external studies.
- Electricity and gas retail margin: growth forecasts were used for the number of customers and unit margins based on the knowledge of the markets in which the IBERDROLA Group operates and the company's relative position in each of them.
- Investment: the best information available has been used on investment plants which are going to be put in use in the coming years.
- Operation and maintenance costs: signed long-term maintenance contracts were considered. Other operating costs were projected consistent with the expected growth of each cash-generating unit, assuming its headcount grows at the same pace.

b) Assumptions used in the regulated business:

- Regulated remuneration: approved remuneration has been used for years in which it is available, while in subsequent periods revision mechanisms of such remuneration set in different regulations have been used, and these have been applied in line with the estimated costs of the corresponding cash-generating units.
- Investment: the projections were based on investment plans consistent with the expected demand growth in each concession, with the minimum required by different regulators and with the estimate of future remuneration used.
- Operation and maintenance costs: the best estimate available of the performance of the operation and maintenance cost was used, which is in line with the remuneration assumed to be received in each year.

c) Assumptions used in the renewables business:

- Production of the facilities: the hours of operation of each plant are consistent with their historical output. In this respect, the long term predictability of wind output should be taken into account, which is also covered in almost all countries by regulatory mechanisms that enable wind farms to produce whenever meteorological and network conditions allow it.
- Electricity sale prices: the prices established in the sales contracts entered into have been used, if applicable. For the production not sold, the prices of futures of the markets where the IBERDROLA Group operates are used. In any case, the existing support mechanisms have been taken into account.
- As described in Note 6.b, an estimate has been made of the regulation that will apply to USA facilities whose construction starts on 31 December 2019.
- Investment: the projections were based on the best information available on wind farms which are expected to be operational in the coming years, taking into account the fixed prices stated in the contracts to buy turbines from various suppliers, including GAMESA (Note 49) and the technical and financial capacity of the IBERDROLA Group to successfully complete the planned projects.
- Operation and maintenance costs: prices set in land leases and maintenance agreements for the useful life of the facilities were used, where the high predictability of the costs of wind farms must be taken into account.

d) Forecast period and nominal growth rate:

The forecast period of future cash flows and the nominal growth rate (g) used to extrapolate such projections beyond the period covered are summarized in the table below:

Cash-generating unit	Number of years	g
Electricity and gas generation and retail in the UK	Useful life / 10	- / 1.5%
Electricity distribution in Scotland	10	2.5%
Electricity distribution in England and Wales	10	2.5%
Electricity transmission in the UK	10	2.5%
Renewable energies in the UK	Useful life	-
Renewable energies in the USA	Useful life	-
Gas storage in the USA	Useful life	-
Gas storage in Canada	Useful life	-
Electricity and gas distribution in New York (NYSEG)	10	0.8%
Electricity and gas distribution in New York (RG&E)	10	0.8%
Electricity transmission and distribution in Maine (CMP)	10	0.8%
Electricity transmission and distribution in Connecticut (UI)	10	0.8%
Distribution of gas in Connecticut (CNG)	10	0.8%
Distribution of gas in Connecticut (SCG)	10	0.8%
Distribution of gas in Massachusetts (BGC)	10	0.8%
Regulated activities in Brazil (ELEKTRO)	Concession life	-

Although IAS 36; "Impairment of assets" recommends the use of projections to five years for impairment test purposes, IBERDROLA has decided to use the periods included in this table for the following reasons:

- The most appropriate method for assets in the generation business is using their remaining useful lives. This is due to the fact that in the Deregulated and Renewable business there are long-term energy sale contracts in force and long-term estimated prices curves are frequently used in the operating activity of the IBERDROLA Group (contracts, hedges, etc.).
- The electricity transmission and distribution concessions include longer regulatory periods and the method that the regulator will use to calculate the new tariff at the beginning of the new regulatory period is known.
- The IBERDROLA Group considers its projections to be reliable and that past experience demonstrates its ability to predict cash flows in periods such as those under consideration.

Moreover, the nominal growth rate considered in the electricity and gas transmission and distribution activities in the United Kingdom and the United States is consistent with the market and inflation growth forecasts used by the IBERDROLA Group for these markets.

e) Discount rate:

The methodology for calculating the discount rate used by the IBERDROLA Group consists of adding to the temporary value of money or risk-free rate of each market the specific asset risks or risk premium of the asset or business in question.

The risk-free rate corresponds to 10-year Treasury bonds issued in the market in question, with sufficient depth and solvency. In countries with economies or currencies lacking sufficient depth and solvency, a country risk and currency risk is estimated so that the aggregate of all such components are considered to be the finance cost without the risk spread of the asset.

The asset's risk premium corresponds to the specific risks of the asset. For the calculation, the unlevered betas estimated on the basis of comparable companies performing the same principal activity must be taken into account.

The following before-tax discount rates were used in the impairment tests:

Cash-generating unit	2016 rates	2015 rates
Electricity and gas generation and retail in the United Kingdom	6.51%	6.28%
Electricity distribution in Scotland	5.01%	4.91%
Electricity distribution in England and Wales	5.01%	4.91%
Electricity transmission in the UK	5.01%	4.91%
Offshore/onshore renewable energies in the UK	5.91% / 7.11%	5.73% / 6.83%
Renewable energies in the USA	6.43%	6.66%
Gas storage in the USA	6.34%	6.09%
Gas storage in Canada	6.18%	6.05%
Electricity and gas distribution in New York (NYSEG)	5.44%	5.26%
Electricity and gas distribution in New York (RG&E)	5.44%	5.26%
Electricity transmission and distribution in Maine (CMP)	5.44%	5.26%
Electricity transmission and distribution in Connecticut (UI)	5.44%	5.26%
Distribution of gas in Connecticut (CNG)	5.44%	5.26%
Distribution of gas in Connecticut (SCG)	5.44%	5.26%
Distribution of gas in Massachusetts (BGC)	5.44%	5.26%
Electricity distribution in Brazil (ELEKTRO)	13.32%	13.19%

Impairments and write-offs recognised in 2016 and 2015

During 2016 and 2015, the IBERDROLA Group has registered the following valuation adjustments as a consequence of the impairment tests carried out:

- As a consequence of the impairment test carried out in 2016 and 2015 on the renewable facilities in the USA (Note 4.b), the IBERDROLA Group has proceeded to revert part of the provision accounted for in relation their intangible assets from past years. In 2016 and 2015 this write off has amounted to EUR 68,182 thousand and to EUR 49,528 thousand (Note 8), respectively.
- Furthermore in 2015, the IBERDROLA Group made the decision to close Longannet in April 2016, a coal-fired power station located in the United Kingdom, three years before the estimated closure date. In this regard, and because it was not expected that Longannet will produce positive cash flows in the first quarter of 2016, in 2015 the whole plant was written-off, except for the amount expected to be recovered through the sale of scrap and similar items. The write-off amounts to EUR 287,800 thousand (recognition of a provision for impairment amounting to EUR 274,617 thousand and a write-off amounting to EUR 13,183 thousand related to specific spare parts) (Note 10).
- Finally, the IBERDROLA Group had a provision for the restructuring of the workforce associated with the plant closure amounting to EUR 36,249 thousand, with a debit to the "Staff costs" heading in the Consolidated income statement of 2015.

Sensitivity analysis

The IBERDROLA Group has performed several sensitivity analyses of the impairment test results carried out in a systematic way including reasonable changes in a series of basic assumptions defined for each cash-generating unit:

- Electricity and gas generation and retail in the United Kingdom:
 - o A 10% decline in energy output.
 - o A 10% decline in the margin obtained per kWh.
 - o A 10% decline in the increase in electricity and gas customers.
 - o A 10% decline in the margin per kWh of retailing electricity and gas.
 - o A 10% increase in operating and maintenance costs.
 - o A 10% increase in investment cost.
- Regulated activities in United Kingdom, United States and Brazil:
 - o A 10% decline in the rate of return on which the regulated remuneration is based.
 - o A 10% increase in operating and maintenance costs.
 - o A 10% decline in investment (which would lead to a consequent decline in remuneration).
- Renewable energies in the United Kingdom and the United States:
 - o A 5% decline in energy output.
 - o A 10% decline in the total price obtained per kWh, only applicable to production for which no long-term sales agreements have been entered into.
 - o A 10% increase in operating and maintenance costs.
 - o A 10% increase in the investment cost.
- Gas storage in the United States and Canada:
 - o A 15% decline in the gas storage spread (margin per bcm due to the seasonality of prices).
 - o A 10% decrease of the operating capacity.
 - o A 10% increase in operating and maintenance costs.
 - o A 10% increase in the investment cost.

The IBERDROLA Group performed an additional sensitivity analysis of a 100 basis point increase in the discount rate applicable in each case.

These sensitivity analyses carried out separately for each basic assumption did not detect the existence of any impairment, except for the following cases:

- Generation of renewable energy in the United States, whose value in use is EUR 1,025 million greater than its carrying amount, meaning that an increase of 85 basis points in the discount rate, would make the value in use lower than the carrying amount.

- Gas storage in the United States, whose value in use is EUR 64 million greater than its carrying amount, in which a decline in the spread of 6%, a decrease in capacity of 8% or an increase of 51 basis points in the discount rate would mean that the value in use would be lower than its carrying amount.
- Gas storage in the Canada, whose value in use is EUR 24 million greater than its carrying amount, in which a decline in the spread of 9%, a decrease in capacity of 9% or an increase of 85 basis points in the discount rate would mean that the value in use would be lower than its carrying amount.

13. FINANCIAL INVESTMENTS

13.a) Investments accounted for using the equity method

The changes in 2016 and 2015 in the carrying amount of investments of the IBERDROLA Group companies accounted for using the equity method (see Appendix) were as follows:

Thousands of euros	Associated company	Joint ventures			Total
		Neoenergia Subgroup	Flat Rock Subgroup	Other joint ventures	
Balance at 01.01.2015	570,645	1,327,973	148,354	247,625	2,294,597
Investment	3,199	4,414	–	61,835	69,448
Modification of the consolidation perimeter (Note 42)	–	–	–	103,573	103,573
Transfers	–	(46,687)	–	45,384	(1,303)
Profit for the year from continuing operations	33,063	42,075	(2,636)	(21,054)	51,448
Value adjustment (charge)/reversion	–	–	–	3,870	3,870
Other global result	1,134	9,716	–	10,898	21,748
Dividends	(8,580)	(34,291)	(6,034)	(13,989)	(62,894)
Translation differences	(4,347)	(247,549)	15,534	(16,770)	(253,132)
Disposals	–	(135,320)	–	5,956	(129,364)
Classification as an asset held for disposal (Note 39)	–	–	–	(43,675)	(43,675)
Others	678	(3,863)	–	(948)	(4,133)
Balance at 12.31.2015	595,792	916,468	155,218	382,705	2,050,183
Investment	13,077	–	1,366	33,017	47,460
Modification of the consolidation perimeter (Note 42)	–	–	–	20,341	20,341
Transfers	–	–	(9,470)	18,500	9,030
Profit for the year from continuing operations	47,400	30,237	(9,406)	(19,508)	48,723
Other global result	(6,611)	(20,120)	–	(6,267)	(32,998)
Dividends	(11,557)	(28,169)	–	(51,469)	(91,195)
Translation differences	4,770	215,657	7,080	21,246	248,753
Disposals	(104)	–	–	(60,153)	(60,257)
Others	(282)	–	–	(103)	(385)
Balance at 12.31.2016	642,485	1,114,073	144,788	338,309	2,239,655

Commitments to associated companies and joint ventures

Scottish Power Transmission Limited is working with the British operator National Grid in relation to the joint venture NGET/SPT Upgrades, Ltd. in order to build a submarine interconnection in the Irish sea to increase the power transmission capacity between England and Scotland. It is a capital-intensive project where the IBERDROLA Group has an investment commitment of EUR 225 million in 2017. The project is scheduled to be completed in the fourth quarter of 2017.

Impairment of investments accounted for using the equity method

The stock exchange listing of the IBERDROLA Group's holding in GAMESA at 31 December 2016 amounts to EUR 1,059,412 thousand, while the book value is EUR 545,851 thousand. Consequentially, the IBERDROLA Group has not considered necessary to carry out an impairment test in 2016 on its ownership interest in GAMESA.

Main Transactions

The main transactions performed by the IBERDROLA Group in connection with these equity investments accounted for using the equity method were as follows:

2016

- On 14 June 2016, the IBERDROLA Group sold its stake in the Italian companies SER S.p.A. (SER) and SER 1 S.p.A. (SER 1). Following the acquisition on February 2016 of 50.1% of the company SER and 2% of SER 1, the IBERDROLA Group owned 100% of SER and 4% of SER 1, being the remaining 96% of the equity owned by SER.

The total amount of the disinvestment amounted to EUR 193,720 thousand, of which EUR 1 million have been collected, EUR 83,980 thousand were received on 28 November 2016 and EUR 108,740 thousand will be received on 31 May 2017.

This transaction has resulted in a gross capital loss of EUR 8,844 thousand which has been registered Consolidated income statement for the period ended on 31 December 2016.

- On 17 June 2016 IBERDROLA and Iberdrola Participaciones, S.A.U., as shareholders (indirect and direct, respectively) of Gamesa Corporacion Tecnologica, S.A. (GAMESA), on the one hand, and Siemens AG (SIEMENS), on the other hand, have subscribed a contract concerning (i) GAMESA in the context of a merger process of the GAMESA wind power business and SIEMENS; and (ii) their future relationship as shareholders of GAMESA after the merger.

In this regard dated 27 June 2016, GAMESA has announced that the Board of Directors of GAMESA and the sole manager of Siemens Wind HoldCo, S.L. Sociedad Unipersonal (Siemens Wind HoldCo) have approved the common terms of the merger under which Gamesa and the wind power business of SIEMENS will be integrated through the absorption of Siemens Wind HoldCo (as absorbed company) by GAMESA (as absorbing company).

SIEMENS will receive, according to the exchange ratio agreed, GAMESA shares representing approximately 59% of the share capital after the merger is complete, while the current shareholders of GAMESA will hold the remaining 41%, approximately. The share of IBERDROLA after the merger will be 8% and will be represented in the Board.

Also, as part of the merger, SIEMENS will make a cash contribution so that GAMESA distributes EUR 3.75 per share to its shareholders (other than SIEMENS) once the merger is completed (amount will be reduced by the amount of Gamesa ordinary dividends distributed until the merger is complete). Taking into account the dividend already distributed by GAMESA in 2016 amounting to EUR 0.1524 per share and the IBERDROLA Group's share in GAMESA, EUR 3.5976 per share which is equivalent to EUR 198 million corresponds to them.

On 25 October 2016 GAMESA's Extraordinary General Shareholders' Meeting approved the operation, and on 7 December 2016 the Spanish National Securities Market Commission (hereinafter, *CNMV*) agreed that SIEMENS should be exempted from drawing up the takeover bid stipulated in Article 8.g) of Royal Decree 1066/2007.

Completion of the merger is subject to approval by the competition authorities. The process is expected to be completed in the first quarter of 2017.

2015

As described in Note 39, Iberdrola Energía, S.A.U transferred to NEOENERGIA all of its direct holding it had in Companhia de Eletricidade do Estado da bahía, S.A. (COELBA) and Companhia de Eletricidade do Rio Grande do Norte, S.A. (COSERN).

Summary of Financial Information

The summarised financial information as of 31 December 2016 (at 100% and before intercompany eliminations) for the major subgroups/companies accounted for using the equity method is as follows:

	Neoenergia subgroup		Flat Rock subgroup	
Thousands of euros	12.31.16	12.31.15	12.31.16	12.31.15
Segment	Networks-Brazil		Renewables-United States	
Current assets	1,597,685	1,608,125	2,961	4,976
Non-current assets	6,952,143	5,364,914	316,958	323,264
Total assets	8,549,828	6,973,039	319,919	328,240
Current liabilities	2,410,958	1,822,602	590	1,065
Non-current liabilities	3,062,941	2,609,247	13,581	20,678
Total liabilities	5,473,899	4,431,849	14,171	21,743
Income from ordinary activity	3,815,832	4,160,241	14,201	31,816
Depreciation and amortization	(300,786)	(303,804)	(21,048)	(19,829)
Interest income	214,438	178,482	18	7
Interest expenses	(538,630)	(409,646)	(346)	(763)
Tax (expense)/income	(41,292)	(50,865)	–	–
Profit for the year from continuing operations	92,057	119,666	(19,870)	5,092
Other global profit	(69,300)	24,915	–	–
Total global profit	22,757	144,581	(19,870)	5,092
Other information				
Cash and cash equivalents	412,444	566,312	1,474	2,647
Current financial liabilities (*)	1,463,175	1,071,616	–	–
Non-current financial liabilities (*)	2,698,621	2,331,281	–	–

(*) Excluding trade and other payables

13.b) Non-current equity instruments

All the financial assets included under this heading in the Consolidated statement of financial position at 31 December 2016 and 2015 were classified as available-for-sale assets.

On 30 June 2015, the IBERDROLA Group disposed of its holding in Euskaltel, S.A. for EUR 24,042 thousand, which led to a gross capital gain of EUR 15,578 thousand recognised under the “Finance income” heading on the Consolidated income statement for 2015 (Note 40).

13.c) Other financial assets

The breakdown of the “Other non-current financial assets” and the “Other current financial assets” headings in the IBERDROLA Group’s Consolidated statement of financial position at 31 December 2016 and 2015 is as follows:

Thousands of euros	12.31.16	12.31.15	Interest rate	Maturity
Non-current				
Collection rights in Brazil (Notes 4.b and 11)	315,073	215,180	Indexed to inflation	From 2027 on
Long-term deposits and guarantees	133,522	110,419	-	Not set
Fixed-income securities				
Related to equity instruments having the substance of a financial liability	–	1,316	-	-
Others	16,461	16,324	Various	From 2018 on
Concessional guarantee of the sufficiency tariff in Brazil (Note 11)	48,672	76,634	13.75%	2018
Long-term deposits	32,375	32,455	Various	From 2018 on
Credits to third parties	48,567	57,707	Indexed to EURIBOR	From 2018 on
Other investments in companies accounted for using the equity method	5,272	84,568	Indexed to EURIBOR	From 2018 on
Others	117,144	35,553		From 2018 on
Bad debt provisions	(21,418)	(21,444)		From 2018 on
Total	695,668	608,712		
Current				
Short-term cash deposits	3,929	17,596	Indexed to EONIA	Less than a year
Fixed-income securities				
Related to equity instruments having the substance of a financial liability	3,018	10,601	7.00%	Less than a year
Others	1,593	1,513	6.00%	Less than a year
Concessional guarantee of the sufficiency tariff in Brazil (Note 11)	66,524	148,292	13.75%	Less than a year
Account receivable for financing imbalance in revenues shortfall in 2016 (Note 4.w)	240,917	–	–	Less than a year
Accounts receivable for financing imbalance in revenues shortfall in 2015 (Note 4.w)	–	150,473	–	–
Other investments in companies accounted for using the equity method	54,843	21,865	Various	Less than a year
Short-term deposits and guarantees	202,420	138,050	–	Less than a year
Others	210,679	194,795	–	Less than a year
Bad debt provisions	(7,582)	(175)	–	Less than a year
Total	776,341	683,010		

Collection rights in Brazil

The "Collection rights in Brazil" heading relates to the indemnification receivable by the Brazilian companies upon expiry of their service concession arrangements (Note 4.b). The Law N°12.783/13 provides that such indemnification must be determined by the replacement value (*Valor Novo de Reposição VNR*) of the concession assets which have not been depreciated/amortised by the end of the concession period.

The fair value of the financial asset receivable from the concession grantor at the end of the concession is determined using the residual value of the Regulatory Asset Base (*Base de Remuneração Regulatória, BRR*) at the end of the contractual term of the concession.

The method specified by the regulator protects the value of the Regulatory Asset Base after each ordinary tariff review. Ordinary reviews are conducted every four years. This means that after the regulator has conducted a tariff review the value of the Regulatory Asset Base prior to that date cannot be changed except to the extent that it might be updated in accordance with Brazilian Market Prices General Index (*Índice General de Precios de Mercado Brasileño - IGPM*). The next tariff review will determine the value of the regulatory asset base only with regard to additions in the interval between two tariff reviews.

To estimate the amount of the financial asset, observable values are used. Specifically, the net replacement value, as calculated by the energy regulator in the course of the latest tariff review. The amount is updated in the intervals between tariff reviews by additions to the underlying fixed assets and currency translation differences or, as the case may be, any changes in the method of calculation of the net realizable value and the IGPM.

Long term deposits and guarantees

The "Long term deposits and guarantees" heading essentially corresponds to the portion of guarantees and deposits received from customers at the time of recruitment as security of electricity supply (which are recorded in "Non-Current Liabilities - Other non-current payables" in the Consolidated statement of financial position - Note 27) and have been deposited with the competent Public Authorities in accordance with the current legislation in Spain.

14. NON-CURRENT TRADE AND OTHER RECEIVABLES

The breakdown of the "Non-current trade and other receivables" heading in the Consolidated statements of financial position at 31 December 2016 and 2015, is as follows:

Thousands of euros	12.31.16	12.31.15	Interest rate	Maturity
Receivables from Brazilian customers	27,317	12,892	–	From 2018 on
CFE (Note 4.u)	303,877	355,461	4.75%	2018-2032
Account receivable for the sale to Neoenergia of COELBA and COSERN (Notes 13.a and 39)	231,800	167,016	12.19%	2018
Others	327,921	80,903	–	
Bad debt provisions	(3,832)	(1,011)	–	
Total	887,083	615,261		

These balances relate to accounts receivable arising in the normal course of business of the IBERDROLA Group and, therefore, are recognised at amortised cost. This broadly coincides with market value.

15. MEASUREMENT OF FINANCIAL INSTRUMENTS

The comparison between carrying amount and fair value of the IBERDROLA Group's financial instruments at 31 December 2016 and 2015 is as follows:

Thousands of euros	12.31.2016		12.31.2015	
	Carrying amount	Fair value	Carrying amount	Fair value
Financial assets				
Equity instruments	64,073	64,073	96,202	96,202
Other financial assets	1,472,009	1,472,009	1,291,722	1,291,722
Derivative financial instruments	1,603,047	1,603,047	1,560,522	1,560,522
Current trade and other receivables	6,102,793	6,102,793	5,985,117	5,985,117
Financial liabilities				
Equity instruments with financial liability characteristics	137,054	144,000	216,430	247,470
Bank borrowings and other financial liabilities	31,220,682	33,442,203	29,444,475	32,177,277
Derivative financial instruments	1,110,319	1,110,319	1,116,554	1,116,554
Other non-current payables	737,269	737,269	689,694	689,694
Trade payables	5,490,634	5,490,634	5,577,148	5,577,148
Other current liabilities	1,791,776	1,791,776	1,754,306	1,754,306

The fair value of these financial instruments has been calculated as set out in Note 4.I.

The sensitivity of the fair value of the IBERDROLA Group's borrowings, after the effect of hedge accounting, to changes in the euro-dollar and euro-sterling pound exchange rates is as follows:

Thousands of euros	2016		2015	
	Depreciation 5%	Appreciation 5%	Depreciation 5%	Appreciation 5%
Dollar/euro exchange rate variation				
Debt's value variation	(261,883)	289,449	(249,887)	276,191

Thousands of euros	2016		2015	
	Depreciation 5%	Appreciation 5%	Depreciation 5%	Appreciation 5%
Sterling pound/euro exchange rate variation				
Debt's value variation	(145,134)	160,412	(167,330)	184,944

The estimated fair value of borrowings bearing fixed interest rates, after the effect of hedge accounting at 31 December 2016 and 2015, calculated by discounting future cash flows at market interest rates, amounted to EUR 16,557,885 thousand and EUR 15,072,306 thousand, respectively. The interest rate curve used to make this calculation takes into account the risks associated with the electricity industry and the credit rating of the IBERDROLA Group. The sensitivity of that fair value to interest rate fluctuations is as follows:

Thousands of euros	12.31.2016		12.31.2015	
Interest rate variation	+0.25%	+(0.25)%	+0.25%	+(0.25)%
Debt's value variation	(230,585)	237,119	(220,294)	226,898

The IBERDROLA Group measures certain available-for-sale assets and derivative financial instruments at fair value, provided they can be measured reliably, classifying them into three levels:

- Level 1: assets and liabilities quoted in liquid markets.
- Level 2: assets and liabilities whose fair value is determined using valuation techniques with observable market data.
- Level 3: assets and liabilities whose fair value is determined using valuation techniques without observable market data.

The breakdown of financial instruments measured at fair value by levels is as follows:

Thousands of euros	Value at 12.31.2016	Level 1	Level 2	Level 3
Other financial investments – Brazil receivables (Note 13.c)	315,073	–	315,073	–
Derivative financial instruments (financial assets) (Note 26)	1,603,047	30,402	1,415,860	156,785
Derivative financial instruments (financial liabilities) (Note 26)	(1,110,319)	(65,508)	(918,560)	(126,251)

Thousands of euros	Value at 12.31.2015	Level 1	Level 2	Level 3
Equity instruments (Note 13.b)	25,897	25,897	–	–
Other financial investments – Brazil receivables (Note 13.c)	215,180	–	215,180	–
Derivative financial instruments (financial assets) (Note 26)	1,560,522	95,671	1,349,664	115,187
Derivative financial instruments (financial liabilities) (Note 26)	(1,116,554)	(25,686)	(952,354)	(138,514)

At 31 December 2016 and 2015 equity instruments of not listed companies classified as available for sale, measured at acquisition cost, whose fair value cannot be measured reliably, amounts to EUR 64,073 thousand and EUR 70,305 thousand, respectively.

The reconciliation between initial and final balances for financial instruments classified as Level 3 of the fair-value hierarchy is as follows:

Thousands of euros	Derivative financial instruments
Balance at 01.01.2015	37,266
Income and expense recognised in Consolidated income statement	21,821
Income and expense recognised in the Consolidated statement of comprehensive income	(532)
Purchases	(4,557)
Sales and settlements	(7,409)
Translation differences	3,336
Transfer outside Level 3	(12,426)
Modification of the consolidation perimeter (Note 42)	(60,826)
Balance at 12.31.2015	(23,327)
Income and expense recognised in Consolidated income statement	60,183
Income and expense recognised in the Consolidated statement of comprehensive income	(725)
Purchases	2,198
Sales and settlements	(6,271)
Translation differences	1,751
Transfer outside Level 3	(3,275)
Balance at 12.31.2016	30,534

The fair value of Level 3-classified financial instruments has been determined by the discounted cash flow method. Projections of these cash flows are based on assumptions not observable in the market, and mainly correspond to purchase and sale price estimates that the Group normally uses, based on its experience in the markets.

None of the possible foreseeable scenarios of the indicated assumptions would result in a material change in the fair value of the financial instruments classified at this level.

In addition, the IBERDROLA Group's financial assets and liabilities are compensated and presented net on the Consolidated statement of financial position when a legally enforceable right exists to offset the amounts recognised and the Group intends to settle the assets and liabilities net or simultaneously. The breakdown of netted financial assets and liabilities at 31 December 2016 and 2015 is as follows:

12.31.2016						
Thousands of euros	Gross amount	Compensated amount	Net amount	Uncompensated amounts under compensation agreements		Net amount
				Financial instrument	Financial guarantee	
ASSET DERIVATIVES:						
Current						
- Commodities	1,052,447	(790,604)	261,843	(125,678)	(21,509)	114,656
- Others	51,185	(10,974)	40,211	–	–	40,211
Non-current						
- Commodities	166,693	(21,809)	144,884	(7,872)	(44,528)	92,484
- Others	69,267	(277)	68,990	–	(59,029)	9,961
Total	1,339,592	(823,664)	515,928	(133,550)	(125,066)	257,312
OTHER FINANCIAL ASSETS:						
- Receivables	569,327	(461,166)	108,161	(38,033)	(17,543)	52,585
LIABILITY DERIVATIVES:						
Current						
- Commodities	1,059,667	(790,604)	269,063	(125,678)	(47,213)	96,172
- Others	17,634	(10,974)	6,660	–	(235)	6,425
Non-current						
- Commodities	56,759	(21,809)	34,950	(7,872)	(2,983)	24,095
- Others	589	(277)	312	–	–	312
Total	1,134,649	(823,664)	310,985	(133,550)	(50,431)	127,004
OTHER FINANCIAL LIABILITIES:						
- Payables	740,552	(461,166)	279,386	(38,033)	(11,810)	229,543
12.31.2015						
Thousands of euros	Gross amount	Compensated amount	Net amount	Uncompensated amounts under compensation agreements		Net amount
				Financial instrument	Financial guarantee	
ASSET DERIVATIVES:						
Current						
- Commodities	623,770	(342,414)	281,356	(72,011)	(28,870)	180,475
- Others	40,644	(23,179)	17,465	–	–	17,465
Non-current						
- Commodities	133,673	(36,955)	96,718	(6,099)	(33,146)	57,473
- Others	47,555	(826)	46,729	–	(39,484)	7,245
Total	845,642	(403,374)	442,268	(78,110)	(101,500)	262,658
OTHER FINANCIAL ASSETS:						
- Receivables	287,533	(217,881)	69,652	(15,491)	–	54,161
- Collateral	33,639	(33,639)	–	–	–	–
LIABILITY DERIVATIVES:						
Current						
- Commodities	573,409	(376,161)	197,248	(71,802)	(3,935)	121,511
- Commodities	26,780	(23,178)	3,602	–	–	3,602
- Others	–	–	–	–	–	–
Non-current						
- Commodities	74,341	(36,848)	37,493	(6,308)	(117)	31,068
- Others	1,377	(826)	551	–	–	551
Total	675,907	(437,013)	238,894	(78,110)	(4,052)	156,732
OTHER FINANCIAL LIABILITIES:						
- Payables	358,042	(217,881)	140,161	(15,491)	–	124,670

16. NUCLEAR FUEL

The breakdown of the “Nuclear Fuel” heading in the Consolidated statement of financial position at 31 December 2016 and 2015, and of the changes therein in 2016 and 2015 is as follows:

Thousands of euros	Fuel loaded into the reactor core	Nuclear fuel in progress	Total
Balance at 01.01.2015	220,539	99,433	319,972
Additions	–	155,737	155,737
Capitalised financing expenses (Notes 4.g and 40)	–	4,204	4,204
Transfers	181,011	(181,011)	–
Fuel consumed (Note 4.g)	(130,031)	–	(130,031)
Balance at 12.31.2015	271,519	78,363	349,882
Additions	–	104,214	104,214
Capitalised financing expenses (Notes 4.g and 40)	–	2,465	2,465
Transfers	112,860	(112,860)	–
Fuel consumed (Note 4.g)	(133,931)	–	(133,931)
Balance at 12.31.2016	250,448	72,182	322,630

The IBERDROLA Group's nuclear fuel purchase commitments at 31 December 2016 and 2015 amount to EUR 628,794 thousand and EUR 609,225 thousand, respectively.

17. INVENTORIES

The breakdown of the “Inventories” heading (Note 4.h) in the Consolidated statements of financial position at 31 December 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Energy sources	344,213	505,380
Emission allowances	61,977	128,750
Real Estate developments	1,278,139	1,271,722
Other inventories	74,378	13,174
Impairment provision	(125,205)	(121,827)
Total	1,633,502	1,797,199

The variations in the impairment provision in 2016 and 2015 are as follows:

Thousands of euros	2016	2015
Initial balance	121,827	101,507
Charges to the year	21,703	9,256
Reversals	(12,120)	(5,078)
Transfers	–	19,834
Translation differences	(868)	372
Applications and others	(5,337)	(4,064)
Final Balance	125,205	121,827

At 31 December 2016, the IBERDROLA Group has in place “take or pay” contracts with several natural and liquefied natural gas suppliers for the supply of 31 bcm of gas during the period from 2017 to 2039, earmarked for retailing and for consumption at the Group's electricity production facilities. The prices under these contracts are determined on the basis of formulas commonly used in the market, which index the price of gas to the performance of other energy variables. Moreover, the IBERDROLA Group has purchase commitments of 9 bcm of natural gas in the National Balancing Point (NBP).

18. OTHER CURRENT TRADE AND OTHER RECEIVABLES

The breakdown of this heading in the Consolidated statements of financial position at 31 December 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Trade receivables	4,793,479	4,976,654
Other receivables ⁽¹⁾	814,044	703,800
Companies accounted for using the equity method	21,140	80,384
Bad debt provision	(412,953)	(390,982)
Total	5,215,710	5,369,856

- (1) The heading “Other receivables” includes the best estimate that IBERDROLA expects to recover due to the favourable judgements from the Supreme court on the non inclusion of the territorial supplement, after the modification introduced by the Royal Decree-law 20/2012 in the tolls’ orders (Order IET/221/2013 and the Order IET/1491/2013) for the period 2013. It amounts to EUR 131.1 million and it has been charged EUR 119.5 million under the heading “Other operating expense – Taxes” and EUR 11.6 million under the heading “Finance income” of the Consolidated income statement for the year 2016.

Generally, the amounts included under this heading in the Consolidated statement of financial position do not bear any interest.

The variation in the bad debt provision during 2016 and 2015 is as follows:

Thousands of euros	2016	2015
Initial balance	390,982	374,858
Charges for the year	190,157	189,515
Applications	(139,666)	(177,955)
Translation differences	(9,689)	7,870
Long-term transfers	(10,656)	–
Excess	(8,175)	(3,306)
Final Balance	412,953	390,982

The bad debt provision relates basically entirely to gas and electricity consumers.

The breakdown of trade receivables and other current and non-current receivables with regard to their credit-risk status is as follows:

Thousands of euros	12.31.2016	12.31.2015
Provisioned trade receivables and other non-current receivables	3,832	1,011
Provisioned trade receivables and other current receivables	412,953	390,982
Non-provisioned financial assets in default	804,566	740,307
Financial assets not in default and not provisioned	5,298,227	5,244,810
Provisions	(416,785)	(391,993)
Total	6,102,793	5,985,117

The breakdown of the age of financial assets in default for which no provision was considered necessary as at 31 December 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Up to 90 days	421,462	421,561
Between 90 and 180 days	201,800	224,692
More than 180 days	181,304	94,054
Total	804,566	740,307

19. CASH AND CASH EQUIVALENTS

The detail of this heading in the Consolidated statements of financial position at 31 December 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Cash	181,692	248,848
Short-term deposits	1,250,994	904,425
Total	1,432,686	1,153,273

Short-term deposits mature within a period of less than three months and bear market interest rates. There are no restrictions on cash withdrawals for significant amounts.

20. EQUITY

Share capital

Changes in 2016 and 2015 in the different items of share capital of IBERDROLA are as follows:

	Date	% Share Capital	Numbers of shares	Nominal	Euros
Balance at 01.01.2015		–	6,388,483,000	0.75	4,791,362,250
Capital reduction	28 April 2015	2.324	(148,483,000)	0.75	(111,362,250)
Paid-up capital increase	20 July 2015	1.552	96,870,000	0.75	72,652,500
Balance at 12.31.2015		–	6,336,870,000	0.75	4,752,652,500
Paid-up capital increase	26 January 2016	0.952	60,327,000	0.75	45,245,250
Capital reduction	26 April 2016	2.457	(157,197,000)	0.75	(117,897,750)
Paid-up capital increase	22 July 2016	1.956	122,079,000	0.75	91,559,250
Balance at 12.31.2016			6,362,079,000	0.75	4,771,559,250

The paid-up capital increases taken place in 2016 and 2015 correspond to the different execution approved by the General Shareholders' Meeting through which the Iberdrola Flexible Dividend system is implemented.

Information on the holders of free of charges allocation rights who accepted the irrevocable rights purchase commitment assumed by IBERDROLA is as follows:

	Free of charges allocation rights		Rights waived
	Number	Thousands of euros	Number
Paid-up capital increase			
20 July 2015	1,009,019,969	115,028	1
26 January 2016	3,320,519,969	421,706	31
22 July 2016	746,444,927	92,559	43

Additionally, on 28 April 2015 and 26 April 2016, capital decreases were performed by redeeming treasury shares already held, as approved at the General Shareholders Meeting of 27 March 2015 and 8 April 2016, respectively.

There were no changes to IBERDROLA's share capital other than those resulting from the transactions described above. There are no claims on IBERDROLA's share capital other than those provided for in the Spanish Companies Law.

IBERDROLA's shares are listed for trading on the Spanish electronic trading system ("*Mercado Continuo Español*"), forming part of the IBEX-35 and the European Eurostoxx-50 indexes.

Major shareholders

Since IBERDROLA's shares are represented by the book-entry system, the exact stakes held by its shareholders are not known. The table below summarises major direct and indirect shareholdings in the share capital of IBERDROLA at 31 December 2016 and 2015, as well as the holdings of financial instruments disclosed by the owners of these stakes in compliance with the Royal Decree 1362/2007 of 19 October. This information is based on filings by the owners of the stakes in the official registers of the CNMV or the company's financial statements or press releases, and it is presented in the 2016 IBERDROLA Group's Annual Corporate Governance Report.

IBERDROLA treats as a significant shareholder any shareholder who exerts a significant influence on the company's financial and operating decisions when (i) they have presence in the Board of Directors or equivalent and (ii) whose ownership interest in the company enables them to exercise the proportional representation system. Therefore, the company treats Qatar Investment Authority as significant shareholder, these being the only shareholders who satisfied that condition at the date of issue of these Consolidated financial statements.

Owner	% of voting rights 2016			% Total 2015	Financial instruments 2016	Executive Directors of IBERDROLA 2016
	Direct	Indirect	Total			
Qatar Investment Authority (1)	–	8.509	8.509	9.726	–	–

(1) Parent company of Qatar Holding Luxembourg II, S.A.R.L. and DGIC Luxembourg, S.A.R.L., direct owners of the holding

In addition, other companies have direct and indirect voting rights in excess of 3% of the share capital.

Owner	% of voting rights 2016		
	Direct	Indirect	Total
Norges Bank	3.196	–	3.196
Blackrock, Inc	–	3.011	3.011
Kutxabank, S.A.	–	3.003	3.003

Financial management

The IBERDROLA Group's main financial management objectives are to ensure short and long-term financial stability, robust financial liquidity ratios, the optimization of the liquidity position, the management of financial risks, and at the same time maintaining a sustainable remuneration policy for its shareholders.

At this time, the credit ratings granted by Moody's, Standard & Poor's and Fitch are Baa1, BBB+ and BBB+, respectively.

Leverage ratios at 31 December 2016 and 2015 stand at:

Thousands of euros	12.31.2016	12.31.2015
Bank borrowings and other financial liabilities - Loans and others (Note 25)	31,220,682	29,444,475
Equity instruments having the substance of a financial liability (Note 21)	137,054	216,430
Derivative financial liabilities	668,010	679,133
Gross debt	32,025,746	30,340,038
Derivative financial assets	1,119,077	1,107,716
Other current financial assets	59,933	11,917
Cash and cash equivalents (Note 19)	1,432,686	1,153,273
Cash assets	2,611,696	2,272,906
Net debt	29,414,050	28,067,132
Equity		
Of the parent company	36,690,965	37,158,658
Of non-controlling interests	3,445,898	3,246,287
Of subordinated perpetual obligations	550,526	551,108
	40,687,389	40,956,053
Leverage	41.96%	40.66%

Derivative financial instruments detailed in the table above only include the ones relating to financing operations which breakdown is as follows (Note 26):

2016						
Thousands of euros	Derivative assets			Derivative liabilities		
	Current	Non current	Total	Current	Non current	Total
Interest rate hedges	31,449	181,928	213,377	40,545	(125,931)	(85,386)
Foreign exchange hedges	318,110	554,748	872,858	(383,536)	(174,555)	(558,091)
Total hedging derivatives	349,559	736,676	1,086,235	(342,991)	(300,486)	(643,477)
Foreign exchange derivatives	22,429	188	22,617	(7,893)	(183)	(8,076)
Interest rate derivatives	–	3,112	3,112	(2,253)	(7,091)	(9,344)
Treasury shares derivatives	–	7,113	7,113	–	(7,113)	(7,113)
Total non-hedging derivatives	22,429	10,413	32,842	(10,146)	(14,387)	(24,533)
Total	371,988	747,089	1,119,077	(353,137)	(314,873)	(668,010)

2015						
Thousands of euros	Derivative assets			Derivative liabilities		
	Current	Non current	Total	Current	Non current	Total
Interest rate hedges	26,966	202,063	229,029	21,998	(91,683)	(69,685)
Foreign exchange hedges	212,670	624,814	837,484	(469,075)	(101,266)	(570,341)
Total hedging derivatives	239,636	826,877	1,066,513	(447,077)	(192,949)	(640,026)
Foreign exchange derivatives	21,700	1,391	23,091	(10,422)	(394)	(10,816)
Interest rate derivatives	–	3,258	3,258	(3,741)	(9,696)	(13,437)
Treasury shares derivatives	–	14,854	14,854	–	(14,854)	(14,854)
Total non-hedging derivatives	21,700	19,503	41,203	(14,163)	(24,944)	(39,107)
Total	261,336	846,380	1,107,716	(461,240)	(217,893)	(679,133)

Powers delegated at the General Shareholders' Meeting

The General Shareholders' Meeting on 8 April 2016 resolved, in respect of items seven and eight on the agenda, to delegate powers to the Board of Directors, with express powers of substitution, for a period of five years, to:

- increase share capital in the terms and to the limits stipulated in Article 297.1 b) of the Spanish Companies Law ("Ley de Sociedades de Capital"), with authorisation to exclude preferential subscription rights, and
- issue bonds or debentures swappable for and/or convertible into shares in the Company or other companies, and warrants on new or existing shares in the Company or other companies, to a maximum amount of EUR 5,000 million. This authorisation includes the delegation of powers to, where applicable: (i) determine the basis and procedures for conversion, swap or exercise; (ii) increase share capital by the amount required to cover applications for conversion; and (iii) exclude shareholders' preferential subscription rights on the issue.

Both authorisations have a joint limit to a maximum nominal amount of 20% of the share capital.

Legal reserve

Under the Restated Text of the Spanish Companies Law, 10% of net profit for each year must be transferred to the legal reserve until the balance of this reserve reaches at least 20% of the share capital.

The legal reserve can be used to increase capital provided that the remaining reserve balance does not fall below 10% of the increased share capital amount. Otherwise, until the legal reserve exceeds 20% of share capital, it can only be used to offset losses, provided that sufficient other reserves are not available for this purpose.

Revaluation reserves

The balance of "Revaluation reserves" arose as a result of the revaluation of property, plant and equipment made by IBERDROLA pursuant to the Royal Decree-law 7/1996. This balance can be used, free of tax, to offset recorded losses both prior years' accumulated losses and current year losses or losses which might arise in the future, and to increase share capital. From 1 January 2007, the balance of this reserve can be taken to unrestricted reserves, provided that the monetary surplus has been realised. The surplus will be deemed to have been realised on the portion on which depreciation has been taken for accounting purposes or if the revalued assets have been transferred or derecognised. If the balance of this account was used in any way other than as specified in the Royal Decree-law 7/1996, it would be subject to tax.

Share premium

The Restated Text of the Spanish Companies Law expressly permits the use of the share premium account balance to increase capital and does not establish any specific restrictions as to its use.

Other restricted reserves

The "Equity" heading of the Consolidated statement of financial position primarily includes the restricted reserve set up by IBERDROLA in accordance with article 335.c) of the Restated Text of the Spanish Companies Law arising from the capital reductions carried out in prior years through the retirement of treasury shares. The restricted reserves relating to Group companies other than the parent IBERDROLA are included under "Retained earnings" of the same heading.

Non-controlling interests

The "Equity – Of non-controlling interests" heading of the Consolidated statement of financial position for an amount of EUR 3,445,898 thousand collects, mainly, 18.5% of minority of the AVANGRID Group posed EUR 3,227,110 thousand.

Subordinated perpetual obligations

On 27 February 2013, the IBERDROLA Group's perpetual subordinated bonds issue was completed and disbursed, in the amount of EUR 525 million. The issue price was set at 99.472% of the face value, with a fixed annual coupon of 5.75% as from the issue date to 27 February 2018. From the first repricing date on, the coupon will be equal to the applicable five-year swap rate plus a 4.81% annual spread during the following five years, a 5.06% annual spread during each of the five-year repricing periods beginning on 27 February 2023, 2028 and 2033, and a 5.81% annual spread during the following five-year repricing periods.

The interest accruing on these bonds will not be callable but rather cumulative. However, the IBERDROLA Group will be obligated to settle the interest accrued in the event it distributes dividends. Although these bonds do not have a contractual maturity date, the IBERDROLA Group has the option of redeeming them on 27 February 2018, and from that date on, every five years.

After analysing the issue conditions, the IBERDROLA Group recognised the cash received with a credit to "Subordinated perpetual obligations" of the equity on the Consolidated statement of financial position, as it considers that it does not meet the criteria for classification as a financial liability, given that the IBERDROLA Group does not have a commitment to deliver cash, as the circumstances that would require it to do so – namely distribution of dividends and exercise of its right to redeem the bonds – are fully under its control. As a result, accrued interests from the obligations issue have been registered amounting to EUR 22,948 and EUR 21,455 thousand, under the heading "Subordinated perpetual obligations owners" of the Consolidated income statement at 31 December 2016 and 2015, respectively.

In unrealised asset and liability revaluation reserves

The change in this reserve arising from valuation adjustments to available-for-sale assets and derivatives designated as cash flow hedges at 31 December 2016 and 2015 is as follows:

Thousands of euros	01.01.2015	Change in fair value and others	Allocation to the values of hedged assets	Amounts charged to income	12.31.2015	Change in fair value and others	Allocation to the values of hedged assets	Amounts charged to income	12.31.2016
In 98 recognized asset and liability revaluation reserves of companies accounted for using the equity method (net of tax):	2,758	16,596	–	150	19,504	(16,559)	–	14	2,959
Available-for-sale assets:									
Others	22	(11)	–	40	51	(13)	–	–	38
	22	(11)	–	40	51	(13)	–	–	38
Cash flow hedges:									
Interest rate swaps	(455,005)	39,035	–	37,925	(378,045)	(225,436)	–	141,870	(461,611)
Collars	(4,448)	(147)	–	468	(4,127)	(716)	–	593	(4,250)
Derivatives on commodities	32,833	(86,011)	–	86,716	33,538	12,221	–	71,847	117,606
Currency forwards	(19,905)	28,280	6,717	7,527	22,619	123,824	(7,884)	(5,009)	133,550
	(446,525)	(18,843)	6,717	132,636	(326,015)	(90,107)	(7,884)	209,301	(214,705)
Tax effect on available-for-sale assets and cash flow hedges	116,742	11,260	(1,352)	(42,241)	84,409	23,983	1,512	(47,590)	62,314
Total	(327,003)	9,002	5,365	90,585	(222,051)	(82,696)	(6,372)	161,725	(149,394)

Treasury shares

The IBERDROLA Group buys and sells treasury shares in accordance with the prevailing law and the resolutions of the General Shareholders' Meeting. Such transactions include purchases and sales of company shares and of derivative instruments having company shares as the underlying asset.

At 31 December 2016 and 2015 the balances of the different instruments are as follows:

	12.31.2016		12.31.2015	
	Number of shares	Thousands of euros	Number of shares	Thousands of euros
Treasury shares of IBERDROLA	151,224,777	868,936	67,636,166	405,458
Treasury shares of SCOTTISH POWER	1,374,405	9,580	1,638,563	10,163
Swaps over treasury shares	1,867,929	11,899	7,800,721	48,979
Futures over treasury shares ⁽¹⁾	–	–	14,000,000	83,962
Accumulators (exercised shares)	1,624,221	9,283	3,027,195	17,799
Accumulators (potential shares)	31,870,828	183,669	12,111,494	72,878
Total	187,962,160	1,083,367	106,214,139	639,239

(2022) Over the Counter (OTC) Futures or of unorganized markets

(a) Treasury Shares

At 31 December 2016 and 2015, IBERDROLA owned 151,224,777 and 67,636,166 shares and SCOTTISH POWER owned 1,374,405 and 1,638,563 shares, respectively.

The changes in 2016 and 2015 in the treasury shares of IBERDROLA (Note 4.m) are as follows:

	Number of shares	Thousands of euros
Balance at 01.01.2015	60,985,277	334,014
Acquisitions	162,118,086	938,283
Capital reduction	(148,483,000)	(827,884)
Disposals	(6,984,197)	(38,956)
Balance at 12.31.2015	67,636,166	405,457
Acquisitions	247,226,143	1,450,724
Capital reduction	(157,197,000)	(946,566)
Disposals	(6,440,532)	(40,679)
Balance at 12.31.2016	151,224,777	868,936

The changes in 2016 and 2015 in the treasury shares of SCOTTISH POWER (Note 4.m) are as follows:

	Number of shares	Thousands of euros
Balance at 01.01.2015	1,996,422	11,705
Acquisitions	438,580	2,759
Iberdrola flexible dividend	66,375	–
Disposals (given to employees)	(862,814)	(4,301)
Balance at 12.31.2015	1,638,563	10,163
Acquisitions	404,154	2,464
Iberdrola flexible dividend	56,040	–
Disposals (given to employees)	(724,352)	(3,047)
Balance at 12.31.2016	1,374,405	9,580

These shares correspond to the matching shares held by the trust in the share plan called Share Incentive Plan.

During 2016 and 2015, treasury shares held by the IBERDROLA Group were below the legal limit.

(b) Derivatives settled by physical delivery

The IBERDROLA Group recognises the transaction directly in equity under the “Treasury shares” heading and records the obligation to buy back the shares under “Bank borrowings and other financial liabilities – loans and others” heading of the liabilities side of the Consolidated statement of financial position.

– Total return swaps

The IBERDROLA Group has arranged a swap on treasury shares with the following features: during the life of the contract it will pay the financial entity 3-month Euribor plus a spread on the notional and will receive the dividends corresponding to the shares paid out to the financial entity. On the expiration date IBERDROLA will buy the shares at the strike price set out in the contract.

The characteristics of these contracts at 31 December 2016 and 2015 are as follows:

	Number of shares 12.31.2016	Strike price	Maturity date	Interest Rate	2016 Thousands of euros
<i>Total Return Swap</i>	1,867,929	6.370	04/18/2017	3-months Euribor + 0.55%	11,899
Total	1,867,929				11,899

	Number of shares 12.31.2015	Strike price	Maturity date	Interest Rate	2015 Thousands of euros
Total return swap	2,202,792	6.047	01/18/2016	3-months Euribor + 0.55%	13,320
Total return swap	1,867,929	6.370	04/18/2016	3-months Euribor + 0.50%	11,899
Total return swap	1,865,000	6.370	04/18/2016	3-months Euribor + 0.50%	11,880
Total return swap	1,865,000	6.370	04/18/2016	3-months Euribor + 0.50%	11,880
Total	7,800,721				48,979

– Futures (OTC – Over the Counter)

Under these contracts the purchase and sale of a given number of shares is agreed at a specified future date and price.

At 31 December 2016, there are no Future contracts. The characteristics of these contracts at 31 December 2015 are shown in the following table:

2015	Number of shares	Average price of the period	Maturity date	Thousands of euros
Futures	14,000,000	5.9973	01/13/2016 – 02/03/2016	83,962

– Treasury share accumulators

The IBERDROLA Group holds several purchase accumulators on treasury shares.

These accumulators are obligations to buy shares in the future, with a notional amount of zero on the start date. The number of shares to be accumulated depends on the market price quoted on a range of observation dates throughout the life of the options – in this case, on a daily basis. A strike price is set, and a knockout level above which the structured product is “knocked out” and shares are no longer accumulated.

The accumulation mechanism is as follows:

- when the spot price is below the strike price, two units of the underlying security are accumulated;
- when the spot price is between the strike price and the knockout level, only one unit of the underlying security is accumulated; and
- when the spot price is above the knockout level, no shares are accumulated.

The characteristics of these contracts at 31 December 2016 and 2015 are as follows:

2016	Number of shares	Average price of the period	Maturity date	Thousands of euros
Exercised shares	1,624,221	5.7154	01/26/2017 – 02/10/2017	9,283
Potential maximum ⁽¹⁾	31,870,828	5.7629	01/26/2017 – 02/10/2017	183,669

2015	Number of shares	Average price of the period	Maturity date	Thousands of euros
Exercised shares	3,027,195	5.8796	01/15/2016 – 02/19/2016	17,799
Potential maximum ⁽¹⁾	12,111,494	6.0173	01/15/2016 – 02/19/2016	72,878

(1) Maximum number of additional shares that could be accumulated according to the described mechanism until the maturity of the structures (assuming that the cash price during the remaining life of the structure is always below the strike price).

Distribution of dividends with charge to 2016 results

The IBERDROLA's Board of Directors agreed to propose to the Ordinary General Shareholders' Meeting, the distribution with a charge to the 2016 results and the retained earnings from previous years, a gross dividend of EUR 0.03 for each IBERDROLA share with dividend entitlement, outstanding at the date on which payment is made.

If the number of IBERDROLA's shares outstanding at the date on which the proposed dividend payment is made is equal to the number of shares outstanding at the date of authorization for issue of these Consolidated financial statements i.e. 6,549,990,000 ordinary shares, the dividend will amount to EUR 193,800 thousand.

In addition, at the date of authorization for issue of these Consolidated financial statements, IBERDROLA's Board of Directors resolved to propose to the General Shareholders' Meeting, to maintain the system of remuneration to shareholders implemented in 2010, known as the *Iberdrola Flexible Dividend*.

Under this scheme, IBERDROLA offered shareholders an alternative that allowed them to receive IBERDROLA's bonus shares without limiting their eligibility to receive in cash at least an amount equal to the paid out as the 2016 final dividend.

This option would be instrumented through a paid-up capital increase, which must be approved by the IBERDROLA's General Shareholders' Meeting. In the case it is approved, the paid-up capital increase may be executed by the Board of Directors or, when delegated by it, by the Executive Committee. The execution would coincide with the date on which the shareholders would traditionally be paid the final dividend for 2016.

In the capital increase, each shareholder of IBERDROLA would receive a free of charge allocation rights for each share of IBERDROLA they hold. These free of charge allocation rights will be eligible for trading on the Madrid, Barcelona, Bilbao and Valencia Stock Exchanges.

Depending on the choice made, during the capital increase execution, each of the IBERDROLA's shareholders would be able to receive either new bonus shares of IBERDROLA or cash on selling the free of charge allocation rights to IBERDROLA (at a guaranteed fixed price through the commitment assumed by IBERDROLA) or at the market rate (in which case the price obtained varies in line with the free of charge allocation rights).

The capital increase was carried out free of fees and expenses for subscribers with regards to the allocation of the new shares issued. IBERDROLA assumed the capital increase, placed into circulation and admission to trading expenses, and any other expenses related to the issues. However, the entities participating in the Spanish Central Securities Depository (Sociedad de Gestión de los Sistemas de Registro, Compensación y Liquidación de Valores, S.A.U. or Iberclear) at which IBERDROLA's shares were deposited were free to establish, in accordance with prevailing legislation, any administration fees, commissions or expenses chargeable to the shareholders for maintaining the securities in the accounting records. Furthermore, these participating entities could freely establish, in accordance with prevailing legislation, any commissions or expenses chargeable to the shareholders for processing purchase and sale orders of free of charge allocation rights.

Share-based compensation plans

2011-2013 Strategic Bonus Programme

The IBERDROLA's General Shareholders' Meeting of 27 May 2011 approved a strategic bonus for executive directors, senior management and other management personnel of IBERDROLA and its subsidiaries (287 beneficiaries), related to the fulfilment of the strategic objectives in 2011-2013, and to be settled with the delivery of IBERDROLA shares.

The 2011-2013 Strategic Bonus had a term of three years for the 2011-2013 period and shares are delivered as deferred income in 2014, 2015 and 2016.

On 24 June 2014 the Board of Directors, on the recommendation of the Appointments and Remuneration Committee, decided to pay the 2011-2013 Strategic Bonus on determining that 93.20% of the objectives had been met.

In the first half of 2016, 2015 and 2014, therefore, three annual payments were made in the form of 2,872,129, 3,120,340 and 3,208,800 shares, respectively. These shares include those delivered to executive directors (Note 46) and to senior management (Note 48).

The heading "Staff costs" of the Consolidated income statements of 2016 and 2015, includes a credit of EUR 2,068 thousand and a debit of EUR 5,483 thousand and, respectively, corresponding to the amount incurred for the incentive plans, that has been registered as a debit and credit under the "Other reserves" heading of the Consolidated statement of financial position, respectively.

2014-2016 Strategic Bonus Programme

The IBERDROLA's General Shareholders' Meeting of 28 March 2014 approved, as the seventh item on the agenda, a strategic bonus for executive directors, senior management and other management personnel (350 beneficiaries), tied to the IBERDROLA Group's performance in relation to certain parameters throughout the assessment period from 2014 to 2016, relating to:

- (a) The performance of consolidated net profit. The target is that annual average growth, taking year end 2014 as the base, should reach 4%. This target will be treated as unmet if growth is less than 2%.
- (b) Comparative performance of the share price with respect to the Eurostoxx Utilities index and the shares of the five main European competitors (ENEL, E.ON, RWE, EDF and ENGIE). This target will be treated as having been met if the share outperforms at least three of the benchmarks.
- (c) Improvement of the IBERDROLA's financial strength as measured by the ratio FFO/Net Debt (Funds From Operations / Net Debt) > 22%.

The maximum number of shares to be delivered to beneficiaries of the 2014-2016 Strategic Bonus is 19,000,000 shares equivalent to 0.3% of the share capital at the agreement date, corresponding to executive directors a maximum of 2,200,000 shares.

The payment period for the scheme will run from 2017 to 2019. Payments will be made in the form of shares on a deferred basis in those three years.

The "Staff costs" heading in 2016 and 2015 Consolidated income statements includes a credit of EUR 5,879 thousand and a debit of EUR 30,239 thousand, respectively, which correspond to the accrued amount for these incentive plans, which have been registered in "Other reserves" and "Provisions – Other provisions" in the Consolidated financial statement, respectively.

As a result of UIL's integration (Note 42), the 2014-2016 Strategic Bonus for AVANGRID's company directors will be liquidated in cash for the accrued amount for 2015 and 2014, and have been substituted in 2016 by a new one referenced to AVANGRID's shares. The accumulated amount at 31 December 2015, which amounts to EUR 11,810 thousand has been reclassified into the heading "Other non-current payables" and will be liquidated as planned in 2017 and 2018.

AVANGRID's share-based incentive plan

As already mentioned, AVANGRID approved a share-based incentive plan, known as the *Avangrid, Inc. Omnibus Incentive Plan*, for managers of companies in its group. The total number of shares on the plan is 2,500,000, of which 1,310,487 have been awarded (1,298,683 in July 2016, and 11,804 in December 2016).

The shares will be awarded in respect of the achievement of a number of performance and market indicators related to the 2016-2019 plan, and will be payable in three equal instalments in 2020, 2021 and 2022. The fair value of the shares at the time of delivery was USD 31.80 per share, which is booked on a straight-line basis over the required service period of approximately seven years based on expected achievement.

Total liabilities in relation to share-based remuneration, booked under "Other non-current liabilities", was EUR 2,291 thousand at 31 December 2016.

SCOTTISH POWER share-based incentive plan

Lastly, SCOTTISH POWER has share-based plans for its employees. There are two types of plans:

- **Sharesave Schemes:** savings plans in which employees decide the amount they want to contribute to the plan (between GBP 5 and GBP 250 on a monthly basis) and this is deducted monthly from their salary. At the end of a three or five year saving period, as applicable to each plan, employees may use the money saved to buy IBERDROLA shares at a discounted option price set at the beginning of the plan or to receive the amount saved in cash.

The fair value of the employee's share purchase options is determined at the start of the plan, and is registered in the income statement over the plan's consolidation period (three or five years) with a credit to equity. The "Staff costs" heading in the 2016 and 2015 Consolidated income statements includes EUR 1,558 thousand and EUR 1,596 thousand, respectively for this concept.

The plan expired at 31 December 2015, therefore the employee options were exercised or had expired. The new plan entitles employees to 5,531,681 shares as of 31 December 2016.

The number of transactions of stock options are as follows:

	Number of accounts	Number of shares
Balance at 01.01.2015	–	–
Additions	3,023	6,298,862
Exercised	(3)	(1,866)
Derecognised	(142)	(257,553)
Balance at 12.31.2015	2,878	6,039,443
Additions	–	–
Exercised	(60)	(58,211)
Derecognised	(202)	(449,551)
Balance at 12.31.2016	2,616	5,531,681

- Share Incentive Plan: this plan has an option for purchasing shares with tax incentives plus a contribution from the company. The employees decide on the amount they wish to contribute, which is deducted from their monthly salary (the maximum contribution allowed by the law in the United Kingdom is GBP 125 on a monthly basis). The shares purchased with this contribution are called partnership shares. Additionally, SCOTTISH POWER complements the employee's contribution to a maximum of GBP 50 monthly. The shares purchased with the company's contribution are called matching shares.

The contributions, both from the company and the employees, are contributed to a trust which buys the shares, and they are held in this trust until withdrawn by the employees. All shares are purchased in the market at the monthly market price.

The partnership shares are owned by the employees who purchased them with their own money, however, the shares acquired with the contribution from the company (matching shares) are not consolidated until three years after the date of purchase. The matching shares acquired by the trust at 31 December 2016 and 2015 amount to 1,370,213 and 1,635,172 shares, respectively. Additionally, at 31 December 2016 and 2015, the trust holds 4,192 and 3,391 shares, respectively, yet not assigned to employees.

The contributions of the Company are made in cash on a monthly basis and are charged to the income statement during the three years the employee must remain in the company in order to be entitled to these shares. The heading "Staff costs" of the Consolidated income statements for 2016 and 2015 includes EUR 2,615 thousand and EUR 3,016 thousand, respectively, for this concept.

21. EQUITY INSTRUMENTS HAVING THE SUBSTANCE OF A FINANCIAL LIABILITY

The change in this heading of the Consolidated statements of financial position at 31 December 2016 and 2015 is as follows:

Thousands of euros	
Balance at 01.01.2015	281,721
Finance costs accrued during the year (Note 41)	22,304
Payments	(118,284)
Translation differences	30,689
Balance at 12.31.2015	216,430
Finance costs accrued during the year (Note 41)	8,821
Payments	(94,156)
Translation differences	5,959
Balance at 12.31.2016	137,054

The balance under this heading of the Consolidated statements of financial position at 31 December 2016 and 2015 accrues interest at an average rate of 5.46% and 8.53%, respectively.

22. DEFERRED INCOME

The change in this heading of the Consolidated statements of financial position at 31 December 2016 and 2015 is as follows:

Thousands of euros	Grants	Investment Tax Credits	Emission rights	Transfer of assets from third parties	Assets financed from third parties	Other deferred income	Total deferred income
Balance at 01.01.2015	292,574	1,316,944	26	2,659,001	1,720,788	131,578	6,120,911
Additions	15,740	–	516	92,285	223,256	16,053	347,850
Disposals	(12)	(268)	–	(1,426)	(832)	–	(2,538)
Transfers	3,622	–	5	(550)	20,055	3	23,135
Translation differences	7,093	148,731	–	4,463	58,416	36,153	254,856
Allocation to the income statement (Note 4.n)	(18,230)	(69,751)	(516)	(82,273)	(46,982)	(15,010)	(232,762)
Balance at 12.31.2015	300,787	1,395,656	31	2,671,500	1,974,701	168,777	6,511,452
Additions	12,944	–	354	81,291	282,421	2,435	379,445
Disposals	(24)	–	(31)	(3,178)	(1,013)	(2)	(4,248)
Transfers	(2,252)	–	–	994	1,279	(21)	–
Translation differences	3,747	69,974	–	(7,798)	(92,434)	7,759	(18,752)
Allocation to the income statement (Note 4.n)	(17,507)	(61,394)	(354)	(113,560)	(70,615)	(14,165)	(277,595)
Balance at 12.31.2016	297,695	1,404,236	–	2,629,249	2,094,339	164,783	6,590,302

23. PROVISIONS FOR PENSIONS AND SIMILAR OBLIGATIONS

The detail of this heading in the Consolidated statements of financial position is as follows:

Thousands of euros	12.31.2016	12.31.2015
Defined benefit plans (Spain)	510,299	459,986
Long-service bonuses and other long-term benefits (Spain)	43,062	41,046
Defined benefit plans (United Kingdom)	519,754	357,273
Defined benefit plans (USA)	1,103,160	1,145,242
Defined benefit plans and other long term benefits (Spain and other countries)	67,409	62,698
Restructuring plans	146,677	177,611
Total	2,390,361	2,243,856

Each year the IBERDROLA Group estimates through independent expert's actuarial evaluations the payment amount for pensions and similar commitments in the year ahead. This amount is recorded as a current liability in the Consolidated statement of financial position.

23.a) Defined benefit plan and other non-current benefits

Spain

The IBERDROLA Group's main defined benefit commitments to its employees in Spain, other than Social Security benefits, are as follows:

- Former employees under the IBERDROLA Group's Collective Labour Agreement retired before 9 October 1996 are covered by a defined benefit retirement pension scheme, the actuarial value of which is externalised in full at 31 December 2016 and 2015.

The IBERDROLA Group has no liabilities in relation to these employees nor does it have any claims on any potential returns from this plan assets in excess of the guaranteed benefits.

- Also, in relation to current employees and employees who have retired since 1996, covered by the IBERDROLA Group's Collective Labour Agreement and participant/beneficiary of the Iberdrola Pension Scheme, its risk benefits (e.g. widowhood, permanent disability or orphanage), guaranteeing a defined benefit at the time the event giving rise to such benefits occurs, are instrumented through a pluriannual insurance policy. The defined benefit is measured as the difference between the present actuarial value of the benefit at the time of the contingency and the employees' consolidated rights at the time of the event giving rise to the benefits under the aforementioned defined benefit plan, if lower. The premium paid for this insurance policy in 2016 and 2015 amounted to EUR 11,112 thousand and EUR 12,662 thousand, respectively, and is recorded under "Staff costs" in the Consolidated income statements.
- In addition, the IBERDROLA Group also has a provision for certain commitments to its employees in Spain other than those indicated above, which are covered by internal provisions related to social benefits, consisting mainly of free electricity supply, with an annual consumption limit for retired employees, and other long-term benefits, primarily long-service bonus for active employees in the 10, 20, and 30 years of service (until the signing of the VI Collective Agreement of the IBERDROLA Group on 20 July 2015, the long-service bonus for active employees was in the 25 and 40 years of service).

The changes in 2016 and 2015 in the provision recognised to meet the commitments set out in the paragraph above are as follows:

Thousands of euros	Electricity for employees	Long-service bonus
Balance at 01.01.2015	551,549	88,354
Service cost (Note 35)	9,136	4,773
Other costs charged to "Staff costs" (Note 35)	(8,241)	–
Interest cost (Note 41)	10,979	1,097
Actuarial gains and losses		
To profits/(losses) (Note 35)	–	2,896
To reserves	(89,071)	–
Payments	(14,366)	(56,074)
Balance at 12.31.2015	459,986	41,046
Service cost (Note 35)	6,981	3,227
Interest cost (Note 41)	9,575	678
Actuarial gains and losses		
To profits/(losses) (Note 35)	–	3,606
To reserves	48,802	–
Payments	(15,045)	(5,495)
Balance at 12.31.2016	510,299	43,062

The main assumptions used in the actuarial valuations undertaken to determine the provision required at 31 December 2016 and 2015 to cover the aforementioned obligations are as follows:

	2016			2015		
	Discount rate	Wage increase/kWh price increase	Survivorship tables	Discount rate	Wage increase/kWh price increase	Survivorship tables
Long-service bonus and electricity for employees	0.80% / 1.50%	1.00% / 2017 1.00%; 2018 1.30%; 2019 1.50%; 2020 1.60%; 2021 1.80%; 2022 on 2.00%	PERM/F 2000P	1.70%/ 2.10%	1.00%/ 2.00%	PERM/F 2000P

In both cases, the retirement age has been established pursuant to the Law 27/2011, of 1 August, on the upgrade, adjustment and modernisation of the Social Security system, providing for a gradual increase in the retirement age in accordance with the law.

The average length at the end of the year of the liability for the long-service bonus and electricity for employees' benefits is 7.8 and 18.6 years, respectively.

The most relevant figures for these commitments over the last years are the following:

Thousands of euros	2016	2015	2014	2013	2012
Present value of obligation	(553,361)	(501,032)	(639,903)	(555,265)	(503,801)
Experience adjustments	4,664	25,355	5,442	15,280	(2,067)

The sensitivity of the present value of the obligation of these commitments to changes in the discount rate at 31 December 2016 is as follows:

Thousands of euros	Increase/decrease in discount rate (basis points)	Effect on present value of the obligation
Electricity for employees	+10 bp (10 bp)	(9,683) 9,970
Long-service bonus	+10 bp (10 bp)	(336) 340

United Kingdom (SCOTTISH POWER)

SCOTTISH POWER employees residing in the United Kingdom, hired before 1 April 2006, are covered by several defined benefit retirement plans: ScottishPower Pension Scheme (SPPS) and Manweb Group of Electricity Supply Pension Scheme (Manweb).

The key data pertaining to the United Kingdom plans are the following:

	United Kingdom	
Thousands of euros	12.31.2016	12.31.2015
Present value of the obligation	(6,261,592)	(6,272,818)
Fair value of the plan assets	5,741,838	5,915,545
Net asset / (Net provision)	(519,754)	(357,273)
Amounts recognized in the Consolidated statement of financial position:		
Provision for pensions and similar obligations	(519,754)	(357,273)
Net asset / (Net provision)	(519,754)	(357,273)

The movement in the present value of the obligation for this concept is as follows:

Thousands of euros	United Kingdom
Present value of obligation at 01.01.2015	5,884,621
Service cost (Note 35)	76,034
Cost for past services (Note 35)	29,847
Interest cost (Note 41)	240,291
Actuarial gains and losses to reserves	(62,670)
Members' contributions	12,531
Payments	(258,194)
Translation differences	350,358
Present value of obligation at 12.31.2015	6,272,818
Service cost (Note 35)	63,851
Cost for past services (Note 35)	18,080
Interest cost (Note 41)	209,637
Actuarial gains and losses to reserves	859,441
Members' contributions	10,507
Payments	(320,807)
Translation differences	(851,935)
Present value of obligation at 12.31.2016	6,261,592

The average length at the end of the year of the liability for the employee benefits described previously is 21 years for SPPS and 19 years for Manweb, approximately.

The movement in the fair value of the plan assets is as follows:

Thousands of euros	United Kingdom
Fair value at 01.01.2015	5,491,355
Revaluation (Note 41)	227,485
Actuarial gains and losses to reserves	(77,098)
Company contributions	197,103
Members' contributions	12,531
Payments	(258,194)
Translation differences	322,363
Fair value at 12.31.2015	5,915,545
Revaluation (Note 41)	201,330
Actuarial gains and losses to reserves	552,312
Company contributions	182,845
Members' contributions	10,507
Payments	(320,807)
Translation differences	(799,894)
Fair value at at 12.31.2016	5,741,838

The main assumptions used in the actuarial evaluations undertaken to determine the provision required at 31 December 2016 and 2015 to cover the aforementioned obligations are as follows:

2016			
	Discount rate	CPI/ Wage increase	Survivorship table (before retirement/after retirement)
United Kingdom	2.90%	3.00%/3.50%	Men: 85% AMC00/ 90% S2PMA CMI2013 (1.50% improvement rate) Women: 85%AFC00/ 100% S2PFA CMI2013 (1.50% improvement rate)
2015			
	Discount rate	CPI/ Wage increase	Survivorship table (before retirement/after retirement)
United Kingdom	3.80%	3.10%/3.60%	Men: 85% AMC00/ 95% PNMA00 CMI 2011 (1.15% improvement rate) Women: 85% AFC00/ 105% PNFA00 CMI 2011 (1.15% improvement rate)

The most relevant figures for this plan over the last years have been the following:

Thousands of euros	2016	2015	2014	2013	2012
Present value of the obligation	(6,261,592)	(6,272,818)	(5,884,621)	(5,055,518)	(4,951,415)
Fair value of the plan assets	5,741,838	5,915,545	5,491,355	4,656,454	4,340,301
Net asset / (Net provision)	(519,754)	(357,273)	(393,266)	(399,064)	(611,114)
Experience adjustments in the plan liabilities	(17,836)	27,541	59,629	(471)	(45,044)
Experience adjustments in the plan assets	552,312	(77,098)	329,368	250,978	204,884

The sensitivity at 31 December 2016 of the present value of the obligation of these commitments to changes in the discount rate, survivorship tables and inflation is as follows:

Basis points	Thousands of euros
<i>Increase/decrease in discount rate</i>	<i>Effect on present value of the obligation</i>
+10	(116,718)
(10)	125,787

Basis points	Thousands of euros
<i>Increase/decrease in inflation</i>	<i>Effect on present value of the obligation</i>
+10	117,235
(10)	(31,834)

Years	Thousands of euros
<i>Increase/decrease in survivorship tables estimates</i>	<i>Effect on present value of the obligation</i>
+1	213,326

USA (AVANGRID)

The former employees of SCOTTISH POWER that now form part of the workforce of the IBERDROLA Group in the United States, most of them belonging to the workforce of the Iberdrola Renewables Holding Inc. (hereinafter, ARHI), are members of various post-employment plans (Supplemental Executive Retirement Plan, Iberdrola Renewables Retiree Benefits Plan and Iberdrola Renewables Retirement Plan).

With effect from 30 April 2011, a change affecting all plan participants occurred in the Iberdrola Renewables Retiree Benefits Plan, whereby the benefit receivable at retirement age was set at the amount accrued until 30 April 2011 and the plan became a defined-contribution scheme from that date onwards.

On the other hand, the employees of the AVANGRID NETWORKS Group are affiliated to various defined benefit retirement pension plans (Qualified Pension Plans, Non Qualified Pension Plans), disability benefit plans (Long Term Disability Plans) and health insurance plans (Postretirement Welfare Plans).

Finally, as indicated in Note 2.c, UIL has been acquired on 16 December 2015. UIL Group's employees were covered by several defined benefit retirement plans (Qualified Pension Plans, Non Qualified Pension Plans) and health plans (Postretirement Welfare Plans).

The most significant data for the ARHI, UIL and AVANGRID NETWORKS plans are as follows:

	ARHI		UIL		AVANGRID NETWORKS	
Thousands of euros	12.31.2016	12.31.2015	12.31.2016	12.31.2015	12.31.2016	12.31.2015
Present value of the obligation	(72,785)	(73,133)	(1,126,064)	(1,055,586)	(2,629,032)	(2,595,775)
Fair value of the plan assets	37,722	38,284	695,330	647,357	1,991,669	1,893,611
Net asset / (net provision)	(35,063)	(34,849)	(430,734)	(408,229)	(637,363)	(702,164)
Amounts recognized in the Consolidated statement of financial position:						
Provision for pensions and similar commitments	(35,063)	(34,849)	(430,734)	(408,229)	(637,363)	(702,164)
Net asset/ (net provision)	(35,063)	(34,849)	(430,734)	(408,229)	(637,363)	(702,164)

The movement in the present value of the obligation for this concept is as follows:

Thousands of euros	ARHI	UIL	AVANGRID NETWORKS
Present value of the obligation at 01.01.2015	73,564	–	2,460,863
Modification of the consolidation perimeter (Note 42)	–	1,057,741	–
Service cost (Note 35)	745	591	37,304
Interest cost (Note 41)	3,065	1,810	99,309
Employee contributions	–	184	–
Plan modifications (Note 35)	–	–	(5,520)
Actuarial gain and losses to reserves	(8,133)	(182)	(117,404)
Payments	(4,445)	(3,676)	(160,303)
Translation differences	8,337	(882)	281,526
Present value of the obligation at 12.31.2015	73,133	1,055,586	2,595,775
Service cost (Note 35)	420	14,538	35,986
Interest cost (Note 41)	2,686	43,918	101,485
Plan modifications (Note 35)	–	(8,989)	–
Actuarial gain and losses to reserves	(1,884)	19,006	(82,042)
Payments	(5,094)	(58,250)	(150,095)
Translation differences	3,524	60,255	127,933
Present value of the obligation at 12.31.2016	72,785	1,126,064	2,629,032

The average duration at the end of the year of the liability for defined benefit plan in ARHI, UIL and AVANGRID NETWORKS is 9, 12 and 11 years, respectively.

The movement in the fair value of the plan assets is as follows:

Thousands of euros	ARHI	UIL	AVANGRID NETWORKS
Fair value at 01.01.2015	38,519	–	1,824,332
Modification of the consolidation perimeter (Note 42)	–	661,020	–
Revaluation (Note 41)	1,573	1,118	73,562
Actuarial gain and losses to reserves	(2,695)	(10,620)	(95,019)
Employee contributions	–	184	–
Company contributions	968	334	43,138
Payments	(4,445)	(3,676)	(160,303)
Translation differences	4,364	(1,003)	207,901
Fair value at 12.31.2015	38,284	647,357	1,893,611
Revaluation (Note 41)	1,353	26,626	73,815
Actuarial gain and losses to reserves	864	20,218	38,298
Company contributions	493	21,757	38,313
Payments	(5,094)	(58,250)	(150,095)
Translation differences	1,822	37,622	97,727
Fair value at 12.31.2016	37,722	695,330	1,991,669

The main assumptions used in the actuarial valuations undertaken to determine the provision required at 31 December 2016 and 2015 related to these plans are as follows:

2016				
	Discount rate	CPI/ Wage increase	Health insurance cost Pre-Medicare/medicare	Survivorship tables
ARHI	3.81%	2.00%/ N/A	Based on the year RX: 6.75%/8.50% (2017); 6.50%/8.00%(2018) ; [...] : 4.50%/4.50% (2028 onwards)	RP-2006 fully generational table using the scale MP-2016
UIL	4.24%	2.00%/ 3.50% -3.80%	Based on the year RX: 6.75%/8.50% (2017); 6.50%/8.00%(2018) ; [...] : 4.50%/4.50% (2028 onwards)	RP-2006 fully generational table using the scale MP-2016
AVANGRID NETWORKS	4.12%	2.00% / Based on the age and Union/ Non Union	Based on the year RX: 6.75%/8.50% (2017); [...]; 4.50%/4.50% (2028 onwards)	RP-2006 fully generational table using the scale MP-2016

2015				
	Discount rate	CPI/ Wage increase	Health insurance cost Pre-Medicare/medicare	Survivorship tables
ARHI	3.90%	2.10%/ N/A	Based on the year RX: 7.00%/9.00% (2016); 6.75%/8.50% (2017); [...]; 4.50%/4.50% (2028 on)	RP-2006 fully generational table using the scale MP-2015
UIL	4.24%	2.00%/ 3.50% -3.80%	Based on the year RX: 7.00%/9.00% (2016); 6.75%/8.50% (2017); [...]; 4.50%/4.50% (2028 on)	RP-2006 fully generational table using the scale MP-2015
AVANGRID NETWORKS	4.10%	2.10% / Based on the age and Union/ Non Union	Based on the year RX: 7.00%/9.00% (2016); 6.75%/8.50% (2017); [...]; 4.50%/4.50% (2028 on)	RP-2006 fully generational table using the scale MP-2015

The main figures for ARHI's pension plans over the past few years have been as follows:

Thousands of euros	2016	2015	2014	2013	2012
Present value of the obligation	(72,785)	(73,133)	(73,564)	(60,777)	(70,708)
Fair value of the plan assets	37,722	38,284	38,519	33,813	38,021
(Net provision)	(35,063)	(34,849)	(35,045)	(26,964)	(32,687)
Experience adjustments arising from plan liabilities	1,626	7,834	(1,955)	2,259	1,040
Experience adjustments arising from plan assets	864	(2,695)	1,805	1,958	1,974

The main figures for AVANGRID NETWORKS' pension plans over the past few years have been as follows:

Thousands of euros	2016	2015	2014	2013	2012
Present value of the obligation	(2,629,032)	(2,595,775)	(2,460,863)	(1,921,426)	(2,270,728)
Fair value of the plan assets	1,991,669	1,893,611	1,824,332	1,671,768	1,754,602
(Net provision)	(637,363)	(702,164)	(636,531)	(249,658)	(516,126)
Experience adjustments arising from plan liabilities	37,797	(11,669)	(17,729)	(17,831)	(22,262)
Experience adjustments arising from plan assets	38,298	(95,019)	40,051	78,020	133,925

The main figures for UIL's pension plans have been as follows:

Thousands of euros	2016	2015
Present value of the obligation	(1,126,064)	(1,055,586)
Fair value of the plan assets	695,330	647,357
(Net provision)	(430,734)	(408,229)
Experience adjustments arising from plan liabilities	(30,075)	182
Experience adjustments arising from plan assets	20,218	(10,620)

The sensitivity at 31 December 2016 of the present value of the obligation of these commitments to changes in the discount rate, wage increase and health cost is as follows:

Thousands of euros			
Basis points	Effect on present value of the obligation		
Increase/decrease in discount rate	AVANGRID NETWORKS	UIL	ARHI
+10	(27,914)	(14,964)	(668)
-10	28,438	15,297	681

Thousands of euros			
Basis points	Effect on present value of the obligation		
Increase/decrease in wages	AVANGRID NETWORKS	UIL	ARHI
+10	2,769	2,732	-
-10	(2,744)	(2,699)	-

Thousands of euros			
Basis points	Effect on present value of the obligation		
Increase/decrease in health cost	AVANGRID NETWORKS	UIL	ARHI
+25	1,371	1,556	268
-25	(1,282)	(1,484)	(239)

ELEKTRO

The employees of ELEKTRO are the beneficiaries of a defined-benefit retirement plan.

The most significant data regarding this plan are as follows:

ELEKTRO		
Thousands of euros	12.31.2016	12.31.2015
Present value of the obligation	(336,323)	(206,387)
Fair value of the plan assets	376,175	270,711
Total	39,852	64,324

The related amounts have not been recognised in the Consolidated statements of financial position at 31 December 2016 and 2015, respectively, since the requirements set forth in the current legislation for their accounting treatment are not met.

The variation in the present value of the obligation on this account is as follows:

Thousands of euros	ELEKTRO
Present value of the obligation at 01.01.2015	273,740
Service cost (Note 35)	1,521
Interest cost (Note 41)	28,060
Actuarial gains and losses to reserves	(22,437)
Members contributions	938
Payments	(14,631)
Translation differences	(60,804)
Present value of the obligation at 12.31.2015	206,387
Service cost (Note 35)	840
Interest cost (Note 41)	26,233
Actuarial gains and losses to reserves	60,057
Members contributions	925
Payments	(16,493)
Translation differences	58,374
Present value of the obligation at 12.31.2016	336,323

The average duration at year end of defined benefit obligation liability in ELEKTRO is 13.7 years.

The variation in the fair value of the plan assets is as follows:

Thousands of euros	ELEKTRO
Fair value at 01.01.2015	336,762
Revaluation (Note 41)	34,696
Actuarial gains and losses to reserves	(10,632)
Company contributions	764
Members contributions	938
Payments	(14,631)
Translation differences	(77,186)
Fair value at 12.31.2015	270,711
Revaluation (Note 41)	34,812
Actuarial gains and losses to reserves	16,502
Company contributions	783
Members contributions	925
Payments	(16,493)
Translation differences	68,935
Fair value at 12.31.2016	376,175

As the surplus was not recognised, the actuarial differences recognised in reserves were adjusted upwards in 2016 and downwards in 2015 by EUR 43,507 thousand and EUR 11,048 thousand in the application of the current legislation IFRIC 14: "IAS -9 - The limit on a defined benefit asset, minimum funding requirements and their interaction". Moreover, in the years 2016 and 2015, and for the same concept, the finance costs recognised were adjusted upwards by EUR 8,475 thousand and EUR 6,636 thousand, respectively.

The main assumptions applied in the actuarial reports that determined the provision needed to meet the abovementioned commitment at 31 December 2016 and 2015 are as follows:

	2016			2015		
	Discount rate	CPI/ Wage increase	Survivorship tables	Discount rate	CPI/ Wage increase	Survivorship tables
ELEKTRO	11.03%	5.00%/7.63%	AT – 2000 (1996 US Annuity 2000)	12.07%	4.50%/7.63%	AT – 2000 (1996 US Annuity 2000)

The most relevant figures for ELEKTRO's pensions plan are as follows:

Thousands of euros	2016	2015	2014	2013	2012
Present value of the obligation	(336,323)	(206,387)	(273,740)	(248,859)	(398,102)
Fair value of the plan assets	376,175	270,711	336,762	317,751	410,516
Net assets	39,852	64,324	63,022	68,892	12,414
Experience adjustments arising from plan liabilities	(15,966)	(5,980)	(3,507)	(1,827)	6,142
Experience adjustments arising from plan assets	16,502	(10,632)	47	(48,654)	55,068

The sensitivity at 31 December 2016 of the present value of the obligation of these commitments to changes in the discount rate, wage increase, and survivorship tables is as follows:

Basis points	Thousands of euros
Increase/decrease in discount rate	Effect on present value of the obligation
+10	(3,601)
-10	4,411
Basis points	Thousands of euros
Increase/decrease in wages	Effect on present value of the obligation
+10	925
-10	(820)
Years	Thousands of euros
Increase/decrease in survivorship tables estimates	Effect on present value of the obligation
+1	4,142

The main categories of plan assets, as a percentage of total plan assets at year end, are shown in the table below:

2016				
	Equity securities	Fixed-income securities	Cash and cash equivalents	Others
United Kingdom	24%	51%	5%	20%
ARHI				
Retirement plan	31%	48%	1%	20%
Retiree Benefits Plan	45%	55%	-	-
UIL				
Qualified Pension Plans	54%	41%	-	5%
Postretirement Welfare Plans	72%	24%	3%	1%
AVANGRID NETWORKS				
Qualified Pension Plans	35%	37%	2%	26%
Postretirement Welfare Plans	49%	35%	3%	13%
ELEKTRO	8%	85%	-	7%
2015				
	Equity securities	Fixed-income securities	Cash and cash equivalents	Others
United Kingdom	23%	50%	5%	22%
ARHI				
Retirement plan	40%	47%	-	13%
Retiree Benefits Plan	46%	54%	-	-
UIL				
Qualified Pension Plans	58%	40%	-	2%
Postretirement Welfare Plans	67%	26%	5%	2%
AVANGRID NETWORKS				
Qualified Pension Plans	34%	36%	3%	27%
Postretirement Welfare Plans	53%	31%	2%	14%
ELEKTRO	11%	79%	-	10%

The assets associated with these plans include neither financial instruments issued by the IBERDROLA Group nor tangible nor intangible assets.

Moreover, the breakdown of assets of the plans measured at fair value by level is as follows:

Thousands of euros	Value at 12.31.2016	Level 1	Level 2	Level 3
United Kingdom	5,741,838	278,660	4,968,932	494,246
ARHI	37,722	126	32,781	4,815
UIL	695,330	3,000	655,052	37,278
AVANGRID NETWORKS	1,991,669	393,345	1,092,734	505,590
ELEKTRO	376,175	224,180	108,280	43,715
Total	8,842,734	899,311	6,857,779	1,085,644

Thousands of euros	Value at 12.31.2015	Level 1	Level 2	Level 3
United Kingdom	5,915,545	197,843	5,065,856	651,846
ARHI	38,284	–	33,652	4,632
UIL	647,357	28,963	618,394	–
AVANGRID NETWORKS	1,893,611	543,613	844,532	505,466
ELEKTRO	270,711	159,243	77,657	33,811
Total	8,765,508	929,662	6,640,091	1,195,755

Other commitments with employees

In addition, some IBERDROLA Group companies have provisions to meet certain commitments with their employees, other than those described above, which are met by in-house pension funds.

The variation in 2016 and 2015 in the provision recognised to meet the commitments referred to in the preceding paragraph is as follows:

Thousands of euros	
Balance at 01.01.2015	59,740
Service cost (Note 35)	5,499
Interest cost (Note 41)	2,028
Actuarial gains and losses	
To profits/(losses) (Note 35)	(582)
To reserves	470
Payments and others	(4,457)
Balance at 12.31.2015	62,698
Service cost (Note 35)	5,147
Interest cost (Note 41)	1,966
Actuarial gains and losses	
To profits/(losses) (Note 35)	(838)
To reserves	1,343
Payments and others	(2,907)
Balance at 12.31.2016	67,409

23.b) Defined contribution plans

The active employees of the IBERDROLA Group and employees who have retired since 9 October 1996, beneficiaries of the IBERDROLA Group's pension plan with joint promoters, are covered by an occupational, defined-contribution pension system independent from the Social Security System, for retirement.

The periodic contribution to be made in accordance with this system and with the existing Collective Labour Agreement of the IBERDROLA Group is calculated as a percentage of the annual pensionable salary of each employee, except for employees hired after 9 October 1996, in which case the tax ratio is 55% contributed by the company and 45% contributed by the employee and for employees hired after the 20 July 2015, in which the company provides 1/3 of the total contribution if the worker contributes the remaining 2/3 until the date in which the employee takes part in the Base Salary Rating (SBC). At this moment the same criteria will be applied to those employees as the ones who were hired since 9 October 1996. The respective subsidiaries finance these contributions for all their active employees under 65.

The contributions made by the IBERDROLA Group in 2016 and 2015 amounted to EUR 22,823 thousand and EUR 25,529 thousand, respectively. These amounts are recognised under the "Staff costs" heading in the Consolidated income statements.

On the other hand, employees of SCOTTISH POWER hired after 1 April 2006 have the choice to be included by a defined contribution plan. The contribution made on behalf of these employees in 2016 and 2015 amounts to EUR 8,169 thousand and EUR 9,044 thousand and is recognised under "Staff costs" in the Consolidated income statements.

AVANGRID has business contribution plans defined as 401k. The contributions made by AVANGRID for these plans for the years 2016 and 2015 amounted to EUR 30,217 thousand and EUR 19,581 thousand, respectively, recorded under the "Staff costs" heading in the Consolidated income statements.

23.c) Restructuring plans

The IBERDROLA Group, given the interest shown by some employees in requesting early retirement, offered these employees a mutually agreed termination of the employment relationship. The IBERDROLA Group has carried out a process of individual termination contracts in Spain. The provisions regarding this concept at 31 December 2016 corresponding to the following restructuring plans are the following:

- 2012 restructuring plan: the IBERDROLA Group signed a total of 412 individual contracts terminating the employment relationship (400 in 2012, 11 in 2013 and 1 in 2014). At 31 December 2016, the IBERDROLA Group has a provision registered for this concept amounting to EUR 10,538 thousand.
- 2014 restructuring plan: the IBERDROLA Group signed a total of 389 individual contracts terminating the employment relationship. At 31 December 2016, the IBERDROLA Group has a provision registered for this concept amounting to EUR 78,904 thousand.
- 2015 restructuring plan: the IBERDROLA Group signed a total of 95 individual contracts terminating the employment relationship. At 31 December 2016, the IBERDROLA Group has a provision registered for this concept amounting to EUR 21,587 thousand.
- 2016 restructuring plan: the IBERDROLA Group signed a total of 64 individual contracts terminating the employment relationship. At 31 December 2016, the IBERDROLA Group has a provision registered for this concept amounting to EUR 16,831 thousand.
- The Company of the IBERDROLA Group, Iberdrola Ingeniería y Construcción, S.A.U. signed a total of 46 individual contracts terminating the employment relationship in Spain at 31 December 2016 (36 in 2015 and 10 in 2016), for which the IBERDROLA Group has registered a provision of EUR 11,198 thousand at 31 December 2016.
- Additionally, SCOTTISH POWER, has a provision at 31 December 2016 regarding various restructuring plans amounting to EUR 7,029 thousand.

The discounted present value of the provisions is charged to the "Finance cost" heading in the Consolidated income statement.

The variation in 2016 and 2015 on the provision recognised to meet these commitments is as follows:

Thousands of euros	Restructuring plans
Balance at 01.01.2015	179,143
Service cost (Note 35)	45,734
Interest cost (Note 41)	1,279
Actuarial gains and losses and other (Note 35)	559
Payments and translation differences (*)	(49,104)
Balance at 12.31.2015	177,611
Service cost (Note 35)	26,412
Interest cost (Note 41)	1,134
Actuarial gains and losses and other (Note 35)	(1,313)
Payments and translation differences (*)	(57,167)
Balance at 12.31.2016	146,677

(*) Payments made during 2016 and 2015 amount to EUR 56,093 thousand and EUR 49,005 thousand, respectively.

The main assumptions used in the actuarial studies undertaken to determine the provision required at 31 December 2016 and 2015 to cover the Group's obligations in relation to the aforementioned restructuring plans are the following:

	2016		2015	
	Discount rate	CPI	Discount rate	CPI
Employment regulation plan and other restructuring plans	0.40% / 0.50%	0.70%/1%	0.50%/1.16%	0.70%/1%

24. OTHER PROVISIONS

The detail and movement of "Other Provisions" on the liability side of the Consolidated statements of financial position in 2016 and 2015 are as follows:

Thousands of euros	Provisions for litigation, indemnity payments and similar costs	Provision for CO2 emissions (Note 4.q)	Provision for facility closure costs (Notes 4.r and 6.a)	Other provisions	Total other provisions
Balance at 01.01.2015	1,258,437	85,983	1,437,482	347,929	3,129,831
Charge or reversals for the year with a debit/credit to "Property, Plant and Equipment" (Note 4.d)	–	–	103,368	–	103,368
Charge for discount to present value (Note 41)	1,576	–	47,755	–	49,331
Charge for the year to income statement	95,756	122,773	–	42,372	260,901
Reversal due to excess	(280,627)	(4,806)	(3,783)	(11,199)	(300,415)
Modification of the consolidation perimeter (Note 42)	2,673	–	17,452	96,026	116,151
Translation differences	(570)	3,552	58,624	39,887	101,493
Payments made, transfers and other	(310,725)	(86,002)	(26,120)	(31,149)	(453,996)
Balance at 12.31.2015	766,520	121,500	1,634,778	483,866	3,006,664
Charge or reversals for the year with a debit/credit to "Property, Plant and Equipment" (Note 4.d)	–	–	(68,806)	(9,416)	(78,222)
Charge for discount to present value (Note 41)	(1,551)	–	31,954	–	30,403
Charge for the year to income statement	57,962	55,275	–	6,565	119,802
Reversal due to excess	(46,506)	(1,873)	(5,695)	(14,048)	(68,122)
Modification of the consolidation perimeter (Note 42)	–	–	–	11,830	11,830
Translation differences	16,308	(8,406)	(18,713)	21,699	10,888
Payments made, transfers and other	(192,000)	(112,375)	(43,457)	(27,254)	(375,086)
Balance at 12.31.2016	600,733	54,121	1,530,061	473,242	2,658,157

The IBERDROLA Group has provisions for responsibilities arising from litigation in progress and from indemnity payments, obligations, collateral and other similar guarantees, and those aimed at covering environmental risks. These last ones have been determined on the basis of a case-by-case analysis of the polluted assets status and the cost that will have to be incurred in cleaning them.

The IBERDROLA Group also maintains provisions to meet a series of costs needed for dismantling work at its nuclear and thermal power plants, its wind farms, and at other facilities.

The cost arising from dismantling obligations is recalculated on a regular basis to incorporate to the estimate of future costs the experience of the reasonableness of provisions of dismantling events, or to include new statutory or regulatory requirements.

The breakdown of provision for facility closure costs is as follows:

Thousands of euros	12.31.2016	12.31.2015
Thermal power plants	66,920	117,010
Nuclear plants	519,670	516,909
Wind-powered farms and other alternative plants	754,560	851,695
Combined cycle plants	146,843	99,287
Other facilities	42,068	49,877
Total	1,530,061	1,634,778

Regarding nuclear plants, this position covers the costs in which the plant operator will incur from the end of its useful life until ENRESA (Note 4.aa) takes control of them.

The discount rates (minimum and maximum range) before taxes of the main countries in which the IBERDROLA Group used in the present value of the operating provisions are:

Country	Currency	2016 Discount Rate	
		5 years	30 years
Spain	Euro	0.26%	2.61%
United Kingdom	Sterling Pound	0.47%	1.87%
United States	US Dollar	1.93%	3.07%

The estimated dates on which the IBERDROLA Group considers that it will have to meet the payments relating to the provisions included in this caption of the Consolidated statement of financial position at 31 December 2016 are as follows:

Thousands of euros	
2017	133,872
2018	169,086
2019	88,175
2020 and subsequent years	2,267,024
Total	2,658,157

25. BANK BORROWINGS AND OTHER FINANCIAL LIABILITIES-LOANS AND OTHERS

The detail of the bank borrowings pending of amortization at 31 December 2016 and 2015 and the repayment schedules are as follows:

Borrowings at 31 December 2016 and maturing in									
Thousands of euros	Balance at 12.31.2015	Balance at 12.31.2016 (*)	Current maturity	Non current maturity					Total non current
			2017	2018	2019	2020	2021	2022 and subsequent years	
Euros									
Finance leases	67,357	64,403	1,986	1,985	1,985	1,985	1,985	54,477	62,417
Debentures and bonds	15,216,656	16,530,475	2,683,621	1,666,937	1,537,720	1,793,616	1,151,514	7,697,067	13,846,854
Other financing transactions	4,246,408	4,860,516	613,332	210,201	2,014,804	931,899	328,536	761,744	4,247,184
Unpaid accrued interest	300,982	274,405	274,405	–	–	–	–	–	–
	19,831,403	21,729,799	3,573,344	1,879,123	3,554,509	2,727,500	1,482,035	8,513,288	18,156,455
Foreign currency									
US dollars	5,183,311	5,431,403	483,493	445,128	346,032	708,460	302,321	3,145,969	4,947,910
Sterling pound	3,441,873	2,984,923	314,449	199,211	47,969	47,972	338,197	2,037,125	2,670,474
Brazilian reals	841,574	879,500	192,501	216,738	73,358	89,449	87,435	220,019	686,999
Others	–	51,088	3,874	3,575	3,367	3,347	3,586	33,339	47,214
Unpaid accrued interest	146,314	143,969	143,969	–	–	–	–	–	–
	9,613,072	9,490,883	1,138,286	864,652	470,726	849,228	731,539	5,436,452	8,352,597
Total	29,444,475	31,220,682	4,711,630	2,743,775	4,025,235	3,576,728	2,213,574	13,949,740	26,509,052

(*) As at 31 December 2016, financial debt includes EUR 710,852 thousand from drawdowns on credit lines and credit facilities, and EUR 1,454,416 thousand from issues of domestic promissory notes and the Euro Commercial Paper (ECP).

The foregoing loan balances correspond to amounts drawn down and not repaid at 31 December 2016 and 2015. At 31 December 2016 and 2015, the IBERDROLA Group had undrawn loans and credit facilities amounting to EUR 6,583,500 thousand and EUR 7,054,459 thousand, respectively, maturing between 2017 and 2021 (Note 50).

The most significant financial transactions performed by the IBERDROLA Group during the year 2016 have been the following:

Capital markets issues:

- On 15 February 2016 the IBERDROLA Group, through its subsidiary Iberdrola International B.V. and with the guarantee of IBERDROLA, has closed a bond issue in the Euromarket for an amount of EUR 50 million. The bonds mature on 15 February 2023 and have a coupon of 6-months Euribor + 0.75%.
- On 21 April 2016 the IBERDROLA Group, through its subsidiary Iberdrola International B.V. and with the collateral provided by IBERDROLA, has closed a second green bonds issue in the Euromarket, after the operation closed in 2014, amounting to EUR 1,000 million. The bonds mature on 21 April 2026 and have a coupon rate of 1.125%. This issue was placed at 68% between Socially Responsible Investors (SRI), being the destination of the funds the refunding of wind farms in Spain, Portugal and the United Kingdom.
- On 13 May 2016 the IBERDROLA Group, through its subsidiary Avangrid Inc., has signed a commercial paper program amounting to USD 1,000 million. Additionally, the existing programs in the subsidiaries Avangrid NYSEG and CMP amounting to USD 200 million and USD 350 million have been cancelled.
- On 16 June 2016, the IBERDROLA Group, through its subsidiary Iberdrola International B.V. and with the guarantee of IBERDROLA, has closed a bond issue in the Euromarket for an amount of EUR 200 million. The bonds mature on 16 June 2018 and have a coupon rate of 3-months Euribor + 0.35%.
- On 15 September 2016 the IBERDROLA Group, through its subsidiary Iberdrola International, B.V., with collateral provided by IBERDROLA, completed its third green bond issue in the Euromarket, for EUR 700 million. The bonds mature on 15 September 2025 and have a 0.375% coupon. More than half of these bonds were placed with socially responsible investors, and the funds were intended to refinance *onshore* wind farms in the UK.
- On 29 November 2016 the IBERDROLA Group, through its subsidiary NYSEG, a company owned by Avangrid, Inc., completed an issue in the amount of USD 500 million. The bonds mature on 1 December 2026 and have a 3.25% coupon.
- On 7 December 2016 the IBERDROLA Group, through its subsidiary Finanzas, S.A.U., with collateral provided by IBERDROLA, completed its fourth green bond issue in the Euromarket, for EUR 750 million. The bonds mature on 7 March 2024 and have a 1.0% coupon. 60% of the bonds were placed with socially responsible investors, and the funds were intended to refinance wind farms in Spain.

On the same date, buyback offers were made for various outstanding bonds issued by IBERDROLA Group companies for subsequent redemption and cancellation. As a result, debt maturities were reduced by EUR 157.2 million in 2017 and EUR 158.3 million in 2018.

Banking Market:

- On 13 February 2016 IBERDROLA has extended the term of two syndicated credits amounting to EUR 4,243 million, extending its maturity in one year until 13 February 2021.
- On 25 February 2016 the IBERDROLA Group, through its subsidiary Iberdrola Mexico S.A. de C.V. (hereinafter, IBERDROLA MEXICO), has disposed of a syndicated bank loan which was signed in 2015 amounting to USD 300 million and maturing on 30 March 2018.
- On 31 March 2016 the IBERDROLA Group through its subsidiaries Iberdrola Renovables Asturias, S.A.U. and Ciener, S.A.U., has signed two bilateral loans totaling EUR 49.5 million maturing on 31 March 2019 and with the possibility of extension of 1 + 1 years.
- On 5 April 2016 the IBERDROLA Group has reorganized the credit facilities of Avangrid Inc., its subsidiary in the United States, to strengthen its liquidity position. A revolving credit facility of USD 1,500 million with a five years maturity and the possibility of a 1+1 year extension was signed, while three existing facilities have been cancelled. This transaction meant an increase in liquidity, longer expiration dates and has improved financing conditions.
- On 21 June 2016 the IBERDROLA Group, through its subsidiary Iberdrola Financiación, S.A.U., has extended the term of a bilateral loan of EUR 600 million which was signed on June 2015 and maturing in 2018, extending the maturity a year until 24 June 2019.
- On 29 June 2016, IBERDROLA has signed a syndicated credit facility amounting to EUR 500 million within a five year period with an option to extend its maturity by 1 + 1 years.
- On 11 July 2016 IBERDROLA renewed the financial lease on the IBERDROLA Group's corporate buildings in Madrid, signed in June 2003, for EUR 166 million. The outstanding lease balance of EUR 91.7 million was refinanced for a new term of 18.5 years, at a lower cost.
- On 4 August 2016 the IBERDROLA Group, through its subsidiary Pier II, where IBERDROLA holds a 51% stake, signed over a project finance loan to fund a 66 MW wind farm in Mexico which had been operational since 2015. Under this contract, on 19 September the company drew down MXN 560.5 million due on 15 August 2023, at a fixed rate, and MXN 560.5 million due on 15 August 2029, at a floating rate.
- On 20 December 2016 IBERDROLA extended the term of two bilateral loans in the amount of EUR 150 million by one year, until 16 December 2019.

Loans from the European Investment Bank (EIB):

- On 4 January 2016 the IBERDROLA Group through its subsidiary Iberdrola Distribución Eléctrica, S.A.U. has disposed of the direct loan signed in 2015 with the European Investment Bank (EIB), for an amount of EUR 325 million maturing on 4 January 2023.
- On 23 May 2016, the IBERDROLA Group, through its subsidiary Iberdrola Financiación, S.A.U., has signed and disposed of a new direct loan with the EIB amounting to EUR 200 million maturing in 2022. This loan program will fund R&D in the Networks, Deregulated and Renewables areas in Spain and the United Kingdom from 2015 to 2018 totalling approximately EUR 420 million.
- On 21 June 2016 the IBERDROLA Group, through its subsidiary, ELEKTRO in Brazil has notified a draw down of a tranche of EUR 50 million at 1 July maturing in 2027, corresponding to the EIB loan signed on December 2015 for a total amount of EUR 150 million.

The most significant financial transactions performed by the IBERDROLA Group during the year 2015 have been the following:

Capital markets issues:

- On 14 January 2015, the IBERDROLA Group issued bonds with a nominal amount of EUR 600 million and an annual coupon of 1.125%, maturing on 27 January 2023.
- On 7 September 2015 the IBERDROLA Group issued EUR 500 million in bonds that mature on 17 September 2023 and a coupon of 1.75%.

These two transactions were part of separate bond exchange operations that have enabled the Group to extend the duration of the debt and laminate the medium term maturity profile and continue to improve liquidity. Therefore, and in parallel with these issues, there have been various offers to repurchase outstanding bonds of the IBERDROLA Group companies for further exchange with the new standards. As a result, it has reduced debt maturities EUR 91.4 million in 2016, EUR 378.7 million in 2017 and EUR 557.5 million in 2018.

- On 6 November 2015 the IBERDROLA Group has structured a bond issue -referenced to the share price of Iberdrola, S.A.- amounting to EUR 500 million maturing in November 2022 and without coupon.

These bonds incorporate an option that may be exercised by their holders around the time when due, under which they would receive a cash payment when which it will be determined the evolution of the share price of IBERDROLA, with a reference price of EUR 8.7479 per share.

To address these potential cash payments, IBERDROLA has simultaneously contracted a put option payable in cash by the same amount issued to hedge the risk. The reference price of this option will also be EUR 8.7479 per share.

Banking Market:

- On 13 February 2015 the IBERDROLA Group arranged the renewal, of EUR 2,000 million revolving credit granted in November 2013, that mature in November 2018. The renewal increased the available credit to EUR 2,500 million, extended the due date to February 2020, and enhanced the applicable economic conditions.
- On 13 February 2015 the IBERDROLA Group arranged the renewal, of EUR 2,000 million revolving credit granted in April 2014, that mature in April 2019. The renewal increased the available credit to EUR 2,500 million, extended the due date to February 2020, and enhanced the applicable economic conditions.
- On 13 February 2015 the IBERDROLA Group cancelled in advance EUR 2,247 million revolving credit granted in June 2011 with a maturity in June 2017.
- On 23 March 2015 the IBERDROLA Group also signed a four-year EUR 900 million bank loan in Club Deal format, with a 1 + 1 year extension option.
- On 23 March 2015 the IBERDROLA Group canceled a loan in advance of EUR 753 million euros maturing on June 2017.
- On 31 March 2015 the IBERDROLA Group also signed a EUR 75 million bilateral loan maturing in March 2019, with a 1 + 1 year extension option.
- On 16 and 18 March 2015 ELEKTRO, a subsidiary of the IBERDROLA Group, signed two bank loans for BRL 300 million pursuant to the Law 4131, maturing in 2018.

- On 24 June 2015 the IBERDROLA Group restructured an existing bilateral EUR 600 million loan, extending the original due date from June 2016 to June 2018 and maintaining the option to extend it for a further year, with the other conditions unchanged.
- On 14 December 2015 IBERDROLA MEXICO signed a syndicated bank loan for USD 300 million maturing on 31 March 2018.

Loans of the European Investment Bank (EIB):

- On 27 May 2015, the IBERDROLA Group renegotiated several tranches of loans held with the European Investment Bank (EIB), which were guaranteed by several banks for a total of EUR 479 million. This restructuring has resulted in improving the cost, due date and structure of this debt as well as the cancelation of guarantees.
- On 27 May 2015, the IBERDROLA Group renegotiated three tranches of the loan held with the EIB in order to finance investments in networks in Scotland and Spain totaling GBP 150 million and EUR 86 million, respectively. This restructuring has resulted in amendments of due dates and has improved financial conditions.
- On 22 June 2015, the IBERDROLA Group renegotiated three loans held with the EIB, which were mediated by a bank, totaling EUR 350 million. This restructuring has entailed reconverting the EIB financing into another series of bilateral loans, keeping the original due dates and reducing the margins to levels that are more in line with current market conditions.
- On 25 June 2015 Iberdrola Distribución Eléctrica, S.A.U. signed up a new direct EUR 325 million loan with the EIB to finance the 2014/2015 investment programme to update the electricity network, telecontrol and automation of substations. This loan's maturity date is in January 2023.

Certain Group investment projects, mainly related to renewable energies, have been financed specifically through loans that include covenants such as the compliance with certain financial ratios or the obligation to pledge in benefit of creditors the shares of the project-companies (Note 45). The outstanding balance of such loans at 31 December 2016 and 2015 amounted to EUR 166 and EUR 658 million, respectively. In some of these loans, amounting to EUR 166 and EUR 226 million at December 2016 and 2015, respectively, the establishment of a reserved deposit for the fulfilment of the obligations under the loan agreements is required, being the default ratios and/or the security deposit not reaching the agreed amount, the reason to preclude the dividends in the year in which they had not been fulfilled.

With regards to the clauses relating to credit ratings, the IBERDROLA Group has agreed with the EIB financing operations at 31 December 2016 and 2015 amounting to EUR 1,349 and 1,531 million, respectively, which may require additional renegotiation in case of a credit rating decline, predictably equating its price to other transactions with the EIB, without that limit. Also, at 31 December 2016 and 2015, the IBERDROLA Group has arranged loans and credits amounting to EUR 1,381 and 900 million, respectively, whose cost would be revised as a result of the decline in its credit rating. However, in both cases, the increase in cost would not be significant.

Additionally, financial entities have facilitated IBERDROLA and its subsidiaries loans and other agreements with a maturity that can be affected by a change of control being; the most significant ones at 31 December 2016 were the following ones:

- There are loans subject to an anticipated maturity date or that may require additional guarantees if a change of corporate control takes place in a public offering. In total they account for EUR 2,073,438 thousand approximately, except in the case when the change of control cannot be prejudicial.

- Moreover, approximately BRL 865,610 thousand (equivalent to EUR 253,933 thousand) in issues and BRL 1,174,013 thousand (equivalent to EUR 344,404 thousand) in loans corresponding to ELEKTRO would be affected by a change of control in the issuer, except for in the case when it takes place as a consequence of reorganizations within the Group or is allowed by lenders.
- On the other hand, approximately EUR 12,250,607 thousand corresponding to shares issued in the Euromarket will be subject to an anticipated maturity date when a change of control takes place if the credit rating of IBERDROLA drops below the investment grade, or if it is already below it, it drops a notch, provided that the rating agency has downgraded the rating due to a change of control.
- Lastly, approximately EUR 678,259 thousand, USD 300,000 thousand (equivalent to EUR 288,434 thousand) corresponding to IBERDROLA MEXICO S.A., BRL 433,095 thousand (equivalent to EUR 127,051 thousand) corresponding to loans belonging to ELEKTRO and USD 1,150,000 thousand (equivalent to EUR 1,105,663 thousand) corresponding to issues by the IBERDROLA Group in the United States would be subject to an anticipated maturity if a change of control of the lender takes place.

At 31 December 2016 and 2015, the IBERDROLA Group had fulfilled all its obligations relating to its financial debt. Therefore, there are no amounts due prior to 31 December 2016.

At the date of authorization for issue of these Consolidated financial statements, neither IBERDROLA nor any of its material subsidiaries were in breach of its financial obligations or any kind of obligation that could lead to early redemption of their financial commitments.

The average cost of debt of the IBERDROLA Group in 2016 and 2015 was 3.17% and 3.57% respectively.

26. DERIVATIVE FINANCIAL INSTRUMENTS

The detail of the balances at 31 December 2016 and 2015 that includes the valuation of derivative financial instruments is as follows:

Thousands of euros	2016				2015			
	Assets		Liabilities		Assets		Liabilities	
	Short-term	Long-term	Short-term	Long-term	Short-term	Long-term	Short-term	Long-term
INTEREST RATE HEDGE:	31,449	181,928	40,545	(125,931)	26,966	202,063	21,998	(91,683)
Cash flow hedge	–	–	(10,638)	(117,934)	–	17,961	(27,716)	(80,073)
Interest rate swap	–	–	(10,609)	(117,934)	–	17,961	(27,267)	(79,956)
Collar	–	–	(29)	–	–	–	(449)	(117)
Fair value hedge	31,449	181,928	51,183	(7,997)	26,966	184,102	49,714	(11,610)
Interest rate swap	31,449	173,705	49,754	–	26,966	174,987	47,195	–
Others	–	8,223	1,429	(7,997)	–	9,115	2,519	(11,610)
FOREIGN EXCHANGE HEDGE:	318,110	554,748	(383,536)	(174,555)	212,670	624,814	(469,075)	(101,266)
Cash flow hedge	223,638	92,717	(51,167)	(49,130)	107,668	86,152	(160,499)	(44,419)
Currency swap	63,364	53,170	6,436	(44,525)	7,874	51,051	6,027	(34,182)
Foreign exchange hedge	160,274	39,547	(57,603)	(4,605)	99,794	35,101	(166,526)	(10,237)
Fair value hedge	30,152	462,031	29,809	(76,031)	71,666	538,662	30,781	(20,498)
Currency swap	30,152	460,988	29,792	(76,031)	71,666	533,740	30,758	(20,464)
Others	–	1,043	17	–	–	4,922	23	(34)
Hedge of a net investment in a foreign country:	64,320	–	(362,178)	(49,394)	33,336	–	(339,357)	(36,349)
Currency swap	(3,804)	–	(4,128)	(42,886)	(3,571)	–	(3,968)	(36,349)
Foreign exchange hedge	68,124	–	(341,075)	(6,508)	36,907	–	(335,389)	–
Collar	–	–	(16,975)	–	–	–	–	–
RAW MATERIAL HEDGE:	195,991	66,921	(236,756)	(38,082)	261,923	41,355	(305,497)	(38,914)
Cash flow hedge	195,991	66,921	(236,756)	(38,082)	261,923	41,355	(305,497)	(38,914)
Forward	195,991	61,095	(236,756)	(38,082)	261,923	41,355	(305,497)	(38,914)
Others	–	5,826	–	–	–	–	–	–
NON-HEDGING DERIVATIVES:	949,894	127,670	(914,321)	(101,347)	464,064	130,041	(431,673)	(137,457)
Derivatives on treasury shares	1	7,113	–	(7,113)	–	14,854	(74)	(14,854)
Equity swap	1	7,113	–	(7,113)	–	14,854	(74)	(14,854)
Derivatives on foreign exchange	22,429	188	(7,893)	(183)	21,700	1,391	(10,422)	(394)
Foreign exchange hedge	22,429	82	(7,893)	(66)	21,700	1,391	(10,422)	(394)
Exchange rate swap	–	106	–	(117)	–	–	–	–
Derivatives on raw materials	927,464	117,257	(904,175)	(86,960)	442,364	110,538	(417,436)	(112,513)
Forward	924,572	117,257	(900,825)	(86,960)	424,486	110,448	(400,085)	(101,389)
Others	2,892	–	(3,350)	–	17,878	90	(17,351)	(11,124)
Interest rate derivatives	–	3,112	(2,253)	(7,091)	–	3,258	(3,741)	(9,696)
Interest rate swap	–	2,097	(131)	6	–	2,024	762	–
Others	–	1,015	(2,122)	(7,097)	–	1,234	(4,503)	(9,696)
NETTED OPERATIONS (Note 15)	(801,579)	(22,085)	801,579	22,085	(365,593)	(37,781)	399,339	37,674
Total	693,865	909,182	(692,489)	(417,830)	600,030	960,492	(784,908)	(331,646)

The detail, by maturity, of the notional amounts of the derivative financial instruments arranged by the IBERDROLA Group outstanding at 31 December 2016 is as follows:

Thousands of euros	2017	2018	2019	2020	2021 and subsequent years	Total
INTEREST RATE HEDGE:	489,061	1,157,334	258,400	1,630,956	5,348,073	8,883,824
Cash flow hedge	57,061	7,334	7,556	65,956	3,422,073	3,559,980
Interest rate swap	7,061	7,334	7,556	65,956	3,422,073	3,509,980
Collar	50,000	–	–	–	–	50,000
Fair value hedge	432,000	1,150,000	250,844	1,565,000	1,926,000	5,323,844
Interest rate swap	432,000	1,150,000	194,794	1,565,000	1,878,000	5,219,794
Others	–	–	56,050	–	48,000	104,050
FOREIGN EXCHANGE HEDGE	11,635,832	11,634,932	1,296,582	262,060	1,714,479	26,543,885
Cash flow hedge	6,117,046	11,305,800	9,619	38,772	490,204	17,961,441
Currency swap	409,085	452,284	–	–	388,087	1,249,456
Foreign exchange hedge	5,707,961	10,853,516	9,619	38,772	102,117	16,711,985
Fair value hedge	–	195,473	1,286,963	223,288	1,224,275	2,929,999
Currency swap	–	195,473	1,283,363	223,288	1,224,275	2,926,399
Others	–	–	3,600	–	–	3,600
Hedge of a net investment in a foreign	5,518,786	133,659	–	–	–	5,652,445
Currency swap	–	93,040	–	–	–	93,040
Foreign exchange hedge	4,656,717	40,619	–	–	–	4,697,336
Collar	862,069	–	–	–	–	862,069
RAW MATERIAL HEDGE	2,048,392	488,987	115,635	2,032	12,469	2,667,515
Cash flow hedge	2,048,392	488,987	115,635	2,032	12,469	2,667,515
Forward	2,048,392	454,157	63,678	2,032	12,469	2,580,728
Others	–	34,830	51,957	–	–	86,787
NON-HEDGING DERIVATIVES	7,475,510	1,767,246	287,601	30,127	1,258,755	10,819,239
Derivatives on treasury shares	30	–	–	–	1,000,000	1,000,030
Derivatives on treasury shares	30	–	–	–	1,000,000	1,000,030
Derivatives on foreign exchange	415,194	35,795	–	–	–	450,989
Foreign exchange hedge	415,194	16,900	–	–	–	432,094
Currency swap	–	18,895	–	–	–	18,895
Derivatives on raw materials	7,060,286	1,701,451	237,601	30,127	183,755	9,213,220
Forward	7,060,245	1,701,451	237,601	30,127	183,755	9,213,179
Others	41	–	–	–	–	41
Interest rate derivatives	–	30,000	50,000	–	75,000	155,000
Interest rate swap	–	–	50,000	–	–	50,000
Others	–	30,000	–	–	75,000	105,000
Total	21,648,795	15,048,499	1,958,218	1,925,175	8,333,776	48,914,463

The information presented in the table above includes gross notional amounts of derivative financial instruments arranged in absolute terms (without offsetting asset and liability or purchase and sale positions) and, therefore, do not constitute the risk assumed by the IBERDROLA Group since this amount only records the basis on which the calculations are made to settle the derivative.

The heading "Finance cost" in the 2016 and 2015 Consolidated income statements includes EUR 105,759 thousand and EUR 98,095 thousand, respectively, in connection with derivatives linked to financial indexes that fail to meet the conditions to qualify as hedging instruments or, having met the conditions, but as explained in Notes 4.I and 41 are partially ineffective. The "Finance income" heading in the Consolidated income statements for the same years also includes EUR 168,332 thousand and EUR 62,771 thousand, respectively, for the abovementioned items (Note 40).

The detail of the nominal value of the main liabilities on which foreign exchange hedges (Note 5) have been arranged is as follows:

2016						
Type of hedge	Thousands of US dollars	Thousands of Japanese yens	Thousands of Norwegian crowns	Thousands of Mexican pesos	Thousands of Swiss francs	Thousands of Sterling pounds
Cash Flow	705,000	–	450,000	1,500,000	250,000	–
Fair Value	2,283,266	28,000,000	–	–	–	700,000

2015						
Type of hedge	Thousands of US dollars	Thousands of Japanese yens	Thousands of Norwegian crowns	Thousands of Mexican pesos	Thousands of Swiss francs	Thousands of Sterling pounds
Cash Flow	247,000	–	450,000	1,500,000	250,000	–
Fair Value	2,407,196	28,000,000	350,000	–	27,000	700,000

The nominal value of the most significant liabilities for which interest rate swaps (Note 5) have been arranged is as follows:

2016			
Type of hedge	Thousands of euros	Thousands of US dollars	Thousands of Sterling pounds
Cash Flow	145,672	–	225,000
Fair Value	5,323,844	–	–

2015			
Type of hedge	Thousands of euros	Thousands of US dollars	Thousands of Sterling pounds
Cash Flow	152,473	473,500	225,000
Fair Value	5,789,784	–	–

27. OTHER NON-CURRENT PAYABLES AND OTHER NON-CURRENT LIABILITIES

The breakdown of "Other non-current payables" heading in the liability side of the Consolidated statements of financial position at 31 December 2016 and at 31 December 2015 is as follows:

Thousands of euros	12.31.16	12.31.15
Long-term guarantees and deposits received (Note 13.c)	134,781	128,658
Tariff sufficiency concessional guarantee in Brazil (Note 11)	68,933	62,582
Debts with companies consolidated by using the equity method	32,735	9,946
Others	500,820	488,508
Total	737,269	689,694

The breakdown of "Other current liabilities" of the Consolidated statements of financial position at 31 December 2016 and 2015 is as follows:

Thousands of euros	12.31.16	12.31.15
Short-term guarantees and deposits received (Note 13.c)	135,340	177,167
Tariff sufficiency concessional guarantee in Brazil (Note 11)	97,475	64,399
Debts with companies consolidated by using the equity method	224,255	228,757
Short term Property, Plant and Equipment suppliers	637,951	496,601
Employee benefits payable	210,577	178,899
Others	486,178	608,483
Total	1,791,776	1,754,306

28. DEFERRED TAXES AND INCOME TAX EXPENSE

As in 2015, in 2016 IBERDROLA as the parent company of the Group 2/86, filed a consolidated annual tax return in Spain. The Group will continue to be taxed under this tax regime indefinitely for as long as the related requirements are met and the Group does not expressly waive application of the regime by filing the related taxpayer registration form.

Without prejudice to this special tax regime in Spain applicable to IBERDROLA and certain of its consolidated Spanish subsidiaries, other Spanish and foreign subsidiaries file individual or aggregated Income Tax returns, in accordance with the legislation applicable to them.

The difference between the tax charge allocated to 2016 and 2015 and the tax payable for those years, recorded under "Deferred tax assets" and "Deferred tax liabilities", as appropriate, in the Consolidated statements of financial position at 31 December 2016 and 2015, arose as a result of the temporary differences relating to the difference between the carrying amount of certain assets and liabilities and their tax bases. The main temporary differences are the following:

- Temporary differences generated from the measurement of available-for-sale investments, derivatives and assets that have been measured at their fair value in business combinations for which the difference between the tax base and the carrying amount is not deductible for tax purposes.
- Temporary differences arising from the application of profits from the free amortisation or accelerated amortisation compared to that recognised in the accounts.

- Temporary differences arising from the non-deductibility for tax purposes of certain liabilities, including those recognised in relation to pension liabilities and to collective redundancy procedure (Notes 4.o, 4.p and 23).
- Temporary differences arising from the tax treatment of financial goodwill generated from the acquisition of equity stakes in non-resident entities.

The detail of current and deferred Income Tax expense is as follows:

Thousands of euros	12.31.16	12.31.15
Current taxes	603,501	319,384
Deferred taxes	301,118	207,708
(Income) / expense	904,619	527,092

The detail of the headings “Deferred tax assets” and “Deferred tax liabilities” in the Consolidated statements of financial position therein is as follows:

	Balance at 01.01.15	Consolidation perimeter modification (Note 42)	Translation differences	Credit (Debit) to Consolidated income statement	Credit (Debit) to asset and liability revaluation reserve	Credit (Debit) to "Other reserves"	Balance at 12.31.15	Consolidation perimeter modification (Note 42)	Translation differences	Credit (Debit) to Consolidated income statement	Credit (Debit) to asset and liability revaluation reserve	Credit (Debit) to "Other reserves"	Balance at 12.31.16
Thousands of euros													
Deferred tax assets:													
Derivative financial instruments valuation	607,813	–	16,087	7,859	(47,338)	–	584,421	–	(4,993)	(28,634)	(4,147)	–	546,647
Balance sheet revaluation 16/2012	1,847,520	–	–	(135,043)	–	–	1,712,477	–	–	(152,273)	–	–	1,560,204
Pension and similar commitments	594,261	111,612	48,209	(35,971)	–	(31,375)	686,736	–	12,123	33,101	–	15,420	747,380
Allocation of non-deductible negative goodwill arising on consolidation	70,630	–	–	(1,893)	–	–	68,737	–	–	(1,856)	–	–	66,881
Provision for facility closure costs	51,921	–	870	3,273	–	–	56,064	–	356	437	–	–	56,857
Tax loss and tax credit deduction	1,703,966	54,309	157,604	125,442	–	–	2,041,321	–	97,944	360,133	–	–	2,499,398
Other deferred tax assets	1,007,889	127,765	299,724	44,374	–	–	1,479,752	446	19,600	(19,011)	–	–	1,480,787
Total	5,884,000	293,686	522,494	8,041	(47,338)	(31,375)	6,629,508	446	125,030	191,897	(4,147)	15,420	6,958,154

Thousands of euros	Balance at 01.01.15	Consolidation perimeter modification (Note 42)	Translation differences	Credit (Debit) to Consolidated income statement	Credit (Debit) to asset and liability revaluation reserve	Balance at 12.31.15	Consolidation perimeter modification (Note 42)	Translation differences	Credit (Debit) to Consolidated income statement	Credit (Debit) to asset and liability revaluation reserve	Balance at 12.31.16
Deferred tax liabilities:											
Available-for-sale assets valuation	8	–	–	(8)	–	–	–	–	–	–	–
Valuation of financial instrument derivatives	547,024	–	16,884	(4,283)	(15,813)	543,812	–	(16,087)	16,887	10,937	555,549
Accelerated amortisation	4,892,793	570,183	480,742	73,233	–	6,016,951	–	183,652	528,145	–	6,728,748
Overprice assigned in business combinations	3,409,713	969,986	267,599	(86,642)	–	4,560,656	76,894	84,761	107,233	–	4,829,544
Other deferred tax liabilities	516,679	–	24,930	233,449	–	775,058	–	11,012	(159,250)	–	626,820
Total	9,366,217	1,540,169	790,155	215,749	(15,813)	11,986,477	76,894	263,338	493,015	10,937	12,740,661

At 31 December 2016 and 2015, there were no significant unrecognised deferred tax assets or other significant tax credits at the IBERDROLA Group companies.

Moreover, based on the information available at the year end, including the historic levels of profits and the IBERDROLA Group's results projections for the coming years, it is considered that sufficient positive taxable bases will be generated to allow the recovery of the deferred tax assets booked at 31 December 2016.

In addition, the headings "Other reserves" and "In unrealised asset and liability revaluation reserves" in 2016 and 2015 Consolidated statements of financial position includes credits and debits of EUR 2,412 thousand and EUR 63,708 thousand, respectively, relating to the tax charge on actuarial deviations and on cash flow hedge valuation adjustments and available-for-sale investments.

Income Tax expense breakdown for 2016 and 2015 is calculated as follows:

Thousands of euros	12.31.2016	12.31.2015
Consolidated profit before tax	3,747,461	2,986,621
Non-deductible expenses and non-computable income:		
- from individual companies	(46,208)	(82,768)
- from consolidation adjustments	1,662	(2,391)
Net result of companies accounted for using the equity method	(48,723)	(55,318)
Adjusted result	3,654,192	2,846,144
Gross tax calculated at the tax rate in force in each country (a)	1,030,738	815,730
Tax credits deductions due to reinvestment of extraordinary profits and other tax credits	(41,172)	(42,224)
Adjustment of prior years Income Tax expense (b)	(74,901)	9,791
Net movement in provisions for litigation, indemnity payments, similar costs and other provisions (c)	11,551	(123,852)
Adjustments of deferred tax assets and liabilities (d)	(82,682)	(216,319)
Taxes related to non-distributed earnings	56,264	84,808
Others	4,821	(842)
Income Tax expense / (income)	904,619	527,092

- (a) The different foreign companies of the IBERDROLA Group calculate the Income Tax expense and the resulting quotas related to the taxes applicable in accordance with the legislation and on the basis of the tax rates in force in each country. Also, the subsidiaries subject to the Basque Country tax legislation apply the tax rate in force in each historical territory.
- (b) The main amount (EUR 54,795 thousand) corresponds to the obligation of the income and expense temporal imputation criteria, derived from the Supreme Courts' jurisprudence, related to the returns, in execution of sentence, of amounts related to taxes and other concepts.
- (c) The amount registered in 2015 is mainly due to the reassessment made by Iberdrola Group, of the necessary provision to cover the potential risk derived from several issues after the favourable Court sentences received in the period.
- (d) The revenue recorded for this concept in 2016 mainly reflects the effect arising from the recalculation of prepaid and deferred taxes of UK's Group companies due to rate reduction from 18% to 17% (EUR 96,894 thousand) and the negative effect from the application in Spain of the Royal Decree-law 3/2016, of 2 December, by which deferred tax assets have been regularized amounting to EUR 29,843 thousand. Likewise, during 2016 deferred tax assets amounting to EUR 38.083 thousand have been registered when its recovery has been confirmed.

In general terms, the companies of the Group in Spain keep 2013 and subsequent fiscal years open to fiscal inspection in relation to the principal taxes in which they are subject to with the exception to the Income Tax which is open for 2012 and subsequent fiscal years. Nevertheless, the aforementioned period may vary for those entities of the Group subject to other tax legislations.

On 11 March 2014, the State Tax Administration Agency initiated a general tax audit of the taxes of Fiscal Group 2/86. The years and taxes that are being inspected are the Income Tax for the years 2008 to 2011; the Value Added Tax of the years 2010 and 2011; withholdings on personal income taxes from May 2009 to December 2011 and non-resident withholdings for years 2010 and 2011.

On December of 2015, inspection minutes have been issued regarding Income tax for the 2008 to 2011 year-ends (specific to transfer pricing), and in accordance (with zero quota) with respect to withholding tax on Personal Income Tax, as well as withholding tax on investment income and on account of the imposition of non-residents.

Agreement and disagreement minutes were signed in the first half of 2016 in connection with Corporate Income Tax for the years 2008 to 2011 and in connection with Value-Added Tax for the years 2010 and 2011, and the settlement agreements confirming the disagreement minutes were received.

The major adjustments in the agreement minutes concern the inclusion of IBERDROLA DISTRIBUCIÓN in Tax Group 2/86 for Corporate Income Tax in respect of the years 2008 and 2009 following the Supreme Court Rulings of November 2014.

The main adjustments in the settlement agreements arising from the disagreement minutes signed in the first half of 2016 are as follows:

- Measurement of the financial goodwill liable for fiscal amortisation due to the acquisition of SCOTTISH POWER.
- Elimination of the dividend exemption of SCOTTISH POWER, as the inspectors understood this is incompatible with an adjustment in the value of the portfolio due to coverage of a net investment.
- Discrepancies in tax consolidation criteria.

Additionally, in July 2016 the Consultative Commission observed the circumstances established in Article 15.1 of Spain's General Tax Law in a debtor-swap operation in a number of bond issues, which will give rise to new disagreement minutes for the years 2009, 2010 and 2011.

Minutes with agreements and conformity minutes were paid during the first six months of 2016, and did not have any material effects in the Consolidated income statement, as provision had already been made for the liabilities in the financial statements of previous years.

With respect to the minutes of disagreement, and its settlement agreements, the IBERDROLA Group considers that its actions concerning these issues are in accordance with reasonable interpretations of the regulations applicable, and has thus submitted economic-administrative claims in due time and format to the Central Economic Administrative Court, pending notifications of the deadline to make claims. The execution of the aforementioned settlements have been suspended through the furnishing of the necessary bank guarantees.

Finally, in January 2017, the Inspection Technical Office has declared the admissibility of the proposed sanctions by the inspection in the related disciplinary proceedings opened in September 2016 in relation to the discrepancies of the financial goodwill of SCOTTISH POWER, understanding that the company had acted based on a reasonable interpretation of the rule. There are not other disciplinary proceedings open for inspection in relation to this general inspection.

The IBERDROLA Group's directors and, where appropriate, their tax consultants consider that the current inspection process will not give rise to additional liabilities of significance derived from the settlement agreements of the disagreement minutes with respect to those already recorded at 31 December 2016 and 2015.

In addition to the abovementioned actions, other inspections have taken place at different times, both from the same tax authorities and from other tax authorities, which have resulted in the initiation of inspection minutes to several Group companies, some of which have been signed in disagreement and are appealed. The directors of the IBERDROLA Group and its tax advisors estimate that the amounts resulting from such actions or resources will not produce additional liabilities of consideration with respect to those already recorded.

29. TAX RECEIVABLES AND PAYABLES

The breakdown of the headings "Income tax receivables/payables" and "Other tax receivables/payables" on the asset and liability sides, respectively, in the Consolidated statements of financial position at 31 December 2016 and 2015 is as follows:

Thousands of euros	12.31.16	12.31.15
Tax receivables		
Income Tax receivable	503,403	411,322
VAT receivable	79,505	60,991
Tax withholdings and prepayments	44,046	80,935
Other tax receivable	19,828	124,714
Total	646,782	677,962
Tax payables		
Income tax payable	237,123	250,361
VAT payable	103,463	129,263
Tax withholdings and prepayments	54,145	58,379
Other tax payable	736,408	791,057
Social Security tax payable	20,477	22,013
Total	1,151,616	1,251,073

30. TRADE PAYABLES

The breakdown of this heading in the Consolidated statements of financial position at 31 December 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Suppliers	3,284,406	3,680,479
Suppliers of services provided	1,799,671	1,447,580
Trade payables	223,011	237,470
Customer advances	183,546	211,619
Total	5,490,634	5,577,148

The majority of these accounts payable do not accrue interest.

31. INFORMATION ON DEFERRED PAYMENTS TO SUPPLIERS. THIRD ADDITIONAL PROVISION. "DUTY OF INFORMATION" OF LAW 15/2010, OF 5 JULY

The breakdown of the required information for the year 2016 y 2015 is as follows:

	Number of days	
	2016	2015
Average payment period to suppliers	19	17
Paid transactions ratio	19	17
Outstanding payment transactions ratio	24	31

Thousands of euros	2016	2015
Total payments made	11,886,390	13,581,910
Total outstanding payments	313,897	189,151

The information in the table above has been prepared in accordance with the Law 15/2010 of 5 July, amending Law 3/2004 of 29 December, establishing measures to combat late payments in commercial operations and in accordance with the Resolution of 29 January 2016, from the *Instituto de Contabilidad y Auditoría de Cuentas*, on the information to be included in the notes to the financial statements in relation to deferred payments to suppliers in commercial operations. The specifications with which such information has been prepared are the following:

- Ratio of paid operations: amount in days of the ratio between the sum of the amount of each of the operations paid and the number of paydays, and in the denominator, the total amount of payments made during the year.
- Ratio of outstanding payment operations: amount in days of the ratio between the sum of the amount of the outstanding payment transaction and the number of unpaid days, and in the denominator, the total amount of outstanding payments.
- Suppliers: trade payables generated from debts of goods or services with suppliers included in the current liabilities heading of Consolidated statements of financial position.
- Property, plant and equipment and other financial lease suppliers are not considered in the information scope.
- Taxes, levies, indemnifications and some other headings are not considered in the information scope since they are not commercial transactions.
- The table shows information corresponding to Spanish companies included in the consolidated group once the credits and debits between the subsidiary companies are eliminated.

32. NET REVENUE

The detail of this heading in the Consolidated income statements for 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015 (Restated Note 2.c)
Deregulated business	18,723,372	21,617,102
Spain and Portugal	11,880,533	12,779,109
United Kingdom	5,468,329	7,561,795
America	1,614,685	1,590,303
Write off	(240,175)	(314,105)
Renewable business	2,399,633	2,790,566
Spain	777,243	764,541
United Kingdom	423,614	797,792
United States	963,971	1,008,310
Rest of the world	234,805	219,923
Network business	8,806,734	7,908,986
Spain	2,049,676	1,965,023
United Kingdom	1,319,093	1,533,604
United States	3,979,421	2,674,955
Brazil	1,458,544	1,735,404
Other business	753,608	870,293
Corporation and adjustments	(1,467,965)	(1,768,254)
Total	29,215,382	31,418,693

33. CONSTRUCTION CONTRACTS

The accumulated amounts relating to uncompleted contracts at 31 December 2016 and 2015 are as follows:

Thousands of euros	Accumulated revenue recognised by reference to percentage of completion since the beginning of the contract	Amount billed to clients since the beginning of the contract	Work in progress at 31 December	Advances received from clients at 31 December
2016	5,747,300	5,537,079	293,789	83,568
2015	5,294,328	5,242,497	187,403	135,572

The amount registered in the Consolidated income statements during the years 2016 and 2015 for these contracts amounts to EUR 500,168 thousand and EUR 616,523 thousand, respectively.

34. PROCUREMENTS

The detail of this heading in the Consolidated income statements for 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015 (Restated Note 2.c)
Deregulated business	14,089,368	16,773,518
Spain and Portugal	8,809,080	9,807,741
United Kingdom	4,468,779	6,255,393
America	1,051,661	1,024,476
Write off	(240,152)	(314,092)
Renewable business	220,132	429,720
Spain	13,552	13,749
United Kingdom	38,466	225,889
United States	161,636	185,738
Rest of the world	6,478	4,344
Network business	2,646,188	2,397,210
Spain	21,496	13,345
United Kingdom	52,240	61,744
United States	1,442,312	976,541
Brazil	1,130,140	1,345,580
Other businesses	647,272	635,279
Corporation and adjustments	(1,303,800)	(1,659,709)
Total	16,299,160	18,576,018

35. STAFF COSTS

The detail of this heading in the Consolidated income statements for 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Wages and salaries	1,850,773	1,779,783
Employer Social Security costs	253,741	252,244
Additional provisions for pensions and similar obligations and defined contributions to the external pension plan (Notes 4.o and 23)	240,269	267,112
By-law stipulated directors' emoluments art. 48.1 (Note 46)	17,000	17,000
By-law stipulated directors' emoluments art. 48.4	3,761	5,050
Other employee welfare expenses	151,757	109,038
	2,517,301	2,430,227
Capitalised staff costs:		
- Intangible assets (Note 8)	(31,073)	(28,939)
- Property, plant and equipment (Note 4.d)	(600,795)	(468,194)
- Nuclear fuel (Note 16)	(958)	-
	(632,826)	(497,133)
Total	1,884,475	1,933,094

In 2016 and 2015 the IBERDROLA Group's average workforce totalled 28,389 and 27,169 employees, of which 6,721 and 6,257 were female workers, respectively.

The average number of employees in the consolidated group corresponds to all the employees in those consolidated companies that have been integrated using the global integration method, as well as the employees of the joint ventures determined based on the participation share in those ones.

36. OPERATING LEASES

The heading "External services" in the Consolidated income statements for 2016 and 2015 included EUR 152,036 thousand and EUR 112,710 thousand, respectively, relating to operating leases. The detail of the total future minimum lease payments under non-cancellable operating leases at 31 December 2016 is as follows:

Thousands of euros	
2017	105,033
2018	92,853
2019	81,380
2020	76,289
2021	73,418
From 2022 onwards	897,052
Total	1,326,025

The leasing contracts for most of the lands on which the IBERDROLA Group's wind power facilities are located have renewal on expiry or early termination clauses. The payments detailed in the table above relate to the period of remaining useful life of the facilities, as well as the expenditure which the termination of the contract at the end of its term would entail.

On the other hand, the IBERDROLA Group acts as lessor in certain operating leases consisting basically on the rental of investment property (Note 9) and the lease of fibre optics.

The heading "Net revenue" in the Consolidated income statements in 2016 and 2015, includes EUR 60,782 thousand and EUR 55,580 thousand, respectively, related to this concept and the detail of the estimated future minimum proceeds under non-cancellable leases at 31 December 2016 is as follows:

Thousands of euros	
2017	54,097
2018	39,026
2019	38,001
2020	36,957
2021	35,429
From 2022 onwards	47,958
Total	251,468

37. TAXES OTHER THAN INCOME TAX

The breakdown of this heading in the Consolidated income statement of 2016 and 2015 is as follows:

Thousands of Euros	12.31.2016	12.31.2015 (Restated Note 2.c)
Deregulated Business	876,124	955,282
Spain	756,767	780,622
United Kingdom	114,321	170,239
United States and Canada	2,905	3,079
Brazil	8	4
Mexico	2,123	1,338
Renewable Business	142,342	153,727
Spain	79,581	92,872
United Kingdom	18,091	18,496
United States	40,075	38,314
Other	4,595	4,045
Network Business	638,025	498,904
Spain	86,877	97,548
United Kingdom	103,170	112,577
United States	446,619	288,124
Brazil	1,359	655
Other businesses	1,768	3,824
Corporation and adjustments	(121,529)	94,726
Total	1,536,730	1,706,463

In addition, Law 15/2012 was published on 28 December 2012, regarding tax measures to ensure sustainability of the energy sector. The law introduced the following tax figures registered under "Taxes other than income tax" of the Consolidated income statements of 2016 and 2015:

- A tax on the value of electricity output, entailing payment of 7% of the total amount to be received by the taxpayer for the production of electricity and incorporation thereof in the Spanish electricity system, measured at power station busbars, during the tax period. This tax gave rise to an expense of EUR 213,582 thousand and EUR 224,548 thousand in 2016 and 2015 respectively.
- A tax on spent nuclear fuel, amounting to EUR 134,131 thousand and EUR 117,792 thousand in 2016 and 2015, respectively.
- A royalty on the use of inland water affecting production of electricity that is levied on the economic value of hydroelectric power produced, with a rate of 22%. The corresponding expense in 2016 and 2015, amounting to EUR 132,162 thousand and EUR 110,228 thousand, respectively.
- A green cent tax levied against energy products used in electricity production, entailing a cost for the IBERDROLA Group of EUR 45,492 thousand and EUR 51,758 in 2016 and 2015, respectively. This payment was recognised under "Procurements" in the Consolidated income statement.

38. AMORTISATION AND PROVISIONS

The detail of this heading in the Consolidated income statements for 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015 Restated (Note 2.a)
Tangible assets depreciation allowances:		
- Property, plant and equipment (Note 10)	2,636,418	2,750,480
- Investment property (Note 9)	7,446	7,516
Intangible asset depreciation allowances (Note 8)	444,028	335,439
Allowances for impairments and write-offs of non-financial assets (Note 12)	(38,937)	279,425
Changes in provisions	204,751	195,248
Total	3,253,706	3,568,108

39. GAINS AND LOSSES ON DISPOSAL OF NON-CURRENT ASSETS

The detail of "Gains on disposal of non-current assets" in the Consolidated income statements for 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Gain on the disposal of land, property, plant and equipment	6,482	16,996
Gain on the disposal of equity investments	46,550	114,849
Total	53,032	131,845

The breakdown of "Losses on disposal of non-current assets" in the Consolidated income statements for the year 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Loss on the disposal of land, property, plant and equipment	3,430	1,267
Loss on the disposal of equity investments	1,456	5,508
Total	4,886	6,775

2016

In the first half of 2016, the IBERDROLA Group sold its share in the Iroquois Gas Transmission System, L.P. (Minority interest in a local gas network) in the United States amounting to EUR 48,599 thousand, which resulted in a gross capital gain of EUR 28,738 thousand, which was recorded under the "Gains on disposal of non-current assets" heading in the Consolidated income statement for 2016.

During 2015, the IBERDROLA Group received offers from several buyers interested in acquiring 50% of the stake in Oceanic Center, S.L. As of 31 December 2015, this interest was classified under the heading "Assets held for sale" of the Consolidated Statement of Financial Position since its carrying amount was deemed to be recoverable through its sale. On 1 June 2016, the IBERDROLA Group sold 50% of its stake in Oceanic Center, S.L. amounting to EUR 61,500 thousand, resulting in a gross capital gain of EUR 17,000 thousand recorded under the "Gains on disposal of non-current assets" heading in the Consolidated income statement of 2016.

2015

- On 27 February 2015, Iberdrola Energía, S.A.U. transferred to NEOENERGIA its entire stake in distributors COELBA and COSERN. The selling price of COELBA shares, accounting for 8.50% of share capital, amounts to BRL 532,101 thousand (the equivalent of EUR 163,714 thousand). The selling price of COSERN shares, accounting for 7.01% of share capital, amounts to BRL 107,048 thousand (the equivalent of EUR 32,936 thousand).

Receipt of the total price of COELBA and COSERN shares will be deferred until 26 February 2018, when Iberdrola Energía, S.A.U. will also receive the sum of interest calculated at an annual rate of 12.19% (Note 14).

The operation has led to a gross gain of EUR 74,024 thousand, recognised under "Gains on disposal of non-current assets" on the Consolidated income statement for the fiscal year 2015.

- On the other hand, on 16 November 2015, the IBERDROLA Group signed a transactional contract with the Bolivian Government which recognizes the payment of compensation to the Group because of the nationalization of the entire shareholding in the companies in which it owned the amount of EUR 31,862 thousand, these amounts are presented under the "Gains on disposal of non-currents assets" heading in the Consolidated income statement in 2015.

40. FINANCE INCOME

The breakdown of "Finance income" in the Consolidated income statements for 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Income from equity investments	4,063	4,363
Other interest and finance income	131,374	205,647
Disposal of the Euskaltel, S.A. investment (Note 13.b)	–	15,578
Other interest and finance income due to credits to associated companies	27,474	28,231
Derivatives not designated as hedging instruments and inefficiencies (Note 26)	168,332	62,771
Exchange gains in foreign currency for financing activities	494,014	53,125
Other positive exchange gains in foreign currency	123,124	116,283
Capitalised finance costs		
- Intangible asset (Note 8)	15,500	13,034
- Property, plant and equipment (Note 10)	93,770	81,749
- Nuclear fuel (Note 16)	2,465	4,204
- Investment properties (Note 17)	65	32
Total	1,060,181	585,017

41. FINANCE COST

The breakdown of "Finance cost" in the Consolidated income statements for 2016 and 2015 is as follows:

Thousands of euros	12.31.2016	12.31.2015
Finance and similar financing costs	1,027,798	1,090,097
Other finance and similar costs	102,355	95,380
Equity instruments having the substance of a financial liability (Note 21)	8,821	22,304
Derivatives not designated as hedging instruments and inefficiencies (Note 26)	105,759	98,095
Exchange losses in foreign currency for financing activities	486,295	62,068
Other negative exchange losses	134,343	134,676
Financial effect of other provisions (Note 24)	30,403	49,331
Financial effect of the provisions for pensions and similar obligations (Note 23)	67,851	56,120
Total	1,963,625	1,608,071

42. BUSINESS COMBINATIONS

2016

The IBERDROLA Group did not enter into any business combination considered material in 2016.

2015

On 25 February 2015, the Boards of Directors of IBERDROLA, Iberdrola USA Inc. and UIL Holdings Corporation (UIL) approved the terms for integrating UIL in the IBERDROLA Group through its absorption by Green Merger Sub. Inc. (hereinafter, GREEN MERGER SUB), a company fully owned by Iberdrola USA, Inc., a company that, as a result of this operation has been renamed as Avangrid, Inc. (AVANGRID).

UIL was an American company whose shares came to trade on the New York Stock Exchange (hereinafter, NYSE) and the headquarters of a group of companies engaged mainly in regulated business of transmission and distribution of electricity and gas in the states of Connecticut and Massachusetts.

This agreement contains the usual terms for this type of transaction and its realization was subject to the following conditions precedent:

- The approval of the transaction by the shareholders of UIL holding the majority of its share capital.
- Obtaining the necessary regulatory approvals in the United States at the state and federal level.
- The listing of the shares of AVANGRID on the NYSE.

These conditions were met on 16 December 2015. On 17 December 2015, AVANGRID's shares begun trading on the NYSE.

The transaction was structured by merging GREEN MERGER SUB (acquiring company) and UIL (the acquired company). Following the merge, the shares of UIL have been canceled and their holders have received as consideration, an action of AVANGRID and USD 10.50 in cash per share (representing a total cash of USD 595 million).

As a result of the transaction, the share capital of AVANGRID is 81.5% owned by IBERDROLA, while the former shareholders of UIL received 18.5%.

This business combination was registered in the 2015 Consolidated financial statements on a provisional basis, since at the date of preparation of the Consolidated financial statements the valuation of the assets acquired and liabilities had not yet been completed and the twelve-month period since the acquisition of UIL has not yet ended established by IFRS 3 "Business Combinations". In this sense, the allocation of the price paid by UIL at the fair value of its assets, liabilities and contingent liabilities has been completed in 2016.

The effect that the correction of the comparative information included in the Consolidated financial statement of 2015 would have had as a consequence of such definitive allocation would not have been significant in relation to them.

Facing the accounting for this business combination, the IBERDROLA Group has opted to measure minority interests in AVANGRID by the proportional share of the fair value of identifiable assets and liabilities.

The fair value of the assets and liabilities of UIL at 16 December 2015 and its book value at that date is as follows:

Thousands of euros	Fair Value at 16 December 2015	Carrying amount at 16 December 2015
Intangible Assets	2,996,548	366,592
Property, plant and equipment	2,801,283	2,806,187
Non-current financial assets	169,899	149,558
Deferred tax assets	294,132	293,719
Current trade and other non-current receivables	1,350	1,350
Inventories	60,788	60,788
Current trade and other current receivables	239,549	239,549
Current financial investments	11,012	11,012
Cash and cash equivalents	43,217	43,217
	6,617,778	3,971,972

Thousands of euros	Fair Value at 16 December 2015	Carrying amount at 16 December 2015
Non-current provisions	524,702	490,344
Non-current bank borrowings	1,784,637	1,615,945
Other non-current payables	12,336	12,336
Deferred tax liabilities	1,617,063	573,822
Current bank borrowings	199,683	199,683
Current trade and other current payables	311,134	311,134
	4,449,555	3,203,264
Net assets	2,168,223	768,708
Goodwill generated in the acquisition (Note 8)	447,352	
Total cost of acquisition	2,615,575	

Taking into account that UIL stock was being negotiated with liquidity in the NYSE while the Iberdrola USA Inc. stock was not listed, the IBERDROLA Group has calculated the cost of the business combination using the UIL quote at the date of acquisition. This cost, amounting to EUR 2,615,575 thousand, breaks down as follows:

Thousands of euros	
Cash	541,389
AVANGRID Shares	2,074,186
Total	2,615,575

The costs incurred in the acquisition amounted to EUR 33,459 thousand, which were recorded under the heading "External services" in the Consolidated income statement for 2015.

As a result of this transaction, the heading "Equity- Of non-controlling interests" in the Consolidated statement of financial position includes 18.5% of the net assets of AVANGRID that has been delivered to the shareholders of UIL on 16 December 2015 amounting to EUR 3,022,264 thousand. The difference between the sum of this amount and the EUR 541,389 thousand paid in cash to shareholders of UIL and the fair value of the net assets of UIL on 16 December 2015, difference that comes up to EUR 948,079 thousand, has been registered under the heading "Other reserves", "In unrealised asset and liability revaluation reserves" and "Translation differences" in the Consolidated statement of financial position.

The calculation of the cash outflow arising from the acquisition of UIL is as follows:

Thousands of euros	
Cash and cash equivalents of UIL at 16 December 2015	(43,217)
Cash paid by AVANGRID	541,389
Other expenses incurred for the acquisition	33,459
	531,631

UIL's contribution to consolidated net income for the IBERDROLA Group since 16 December 2015, amounted to a loss of EUR 19,727 thousand approximately. If the acquisition would have taken place on 1 January 2015, the increase in net consolidated revenues and consolidated net income for the year 2015 would have amounted to EUR 1,401,068 thousand and EUR 116,990 thousand, respectively.

The goodwill resulting from this business combination, which comes up to EUR 447,352 thousand, consists mainly of future economic benefits from the activity of UIL that do not meet the conditions established for accounting recognition at the time of the business combination.

43. CONTINGENT ASSETS AND LIABILITIES

The IBERDROLA Group companies are part of some legal and out-of-court disputes arising as part of their ordinary course of business (ranging from conflicts with suppliers, clients, administrative or tax authorities, individuals, environmental activists and employees).

The IBERDROLA Group's legal advisors believe that these proceedings will not have a material impact on its financial and equity position.

The most important proceedings in which IBERDROLA or its subsidiaries in Spain are involved at the date of authorization for issue of these Consolidated financial statements are described below:

Contingent liabilities

- a) Ordinary Proceeding 62/2016 in Madrid Court of First Instance No 77, where Iberdrola applied for a declaration in its favour of ownership of lot number 1 of the Madrid City Council Expropriation Procedure, located at Calle Gallur, Carabanchel district. Iberdrola has applied for a declaration that it is the owner of the land, as against parties now disputing that ownership, on the basis of Iberdrola's title to the property. The benefit of securing this declaration would be that Iberdrola would then receive the fair value of the land as appraised in the course of the compulsory expropriation procedure; that amount has so far been paid into court until the dispute as to ownership is resolved. The action was brought on 30 December 2015. The proceedings are now at the stage of service of claim and filing of the defence. The defendants are 18 co-owners: 16 members of the Esquerdo family, holding a total of 45.62% of the property, Prados del Este, S.L., holding 50%, and Comunidades Santa Ana, S.L., holding 4.375%. At the date of authorization for issue of these Consolidated financial statements, the proceedings are at the stage of service of claim and filing of the defence. This amount stands at EUR 6,708 thousand.
- b) The Lorca Town Hall notified IBERDROLA DISTRIBUCIÓN of a provisional settlement for administrative activities for the granting of a business licence for the Carril transformation substation, in the amount of EUR 10.8 million. The amount of the settlement is excessive and disproportionate because it exceeds the limits set by the actual or foreseeable cost of the municipal service or activity or, failing this, the value of the services received. On 12 March 2013 an application was submitted for reconsideration by the same authority. A decision was issued on 12 April 2013, upholding the application and issuing a new settlement for a value of EUR 4 million, plus EUR 748 thousand in late-payment interest. This decision was challenged in proceedings in the Murcia Contentious-Administrative Court number 6. Application was made for suspension of the administrative act. The Court issued a ruling on 20 November 2013 suspending execution of the challenged act, on condition a bond was paid into court in the amount of the settlement to the defendant local authority. On 20 December 2013 a bank guarantee was presented to the Lorca Town Hall as security for the suspension of the tax debt challenged. Lorca Town Hall returned the guarantee to Caixabank for cancellation. On 25 February 2014 Caixabank announced it had cancelled it on notification of suspension of the settlement, with no need for the guarantee stipulated by the Town Hall. The Court agreed to combine proceedings. A ruling in the first instance is pending by the Lorca Contentious-Administrative Court.

- c) On 16 June 2014, the CNMC began sanction proceedings against IBERDROLA GENERACIÓN ESPAÑA for alleged fraudulent procedures to alter the price of electricity at the Duero, Tajo and Sil hydroelectric power generation units in December 2013. The fine was announced on 30 November 2015, in the amount of EUR 25 million. IBERDROLA GENERACIÓN ESPAÑA submitted an appeal to the National Court's Contentious-Administrative Section, and this was admitted to proceedings, being also granted the suspension of the execution of the sanction. The IBERDROLA Group believes its action was proper and legal, and did not therefore make any provision for this during the year.
- d) Claim filed by Banco Mare Nostrum (BMN) against IBERDROLA INMOBILIARIA in Madrid Court of First Instance No 14. Ordinary Proceedings No 496/2014, to which two other court proceedings, formerly conducted in another Madrid court and in a Murcia court, have been joined. This is a claim for a specified amount in which the claimant seeks a declaration that the deed of sale of 20% of the undivided joint title to the lots located at Cabo Cope is a nullity, an order that the deed be discharged by reason of supervening absence of its objects or frustration, with a refund of the price paid, the return of the commercial paper made over by BMN, and an award of damages, in a total amount of EUR 18,447 thousand.

Contingent assets

- a) IBERDROLA RENOVABLES ANDALUCIA, S.A (IBERANDA) filed a money claim against Grupo GESA on 1 March 2016 for a total value of EUR 7,086 thousand (increased by interest accrued until payment in full) in Madrid Court of First Instance No 11 (Ordinary Proceeding 265/2016). On 13 July 2016, Grupo GESA filed its defence and counterclaim, seeking to extract from IBERANDA a payment of EUR 4,503 thousand in respect of success fees not paid to Grupo GESA for its assistance in the application for and obtainment of megawatt licences for the benefit of IBERANDA in wind power competitive bidding procedures in Andalucía. On 19 October 2016, IBERANDA filed its defence in reply to the counterclaim, which it contested on the grounds that the stipulated condition for such success fees had gone unmet: that condition was that there be obtained a certificate of final commissioning of the various projects in question.
- b) On 9 May 2016, IBERDROLA filed a claim against BANKIA, S.A. to recover damages sustained as a consequence of IBERDROLA's purchase of shares in the context of the bank's IPO in 2011. IBERDROLA's decision to subscribe for shares was taken in reliance on the information provided in the prospectus published for that purpose by BANKIA, S.A. The business and financial information contained in that prospectus has been shown to be severely inaccurate, incorrect and false, with material omissions; therefore, IBERDROLA made a clear mistake when placing orders to subscribe shares, which mistake is excusable and invalidates the transaction.

On 7 September 2016, IBERDROLA was served with BANKIA, S.A.'s statement of defence, and on 2 and 5 December 2016 a preliminary hearing was held at which the parties proposed to introduce evidence and the trial was appointed to be held on 9 and 10 March 2017.

The value of IBERDROLA's claim comes to EUR 12,400 thousand in respect of losses sustained as a result of that investment.

- c) On 29 April 2016, IBERDROLA, Endesa, S.A., Mondragón Inversiones, S. Coop. and Kutxabank, S.A. submitted joint civil proceedings against International Cable, B.V. in the court of First Instance in Madrid. The proceedings concern a contract for the purchase of shares of Euskaltel, S.A. on 5 October 2012, between the plaintiffs (as the sellers) and the defendant (as the buyer), whereby the plaintiffs request a ruling against the defendant for payment of the amount owed to each plaintiff for in relation to the variable price payable (earn-out). Specifically, the amount claimed by IBERDROLA is EUR 9,080 thousand (plus statutory interest and costs). On 24 November 2016 the response was received to the demand and the preliminary hearing is set for 27 June 2017.

The IBERDROLA Group's appeals on regulatory issues were submitted in opposition to general dispositions of an indefinite amount, affecting the regulatory and remuneration framework of the companies. Therefore, they concern regulatory dispositions that were in force at the time of appeal.

IBERDROLA's net assets are not at risk with respect to the appeals submitted against general energy stipulations because the economic effects of the stipulations challenged apply when they come into force. An estimate of the appeals submitted by third parties has a limited economic scope, as this would force amendments to the regulatory framework and possible refunds.

The following are the main appeals submitted by IBERDROLA against general regulatory dispositions:

- a) Iberdrola Generación, S.A.U. (IBERDROLA GENERACIÓN) and Tarragona Power, S.L. submitted appeals to the National Court against the Ministerial Orders ITC/2844/2011 and IET/2599/2012 regulating transfers of funds for the years 2011 and 2012 to Spain's Institute for Energy Diversification and Savings. The National Court's Contentious Section decided to investigate whether the Savings Plans were unconstitutional on the grounds they could constitute a breach of equal rights. Both appeals are pending a ruling by the Constitutional Court concerning the constitutionality of Additional Provision 3 of the Royal Decree-law 14/2010. The Constitutional Court, in its decision of 6 October 2016, dismissed the unconstitutionality issue. The case will accordingly be returned to the National Court, which will decide on the merits.

IBERDROLA considers there is a contingent asset for the periods challenged that are pending a ruling. The Consolidated income statement for 2016 does not include any income for these periods, a sum of EUR 210,422 thousand.

- b) On 29 January 2014 IBERDROLA GENERACIÓN, S.A. and Tarragona Power, S.L. submitted contentious-administrative appeals against the Ministerial Order IET/75/2014 of 27 January regulating transfers of funds, charged to electricity production companies, from the specific CNMC account to the Institute for Energy Diversification and Savings, in 2013 in implementation of the 2011-2020 Energy Savings and Diversification Action Plan, and the criteria for implementation of the measures stipulated in this plan. As in the matter referred to above, the Constitutional Court, in its decision of 6 October 2016, dismissed the unconstitutionality issue. The case will accordingly be returned to the National Court, which will decide on the merits.

IBERDROLA considers there is a contingent asset for the periods challenged that are pending a ruling. The Consolidated income statement for 2016 does not include any of the income for these periods, income that would amount to EUR 56,357 thousand.

- c) IBERDROLA RENOVABLES ENERGÍA, S.A.U. (IRE) submitted an application for judicial review before the Supreme Court against the Royal Decree 413/2014, of 6 June, regulating electricity production from renewable energy sources, cogeneration and waste, and against the Ministerial Order IET/1045/2014, of 16 June, adopting the remuneration metrics for model facilities applicable to certain facilities for electricity production from renewable energy sources, cogeneration and waste. The separate challenges to each statutory instrument have been joined into a single set of proceedings because the "Metrics Order" was adopted by way of implementing the Royal Decree 413/2014, and the two instruments shape the new regulatory scenario that now governs facilities for producing electricity from renewable energy sources. On 1 July 2016, the Supreme Court dismissed the appeal, with three particular opinions. The Court takes the view that the new remuneration framework does not constitute a prohibited retrospective exercise of power, because it is designed to take account of the reasonable return earned by the facility throughout its entire useful life, even where this approach involves reviewing past remuneration. Neither does the Court believe that there has been any violation of the principles of legal certainty and legitimate expectation, insofar as no one could have assumed that the former remuneration framework was immune to change.

An appeal having been lodged with the Constitutional Court, on 2 September 2016 the ancillary suit for the nullity of proceedings was formally filed with the Supreme Court. On 26 October 2016 IRE was served with notice of the dismissal of its ancillary suit formality of the proceedings. Appeals to the Constitutional Court were lodged on behalf of Energyworks Carballo and Energyworks Cartagena on 29 November and 2 December 2016, respectively. On 5 December 2016, an appeal was filed on behalf of IRE.

- d) The application for amparo to the Constitutional Court by IBERDROLA against the ruling by the Supreme Court refusing to accept an appeal against CNE settlement 14/2011 (the issue was whether or not the provisional settlement formed part of proceedings). On 6 July 2015 the Constitutional Court agreed to admit the application for amparo to proceedings. The ruling stipulated that the issue was related to the specific case because it involved a legal precept with major general social or economic repercussions. On 30 September 2015 the allegations were presented.
- e) Iberdrola Energía Solar de Puertollano S.A. (IESP), on 14 March 2016, lodged an application for judicial review of the decision of the CNMC (Spain's markets and competition regulator) of 14 January 2016 approving final settlement of the equivalent premiums, premiums, incentives and supplements due to thermal solar power facilities for 2009, 2010 and 2011 in the amount of EUR 12,319 thousand, which the CNMC decided ought to be refunded, on the basis that the upper bounds for gas usage permitted by statute had been surpassed, the CNMC having assumed that some of the power delivered to the system had been generated using gas rather than solar energy. On 13 June 2016, the National Court decided to adopt the interim measure applied for by IESP, for which purpose a sufficient bond was paid into court on 6 September 2016. On 7 November 2016 the claim was formally lodged, supported by expert witness reports produced by NERA, Técnicas Reunidas (the manufacturer of the steam generator) and Fundación para el Fomento de la Innovación Industrial. The Attorney General's defence contesting LIBERSOL's claim was served on us on 15 February 2017, and at the date of authorisation of issue of these Consolidated financial statements is still under analysis.
- f) The contentious-administrative appeal by IBERDROLA ESPAÑA to the Supreme Court against the Order IET/2444/2014 of 19 December by the Ministry of Industry, Energy and Tourism determining electricity access fees for 2015. On 28 October 2016, the proceedings were pending for a vote and a ruling.
- g) The contentious-administrative appeal by IBERDROLA DISTRIBUCIÓN to the National Court against the Resolution by the State Energy Secretariat of 2 June 2015 approving certain procedures for the processing of data from type 5 measurement units for the purposes of energy billing and payment. After the expert witness report was ratified, IBERDROLA DISTRIBUCIÓN's conclusions were presented on 2 February 2017. We are awaiting the conclusions of the General Attorney and of the co-defendant, Red Eléctrica.
- h) An application for judicial review was filed with the Supreme Court by IBERDROLA DISTRIBUCIÓN against the final settlement of regulated activities in the electricity sector for 2011, which was approved 5 November 2015 by the CNMC and notified to IBERDROLA DISTRIBUCIÓN on 11 November 2015. The application also extends to the presumed dismissal (by virtue of absence of a reaction from the competent authority) of the extraordinary application for reconsideration and the application for ex officio review lodged against article 5 of Order IET/107/2014 of the Ministry of Industry, Energy and Tourism. On 23 November 2016, we requested that the application be broadened in scope to encompass the express dismissal of the extraordinary application for reconsideration.
- i) IBERDROLA ESPAÑA lodged an application for judicial review with the National Court against the final settlement of regulated activities in the electricity sector for 2014, which was approved by the CNMC on 24 November 2015. On 5 October 2016, the application was given leave to proceed, and the case file was served on the General Attorney for him to file a defence.

- j) An application for judicial review was lodged by IBERDROLA ESPAÑA with the Supreme Court against Order IET/2735/2015 of 17 December, setting electricity access tolls for 2016 and adopting a range of model facilities and remuneration parameters for electricity production facilities that use renewable sources of energy, combined heat and power, and waste. On 9 January 2016, the application was given leave to proceed, and the case file was served on the General Attorney for him to file a defence.
- k) Appeal in cassation lodged by IBERDROLA with the Supreme Court against the decision of the National Court in appeal Number 143/2014 (formerly Number 1156/2013, heard by the High Court of Justice of Madrid) against the Decision of 17 May 2013 of the Interdepartmental Commission for the Supervision of the Securitisation of the Electricity System Revenue Shortfall, which dismissed the application for reconsideration filed by IBERDROLA against the decision of that same Commission of 26 November 2012, declaring the presence of exceptional circumstances in the markets for the purposes of article 5.2 of Royal Decree 437/2010 of 9 April. On 24 November 2016, the General Attorney contested IBERDROLA's appeal in cassation.
- l) IBERDROLA GENERACIÓN filed an application with the National Court for enforcement of the decision of 8 October 2014 handed down in the judicial review proceedings brought by IBERDROLA GENERACIÓN against the decision of the CNE (Spain's former energy regulator) of 24 April 2008. On 21 November 2016, an application for enforcement was filed on the grounds that the calculation of the interest on the decrease in rights for 2006 conducted by the CNMC is incorrect, being inconsistent with the Court's decision and with the relevant case-law.

Among the regulatory litigation brought by third parties that may affect the remuneration and equity of the IBERDROLA Group there are no outstanding resources for its importance.

Regarding judicial proceedings dealing with tax matters the most significant litigations are as follows: As to national taxes, and in particular the new electricity taxes created under the Law 15/2012, of 27 December, of tax measures for energetic sustainability, applications for judicial review have been submitted in respect of the orders (issued by the national government and the regional governments of the Basque Country and Navarre) adopting self-assessment forms for the tax on the value of electricity production and the taxes on the production and storage of spent nuclear fuel and radioactive waste. The Supreme Court ordered that an issue of unconstitutionality be referred to the Constitutional Court, which then refused leave to proceed. The case is now pending a vote and decision by the Supreme Court.

- b) An appeal was submitted against the Royal Decree 198/2015 of 23 March implementing the article 112 bis of the Rewritten Text of the Spanish Water Law and regulating the fee for using ground water to produce electricity in intercommunity demarcations, published in the Official State Journal Nº 72 of 25 March 2015. The Supreme Court has issued a ruling stipulating its competence, the proceedings are pending for vote and decision point.
- c) Concerning the Extremadura "green tax", applications for judicial review have been submitted in respect of the settlements for the period 2006-2014 under the "Ley de la Asamblea de Extremadura 8/2005" of the Tax on Facilities Affecting the Environment in the Community of Extremadura. The Constitutional Court upheld the unconstitutionality declared by the Supreme Court in a ruling handed down on 16 February 2015. Final judgments were issued in respect of IBERDROLA GENERACIÓN's years 2006, 2007, 2008 and 2009. The Extremadura High Court agreed to submit a new issue of unconstitutionality to the Constitutional Court in the proceedings instigated against the settlement in respect of 2012 by IBERDROLA GENERACIÓN NUCLEAR. The Extremadura High Court is issuing rulings to maintain suspension of processes as of 2010, until the Constitutional Court issues its own ruling.

After these favourable decisions, IBERDROLA considers there is a contingent asset for the periods challenged that are pending a ruling. The Consolidated income statements at 31 December 2016 and 2015 do not include any income for these periods, a sum of EUR 319 million.

- d) With respect to the Tax on environmental damage caused by certain usages and processes involving reservoir water, created by the Galician Parliament Law 15/2008 of 19 December, IBERDROLA GENERACIÓN appealed against the settlements paid in respect of the years 2009, 2010, 2011 and 2012 under this law on the possible grounds of unconstitutionality. The High Court in Galicia issued final judgments in 2009, 2010 and 2012. An appeal was submitted against settlements in respect of the year 2011. The Supreme Court dismissed the appeal on the ground that the value was insufficient, given that the only reason why the appeal was lodged was the fact that there was an error in the paragraph on available forms of appeal in the judgement of the High Court of Justice of Galicia, which we leveraged to gain access to cassation proceedings for a tax in connection with which such proceedings would otherwise have been unavailable to us. Contentious-administrative appeals were submitted against the settlement agreements arising from the Non-conformity Documents in the years 2009, 2010, 2011 and 2012 with respect to the tax on environmental damage caused by certain usages and processes involving reservoir water. The High Court of Justice of Galicia partly allowed our appeals as to the penalties, but not the settlements, ordered by the Galicia regional revenue agency, owing to inconsistencies in the calculation of the taxable base. Specifically, the amount that has been quashed comes to EUR 1,725 thousand. However, it is to be borne in mind that the settlements and penalties for the period 2013-2015 are still at the administrative proceedings stage. It is probable that the penalties for those periods will likewise be quashed, in an amount of EUR 1,011 thousand, making for total savings of EUR 2,736 thousand.

The Register Corrections relating to hydro facilities in Galicia have been appealed against in the High Court of Justice of Galicia. These appeals are at various different procedural stages.

- e) Appeals were submitted against the self-assessments as a result of wind power charges by the Castilla La Mancha, Galicia and Castilla y León Communities, the Tax on facilities affecting the environment in Murcia and Valencia, the Tax on the visual impact caused by equipment and the supply of electricity and fixed communications equipment in La Rioja, and the Tax on disposal of waste at dumps in Castilla y León. An appeal was also submitted against provisions for the Tax on the production of nuclear electricity-production facilities in Catalonia.

In the matter of the wind power levy assessed by the Castilla La Mancha Community, the High Court of Justice referred a prior issue for a preliminary ruling by the Court of Justice of the European Union and an issue of unconstitutionality to the Constitutional Court. The Constitutional Court refused leave to proceed to the issue of unconstitutionality. The proceedings are at a halt until the Court of Justice of the European Union rules upon the prior issue referred to it.

- f) An appeal was submitted against the resolution by the Central Economic-Administrative Court of 5 March 2015, issued with respect to Economic-Administrative Claims 00/00317/2005, submitted against the resolution of 4 November 2004 issued by the Tax Authority's National Inspection Agency, against the provisional settlement agreement by the National Inspection Agency concerning the Tax on Corporations - Consolidated Taxation Regime, in the year 2002, and 00/05607/2013, submitted against the resolution of 6 September 2013 by the Central of Major Taxpayers' Delegation, which overruled the appeal against the final settlement agreement by the Central of Major Taxpayers' Delegation concerning the Tax on Corporations - Consolidated Taxation Regime, in the year 2002. The proceedings are pending for vote and decision point.

The main legal proceedings in which IBERDROLA or foreign subsidiaries are involved at the date of authorization for issue of these Consolidated financial statements are as follows:

Contingent liabilities

- a) There are eight lawsuits (one administrative and seven civil) involving IBERDROLA in relation to the authorization for issue on 1 July 2008 by its subsidiary IBERDROLA RENOVABLES, S.A. of a takeover bid targeting the ordinary and preference shares of the Greek investee C. ROKAS, S.A. On the occasion of the merging out of existence of IBERDROLA RENOVABLES, S.A. into IBERDROLA, the latter became subrogated to all rights and obligations of the former, including those arising from the proceedings so far referred to. The administrative proceedings consist of an appeal in cassation against the penalty imposed by the Greek Securities Market Commission (HCMC) on IBERDROLA RENOVABLES, S.A. with respect to the takeover bid launched in 2008. The hearing at which that appeal in cassation was to be decided upon had been originally scheduled for 19 May 2015 and although it was foreseen that the sentence would be known before mid 2016. There is currently no available information to predict when this appeal will be resolved.

The remaining civil actions (seven) were instituted by shareholders of C. ROKAS, S.A. and consist of claims for damages equivalent to the difference between the price at which IBERDROLA RENOVABLES, S.A. launched the takeover bid (EUR 16 per ordinary share and EUR 11 per preference share), a price which was authorised by HCMC, and the price which those shareholders believe ought to have been set (EUR 21.75 per ordinary share and EUR 21.50 per preference share).

On 14 October 2014, IBERDROLA was notified of the decision issued regarding three of the civil actions, which had been joined into a single one. The decision was unfavorable and IBERDROLA was ordered to pay EUR 10.9 million plus interests (which, at 24 October 2014, came to EUR 4.1 million), of which EUR 0.632 million (plus interests) are IBERDROLA's responsibility on its own, whereas the rest of the amount of the damages must be paid severally by IBERDROLA, Christos Rokas and Georgios Rokas. IBERDROLA does not have face claimants' costs awarded in these proceedings. IBERDROLA has appealed against this decision having set the date to resolve it on 12 November 2015. However, the hearing was finally summoned on 6 October 2016. The ruling that resolves this appeal is expected to be issued within 4 to 10 months (or even more) since the hearing.

In relation two of these three accumulated proceedings, on 26 March 2015 the Court handed down a definitive ruling dismissing IBERDROLA's request for injunctive stay of the provisional implementation of the ruling of 14 October 2014, confirming provisional implementation of the ruling, and compelling IBERDROLA to pay out EUR 420 thousand in relation to two of the three proceedings (EUR 300 thousand and EUR 120 thousand respectively), and EUR 300 in court costs. In May 2015 IBERDROLA proceeded to pay such amounts (EUR 420 thousand) to the plaintiffs which, in return, proceeded to return the guarantees provided by IBERDROLA. With regard to the third set of proceedings (Collective Suit, Litsa and others), IBERDROLA abandoned its request for stay of execution after reaching an agreement with the plaintiffs, whereby IBERDROLA issued a first-request bank guarantee in their favour for a total of EUR 12.7 million, which can only be called if an unfavourable ruling is handed down against IBERDROLA's appeal. On 23 September 2015 the plaintiffs in the third case (Collective Suit, Litsa and others) instigated a fresh round of proceedings to claim capitalisation of the interest accrued and not paid in connection with the ruling of 14 October 2014. The total amount of the capitalised interest claimed by the plaintiffs was EUR 824 thousand, calculated from the date on which the claim was notified (23 September 2015) to the intended date of the hearing (scheduled for 21 September 2017), with consideration of the prevailing rate in Greece (9.30%). The amount claimed is an estimate, as the interest rate can fluctuate and depends on the date on which the hearing actually takes place.

The remaining other three civil actions are still in a preliminary phase, so it is difficult to determine when a decision upon them will be forthcoming, given the circumstances of the courts of that country. At the date of authorization for issue of these Consolidated financial statements, the hearing for two of the procedures is set on 2 March 2017 and 8 November 2017. The hearing for the third procedure was celebrated on 18 January 2017 and it is expected that the sentence will be issued within a period between 6 months and a year from the date of the hearing.

The total amount now being claimed (excluding the proceedings where a final judgement has been handed down in favour of IBERDROLA), after reduction of the claimed amounts, mainly under the head of moral damages, has been fixed at EUR 15.5 million, to which must be added any amounts relating to statutory interest and legal costs.

- b) There are various employment, civil and tax claims imposed on ELEKTRO and on different companies of the NEONERGIA Group in Brazil. The IBERDROLA Group considers the chance of losing these claims to be very slight and the related amounts not significant.
- c) Arbitration proceedings in the International Chamber of Commerce instigated by the consortium (led by EDF) which purchased 30 wind farms owned by Iberdrola Renovables Energía, S.A. in France through its French subsidiary. The sale was concluded in May 2013. The claim is based on a purported breach by IBERDROLA of the representations and warranties set out in the contract as to compliance with maximum noise levels permitted by French law. In January 2016, the purchaser consumption submitted a request for arbitration. In July 2016, the parties agreed on the terms of reference of the arbitration and the procedural timetable (four months for filing the statement of claim, four months for filing the answer, three months for a counter-answer and three months for the final answer). We have already received the arbitration claim, which sets the amount sought to be recovered at EUR 52,000 thousand, subject to review (as against the originally claimed amount of EUR 78.4 million). The statement of claim cleaves to the line of reasoning presented from the outset: the alleged breach by IBERDROLA of the representations and warranties set out in the contract and breach of the noise levels permitted by French law.
- d) The US Environmental Protection Agency has filed claims against various subsidiaries of AVANGRID for failing to comply with environmental issues. The IBERDROLA Group considers that the possibility of these claims being lost is remote and that the amount involved could not be significant. On the other hand, AVANGRID instigated legal proceedings against the former owners of certain sites in order to recover the costs of environmental restoration work it was forced to pay. The IBERDROLA Group did not recognise collection rights for this item, as the conditions of registration required by accounting regulations had not been met.
- e) Normal development of building facilities for third parties includes a negotiation phase and friendly closure at the completion in which aspects of different nature are discussed, and may give rise to claims for and against the Group. In the year 2015, the consortium, of which Iberdrola Ingeniería y Construcción, S.A.U. (IBERDROLA INGENIERÍA) is part of, for the construction of a combined cycle project in Algeria has opened a claim filed before a customer consortium amounting to EUR 240 million and a complaint received by the consortium in the amount of EUR 250 million in relation to the delay and extra costs arising from the implementation of the project. On 28 September 2016, the consortium and the client reached an agreement of principles for the closing of the reciprocal claims by which the consortium undertakes to pay the client financial compensation.
- f) In October 2016, the civil engineering subcontractor for a project in Canada filed an arbitration claim against IBERDROLA INGENIERÍA for a value of CAD 13,660 thousand, plus interest and costs, for work performed, and cost overruns and delays in the performance of the work. IBERDROLA INGENIERÍA submitted its answer in November 2016, comprehensively contesting the claim, which the company believes to be unfounded, and submitting a counterclaim for an approximate amount of CAD 14,954 thousand.

- g) In November 2016, furthermore, the subcontractor for assembly of the fuel management system for a project in Canada submitted a request for arbitration of a claim for approximately CAD 5,631 thousand in respect of alleged interference and delays caused by IBERDROLA INGENIERÍA, which has contested the claim and submitted a counterclaim against that subcontractor for delay and other breaches for a value of approximately CAD 5,296 thousand.
- h) At the São Paulo Regional Court, revocatory action was submitted by ELEKTRO to overturn the decision by that Court not to exempt the company from payment of charges to use hard shoulders on motorways to lay electricity cable. The estimated amount due for those charges in 2016 terms comes to almost EUR 30 million. According to its litigation advisers, ELEKTRO may succeed in these proceedings. The outcome of the action is uncertain, because it involves a conflict between sector-specific regulations: energy sector regulations determine that use of hard shoulders is free of charge for distributors, while the transport sector regulations establish an annual charge for the right to use them. This issue aside, some concession holders have started to collect their debits, as has ELEKTRO. In 2016, the Supreme Court ruled that the statute of limitations for debts owed by public service concession holders is only five years. This translates into a considerable reduction in ELEKTRO's potential debt if it loses in the courts. In addition, in December 2016 ELEKTRO obtained for the first time an important favourable decision in the São Paulo Court, which examined the merits of the case for the first time: the prospects of final success have therefore improved. There are indications that the electricity regulator ANEEL would agree for these amounts to be transferred to tariffs if they finally had to be paid.
- i) Claim by the California Public Utilities Commission: In 2002, just after the energy crisis in the state of California, the California Public Utilities Commission and the California Electricity Oversight Board ("CPUC" and "CEOB", respectively) submitted a claim to the FERC against a number of electricity producers, alleging that these companies had manipulated the market and that the prices set in energy purchase contracts were "unfair and unreasonable", and demanded modifications to the contracts.

FERC dismissed the claim and, following a review by the Californian courts, the Supreme Court ordered FERC to review the case, which had remained dormant since 2008.

In 2014, FERC reopened the case at the behest of the California Public Utilities Commission and appointed an investigating judge, who in April 2016 issued an initial ruling that dismissed any market manipulation by the IBERDROLA Group, but considered that the prices in its energy purchase contract were excessive and to the detriment of end consumers. Damages were set at USD 258 million plus interest. This recommendation is not binding for FERC.

AVANGRID submitted its written plea at the end of May, and its written conclusions on 27 June 2016. The opinion of FERC's technical unit was favourable, and recommended the proceedings be suspended without sanctions. Following these proceedings, FERC is expected to issue a final ruling in the last quarter of the year, and its decision may be appealed in the courts.

The IBERDROLA Group expects that the proceedings will eventually be suspended without any sanction.

Contingent assets

- a) SCOTTISH POWER has begun legal proceedings against BP Exploration Operating Company Limited (hereinafter, BP) in which the Group is claiming GBP 83 million for breach of a long-term gas supply contract and with its partners in the joint business (Talisman North Sea Limited, ENI TNS Limited and JX Nippon Exploration and Production (UK) Ltd.) under which SCOTTISH POWER buys gas to Andrew Field. BP ceased supplying gas to SCOTTISH POWER in May 2011. In July 2015 preliminary issues were heard, following which a ruling was issued on 25 September 2015 establishing that SCOTTISH POWER was entitled to gas for the duration of the supply shutdown, although the exact amount has still to be decided. In addition, it has been established that there was a breach of contract by BP for not acting as a “reasonable and prudent operator”. The legal ruling, however, did not establish that SCOTTISH POWER was entitled to damages, and it was given leave to appeal. The appeal has taken place in October 2016 but it was not satisfactory. The trial to resolve the outstanding issues between the parties is scheduled for October 2017.
- b) In September 2016, IBERDROLA INGENIERÍA initiated arbitration proceedings in the London Court of International Arbitration (LCIA), based in London, United Kingdom, to recover damages caused by the client's actions in a network and substation construction project in Kenya awarded to IBERDROLA INGENIERÍA. The preliminary value of the claim is estimated at EUR 31,497 thousand, including the value of bank guarantees wrongly enforced. In November 2016, the client submitted its answer to the request for arbitration, together with a counterclaim against the company for approximately EUR 150 million, comprising over EUR 110 million for indirect and consequential damages expressly excluded by the terms of the contracts: therefore, the IBERDROLA Group believes it is unlikely the counterclaim will succeed.

Contingent assets and liabilities as at 31 December 2015 are described in the Consolidated financial statements of the IBERDROLA Group for 2015.

44. INTERESTS IN JOINT VENTURES

The detail (at 100%) of the most significant financial figures in 2016 and 2015 relating to the main joint ventures involving the IBERDROLA Group is as follows:

Thousands of euros	Joint property of nuclear and thermal plants					A.I.E. Almaraz-Trillo	A.I.E. Ascó-Valdellós	West of Duddon Sands	Wikingier OSS	Torre Iberdrola
2016	Almaraz	Trillo	Vandellós	Ascó	Aceca	A.I.E. Almaraz-Trillo	A.I.E. Ascó-Valdellós	West of Duddon Sands	Wikingier OSS	Torre Iberdrola
Segment	Deregulated					Renewables			Other businesses	
Intangible assets	–	–	–	–	–	4,524	–	–	–	21
Property, plant and equipment										
Technical instalations	789,148	1,095,139	1,098,376	701,214	–	–	–	1,534,710	117,158	–
Other fixed assets	395	4,889	14,599	–	1,811	1,789	–	–	–	231,023
Non-Current financial Assets	22,710	11,290	44,311	9,864	2,430	2,087	143,569	–	–	–
Currents assets	736,438	385,149	382,552	341,594	769	64,441	160,618	18,433	–	1,592
Total assets	1,548,691	1,496,467	1,539,838	1,052,672	5,010	72,841	304,187	1,553,143	117,158	232,636
Non-Current Liabilities	286,556	438,858	484,165	206,035	–	47,619	152,480	–	–	1,483
Current Liabilities	1,287,877	1,130,214	1,160,643	870,211	4,036	25,222	132,474	41,673	–	31,984
Income	600,645	330,146	285,468	306,241	1,489	165,476	292,017	7,965	–	12,564
Expenses	639,002	413,596	428,230	342,988	1,430	165,476	261,906	32,134	–	9,842

Thousands of euros	Joint property of nuclear and thermal plants					A.I.E. Almaraz-Trillo	A.I.E. Ascó-Valdellós	West of Duddon Sands	Wikingier OSS	Torre Iberdrola
2015	Almaraz	Trillo	Vandellós	Ascó	Aceca	A.I.E. Almaraz-Trillo	A.I.E. Ascó-Valdellós	West of Duddon Sands	Wikingier OSS	Torre Iberdrola
Segment	Deregulated					Renewables			Other businesses	
Intangible assets	–	–	–	–	–	4,437	–	–	–	6
Property, plant and equipment										
Technical instalations	840,152	1,167,698	1,163,848	746,319	–	–	–	1,797,206	62,756	–
Other fixed assets	413	5,268	14,762	–	1,811	1,626	–	19,191	–	218,207
Non-Current financial Assets	22,913	11,290	45,533	9,864	2,430	1,823	110,437	–	–	11,916
Currents assets	518,022	320,585	312,386	318,793	5,380	59,946	142,587	12,142	–	–
Total assets	1,381,500	1,504,841	1,536,529	1,074,976	9,621	67,832	253,024	1,828,539	62,756	230,129
Non-Current Liabilities	283,565	439,338	456,793	200,342	3,088	46,015	125,320	–	–	1,445
Current Liabilities	1,078,506	1,063,930	1,071,935	824,055	1,669	21,817	108,469	61,651	–	1,769
Income	807,316	406,438	381,018	424,798	6,192	154,629	287,233	6,461	–	11,788
Expenses	798,560	416,689	414,391	387,968	2,243	154,629	297,222	36,770	–	10,741

45. GUARANTEE COMMITMENTS TO THIRD PARTIES AND OTHER CONTINGENT LIABILITIES

IBERDROLA and its subsidiaries are required to provide the bank or corporate guarantees associated with the ordinary management of the Group's activities in the countries where the Group operates.

For its activity of electricity generation, the IBERDROLA Group guarantees the obligations undertaken in energy purchase agreements and grid access transactions in different energy markets and against the operators of different electricity systems (MEFF, OMEL, OMI Clear, National Grid, CFE, REE and EDP Distribución).

With regard to generation from renewable sources, the IBERDROLA Group has provided guarantees to third parties to cover the construction, bringing into service and dismantling of facilities, in addition to its responsibilities in long-term energy sales.

Furthermore, as part of its engineering business, the IBERDROLA Group guarantees not only the supply, but also the design, bringing into service and operation of turnkey construction projects sold to its customers.

In 2016, the signing of nonconformity has taken place regarding the corporate Income Tax for the years 2008 to 2011 and regarding the Value Added Tax, for years 2010 and 2011. IBERDROLA has filed the corresponding claims to the Economic Administrative Court against the liquidation agreements, which confirm the acts of nonconformity, requesting the automatic suspension of the execution of the settlements by means of the necessary bank guarantees (Note 28).

In addition, at 31 December 2016 and 2015, there were outstanding obligations resulting from bond issues in the United States amounting to EUR 1,657,533 and EUR 1,574,141 thousand that were secured by the items in the property, plant and equipment of the subgroup AVANGRID.

At 31 December 2016 and 2015, there were no outstanding obligations resulting from mortgage loans secured by items of the property, plant and equipment.

IBERDROLA considers that any additional liabilities that could arise from the guarantees provided at 31 December 2016 and 2015, if any, will not be significant.

Moreover, the IBERDROLA Group in compliance with the contractual obligations associated with loans received from banks, had fully or partially pledged some of its subsidiaries shares at 31 December 2016 and 2015. The detail, by company, of the shares pledged is as follows:

Thousands of euros		2016			2015	
Company	Carrying amount	IBERDROLA Group's % of ownership	Carrying amount by the % of IBERDROLA Group's ownership	Carrying amount	IBERDROLA Group's % of ownership	Carrying amount by the % of IBERDROLA Group's ownership
Renewables business - Spain						
Biovent Energía, S.A.	–	-	–	63,754	95.00%	60,566
Energía de Castilla y León, S.A.	7,755	85.50%	6,631	6,466	85.50%	5,528
Energías Eólicas de Cuenca, S.A.	20,514	100.00%	20,514	16,174	100.00%	16,174
Eólica 2000, S.L.	4,985	51.00%	2,542	4,663	51.00%	2,378
Eólica de Campollano, S.A. (1)	24,512	25.00%	6,128	25,010	25.00%	6,253
Molinos de La Rioja, S.A. (1)	11,467	42.37%	4,859	8,260	42.37%	3,500
Molinos del Cidacos, S.A. (1)	35,606	31.78%	11,316	27,942	31.78%	8,880
Iberdrola Renovables La Rioja, S.A.(1)	–	–	–	96,862	63.55%	61,556
Renewables business – United States						
Colorado Green Holdings, LLC.	82,020	40.75%	33,423	72,917	40.75%	29,714
Renewables business - Brazil						
Arizona 1 Energía Renovável, S.A.	13,910	69.50%	9,667	10,711	69.50%	7,444
Caetité 1 Energía Renovável, S.A. (1)	22,020	69.50%	15,304	16,558	69.50%	11,508
Caetité 2 Energía Renovável, S.A. (1)	25,436	69.50%	17,678	17,562	69.50%	12,206
Caetité 3 Energía Renovável, S.A.	20,932	69.50%	14,548	15,826	69.50%	10,999
Calango 1 Energía Renovável, S.A. (1)	17,560	69.50%	12,204	12,875	69.50%	8,948
Calango 2 Energía Renovável, S.A.	12,383	69.50%	8,606	8,920	69.50%	6,199
Calango 3 Energía Renovável, S.A.	14,254	69.50%	9,907	10,021	69.50%	6,965
Calango 4 Energía Renovável, S.A. (1)	13,513	69.50%	9,392	9,951	69.50%	6,916
Calango 5 Energía Renovável, S.A. (1)	15,482	69.50%	10,760	11,505	69.50%	7,996
Energías Renovaveis do Brasil, S.A.	35,840	100.00%	35,840	25,287	100.00%	25,287
Mel 2 Energía Renovável, S.A.	8,271	69.50%	5,748	7,407	69.50%	5,148
Força Eolica do Brasil 1, S.A. (1)	96,495	69.50%	67,064	72,484	69.50%	50,376
Força Eolica do Brasil 2, S.A. (1)	76,889	69.50%	53,438	60,099	69.50%	41,769

Thousands of euros		2016			2015		
Company	Carrying amount	IBERDROLA Group's % of ownership	Carrying amount by the % of IBERDROLA Group's ownership	Carrying amount	IBERDROLA Group's % of ownership	Carrying amount by the % of IBERDROLA Group's ownership	
Renewables business - Other							
Società Energie Rinnovabili 1, S.p.A. ⁽¹⁾ (Note 13.a)	–	–	–	22,367	49.90%	11,161	
Società Energie Rinnovabili, S.p.A. ⁽¹⁾ (Note 13.a)	–	–	–	21,645	49.90%	10,801	
Network business - Brazil							
Baguari Geração de Energia Elétrica, S.A. ⁽¹⁾	36,950	39.00%	14,411	25,025	39.00%	9,760	
Bahia PCH I, S.A. ⁽¹⁾	39,779	39.00%	15,514	28,624	39.00%	11,163	
Companhia Hidreletrica Teles Pires, S.A. ⁽¹⁾	618,428	19.89%	123,005	468,881	19.54%	91,619	
Energetica Aguas da Pedra, S.A.	127,360	19.89%	25,332	104,681	19.89%	20,821	
Geração CIII, S.A. ⁽¹⁾	63,058	39.00%	24,593	40,067	39.00%	15,626	
Goiás Sul Geração de Energia, S.A. ⁽¹⁾	62,750	39.00%	24,473	47,924	39.00%	18,690	
Rio PCH I, S.A. ⁽¹⁾	38,111	27.30%	10,404	29,131	27.30%	7,953	
Belo Monte Participações, S.A. ⁽¹⁾	314,407	39.00%	122,619	165,833	39.00%	64,675	
Deregulated business - Mexico							
Iberdrola Energía Altamira, S.A. de C.V. ⁽²⁾	–	–	–	330,102	100.00%	330,102	
Iberdrola Energía del Golfo, S.A. de C.V. ⁽²⁾	–	–	–	177,144	100.00%	177,144	
Iberdrola Energía La Laguna, S.A. de C.V. ⁽²⁾	–	–	–	186,626	99.99%	186,607	
Iberdrola Energía Monterrey, S.A. de C.V. ⁽²⁾	–	–	–	131,185	99.99%	131,172	
Iberdrola Energía Tamazunchale, S.A. de C.V. ⁽²⁾	–	–	–	197,739	99.99%	197,719	
Iberdrola Generación México, S.A. de C.V. ⁽²⁾	–	–	–	638,019	100.00%	638,019	
Enertek, S.A. de C.V. ⁽²⁾	–	–	–	92,678	99.99%	92,669	
PIER II Quecholac Felipe Angeles, S.A. de C.V.	21,012	51.00%	10,716	–	–	–	
Deregulated business - Spain							
Tirme, S.A. ⁽¹⁾	20,057	20.00%	4,011	35,875	20.00%	7,175	
Total	1,901,756		730,647	3,344,800		2,419,186	

(1) Companies accounted for using the equity method.

(2) 99% of the shares is in trust. The bank debt of these companies has been paid off in 2016.

46. REMUNERATION OF BOARD OF DIRECTORS

46.1 Application of by-law stipulated remuneration corresponding to 2016

Article 48 of IBERDROLA's by-laws provides that the Company shall assign annually, as an expense, an amount equal to a maximum of two percent of the profit obtained in the year by the consolidated group for the following purposes:

- a) To remunerate directors, in accordance to both, the positions they have held and their executive functions, considering their dedication and attendance at meetings of corporate bodies.
- b) To set up a fund to meet the Company's obligations in pensions, life insurance premiums and payment of indemnities to current and former directors.

In particular, the directors will receive a remuneration which consists of an annual fixed assignment, assistance fees and appropriate hedge risk benefits (death or permanent disability).

Assignment of up to two percent may be accrued only if the previous year's profit is sufficient to cover assignments to the legal reserves and any other obligatory charges, and if shareholders have been allotted a dividend equal to four percent of the share capital.

On the proposal of the Appointments and Remuneration Committee, the Board of Directors has decided to propose to the General Shareholders Meeting to assign by-law stipulated remuneration of EUR 17,000 thousand in 2016, the same amount as in 2015.

These amounts have been registered under "Staff costs" in the Consolidated income statements (Note 35) and the breakdown is as follows:

a) Fixed Remuneration

The fixed annual remuneration received by the board members depends on the duties assigned to them in the Board of Directors and its commissions in 2016 and 2015. The breakdown is as follows:

Thousands of euros	2016	2015
Board chairman	567	567
Committee chairmen	440	440
Committee members	253	253
Board members	165	165

The fixed remuneration earned by members of the Board of Directors with a charge to the by-law stipulated remuneration amounted to EUR 4,599 thousand and EUR 4,551 thousand in 2016 and 2015, respectively.

The detailed fixed remuneration accrued by the members of the Board of Directors, individually, during 2016 and 2015, respectively, is detailed as follows:

Thousands of euros	Fixed remuneration 2016 (*)	Fixed remuneration 2015
Board chairman		
José Ignacio Sánchez Galán	567	567
Committee chairmen		
Inés Macho Stadler	440	440
Samantha Barber	440	440
María Helena Antolín Raybaud ⁽¹⁾	440	396
Georgina Kessel Martínez ⁽²⁾	440	415
Committee members		
Iñigo Víctor de Oriol Ibarra	253	253
Braulio Medel Cámara	253	253
Santiago Martínez Lage	253	253
José Luis San Pedro Guerenabarrena	253	253
Angel Jesús Acebes Paniagua	253	253
Denise Mary Holt	253	253
José Walfredo Fernández ⁽³⁾	253	220
Manuel Moreu Munaiz ⁽⁴⁾	253	211
Xabier Sagredo Ormaza ⁽⁵⁾	180	–
Directors that resigned		
Julio de Miguel Aynat ⁽⁶⁾	–	58
Sebastián Battaner Arias ⁽⁷⁾	–	33
Xabier de Irala Estévez ⁽⁸⁾	68	253
Total	4,599	4,551

(*) Amounts accrued in 2016, not satisfied until the approval of 2016 by-law stipulated remuneration by the General Shareholders Meeting of 2017.

(1) Appointed president of the Appointment Committee after the constitution on the 27 March 2015.

(2) Appointed president of the Audit and Risk Supervision Committee by the Board of Directors in the meeting on the 17 February 2015.

(3) Appointed director by the Board of Directors at its meeting on 17 February 2015. Furthermore, on the same date his appointment was approved by the Board of Directors as a member of the Audit and Risk Supervision Committee.

(4) Appointed member of the Board of Directors, in the meeting on the 17 February 2015. Additionally, on the 27 March 2015, the Board of Directors approved his appointment as member of the Corporate Social Responsibility Committee. On the 26 April 2016 the Board of Directors approved his appointment as member of the Executive Committee.

(5) Appointed member of the Board of Directors, in the meeting on the 8 April 2016. Additionally, on the 26 April 2016, the Board of Directors approved his appointment as member of the Audit and Risk Supervision Committee.

(6) Ceased as member of the Board of Directors at their meeting on 17 February 2015.

(7) Ceased as member of the Board of Directors at their meeting on 17 February 2015.

(8) Ceased as member of the Board of Directors at their meeting on 8 April 2016.

As a proposal of the Board of Directors, at the General Shareholder's Meeting which took place on 27 March 2015, approved the separation of the Appointments and Remuneration Committee into two different Committees; creating on one hand the Remuneration Committee and on the other, the Appointments Committee.

Currently, all members of the Board of Directors of IBERDROLA assume responsibility for at least one of the five committees of the Board of Directors.

b) Attendance fee

The attendance fees paid in 2016 and 2015 for attending the meetings of the Board of Directors and its Committees, based on the duties discharged in each case, were as follows:

Thousands of euros	2016	2015
Chairman of the Board of Directors and committees chairmen	4	4
Committee members and members of the Board of Directors	2	2

The attendance fees paid to the members of the Board of Directors with a charge to the by-law stipulated remuneration amounted to EUR 676 thousand in 2016 and 2015.

Below are listed, individually, the attendance fees received by the members of the Board of Directors during 2016 and 2015, respectively:

Thousands of euros	Attendance fee 2016	Attendance fee 2015
Board chairman		
José Ignacio Sánchez Galán	84	88
Committee chairmen		
Inés Macho Stadler	66	72
Samantha Barber	60	44
María Helena Antolín Raybaud	44	44
Georgina Kessel Martínez	60	68
Committee members		
Íñigo Víctor de Oriol Ibarra	42	42
Braulio Medel Cámara	30	28
Santiago Martínez Lage	28	30
José Luis San Pedro Guerenabarrena	42	42
Angel Jesús Acebes Paniagua	56	56
Denise Mary Holt	36	42
José Walfredo Fernández	34	36
Manuel Moreu Munaiz	58	24
Xabier Sagredo Ormaza	24	–
Directors that resigned		
Julio de Miguel Aynat	–	10
Sebastián Battaner Arias	–	6
Xabier de Irala Estévez	12	44
Total	676	676

c) Remuneration of the executive directors for their executive duties

The remunerations received in 2016 and 2015 by the chairman and chief executive officer for his executive duties, and which are also recognised with a charge to the by-law stipulated remuneration for the year are indicated below individually by remuneration components:

Remuneration components of chairman and chief executive officer:

Thousands of euros	2016	2015
Fixed remuneration	2,250	2,250
Variable annual remuneration ⁽¹⁾	3,250	3,200
Compensation in kind	68	66

(1) Amount relates to variable remuneration received in the years 2016 and 2015, respectively, based on attainment of targets and personal performance in 2015 and 2014, respectively.

The Board of Directors has resolved to maintain the fixed remuneration for the chairman and chief executive officer in 2017 at EUR 2,250 thousand. It also decided to maintain the limit of the variable annual remuneration, which may not exceed EUR 3,250 thousand and which will be paid as far as been agreed in 2018.

On the other hand, in 2015, the former Chief operating officer received EUR 500 thousand as annual variable remuneration for carrying out functions up until 24 June 2014.

d) Provisions and guarantees provided by the Company for directors

This account includes the following items:

- The premium incurred to cover benefits payable in the event of the death, disability and other insurance of current directors, amounting to EUR 256 thousand and EUR 658 thousand in 2016 and 2015, respectively.
- The premium paid to cover directors' Civil Liability Insurance amounts to EUR 62 thousand and EUR 68 thousand in 2016 and 2015, respectively.
- In 2016 and 2015 rebates were received amounting to EUR 287 thousand and EUR 447 thousand, respectively, with respect to the adjustment of the pension insurance policies relating to former members of the Board of Directors.

e) Others

The expenses of the Board of Directors related to external services and other items during 2016 and 2015 amounted to EUR 1,606 thousand and EUR 1,393 thousand, respectively.

Additionally, under the by-law stipulated in 2015 agreements acquired by the company have been addressed amounting to EUR 63 thousand. No such payment has been recorded in 2016.

The undistributed by-law stipulated remuneration for 2016 amounting to EUR 4,520 thousand can be externalized to cover the obligations incurred by the Company to ensure them, in the event they would be materialized.

At 31 December 2016 and 2015 there are no loan or advance granted by the IBERDROLA Group to the members of the Board of Directors of IBERDROLA.

46.2 Remuneration through the delivery of Company shares

Section 4 of article 48 of IBERDROLA's by-laws stipulates that independently of the provisions of the foregoing paragraphs, and subject always to the approval of the General Shareholders' Meeting, the remuneration of directors may also consist on the delivery of shares or options thereon, as well as a payment which takes as its reference the value of the Company's shares.

Consequently, the remuneration through the delivery of Company's shares, or any other remuneration related to such shares is additional, compatible and independent of profit sharing, which is established in section 1 of article 48 of the by-laws of the company.

a) 2011-2013 Strategic Bonus

On 24 June 2014, based on a proposal from the former Appointments and Remuneration Committee, the Board of Directors resolved to settle, having met 93.20% of the targets set, the 2011-2013 Strategic Bonus, approved at the General Shareholders' Meeting of 27 May 2011 and regulated by the 2011-2013 Strategic Bonus Regulations which was also approved by the Board of Directors. Accordingly, the third and last settlement was made in 2016. The Chairman and CEO received 536,359 IBERDROLA shares while the former Chief Operating Officer received 90,640 shares.

b) 2014-2016 Strategic Bonus

On 28 March 2014, the General Shareholders' Meeting resolved, in connection with item seven on the agenda, on the 2014-2016 Strategic Bonus (Note 20) aimed at executive directors, senior executives and other management personnel of the Company and its subsidiaries. The maximum number of shares to be delivered to the beneficiaries (350) of the 2014-2016 Strategic Bonus will be 19,000,000 shares, equal to 0.3% of the share capital at the time this resolution is adopted. A maximum of 2,200,000 shares will be delivered to the executive directors in compliance with the terms and conditions of the scheme. The liquidation of this strategic bonus depends on the completion of the planned objectives and it will be realised in the years 2017, 2018 and 2019.

46.3 Termination benefits

In the event of termination of an external director prior to the end of the period for which he was appointed not due to non-compliance attributable to such director and not due exclusively to his own will, the Company will pay such director a termination benefit subject to the director's obligation during the remaining period of his term (with a maximum of two years) not to accept positions on the governing bodies of companies in the energy sector or competing companies and not to participate in the management or advisory of the same in any other form.

Termination benefits will be equal to 90% of the fixed amount the director would have received for serving his or her remaining term as officer (maintaining any annual fixed amount receivable upon leaving the Board), that could not exceed an amount that is twice 90% of that annual fixed amount.

Since the end of the 90s, executive directors, as well as a group of managers, have the right to receive a termination benefit in the event of termination of the contractual relationship with the Company not due to non-compliance attributable to such director and not due exclusively to his own will. The amount of compensation for the chairman and chief executive officer is currently set at three annuities. The limit shall be two annuities for new contracts with executive directors and senior executives, since 2011.

In addition, executive director contracts contain a non-compete clause in respect of companies and activities of a similar nature, applicable throughout the director's relationship with the Company and for a maximum of two years subsequent to departure. As compensation for this commitment, the executive directors are entitled to receive a payment equal to the remuneration that would correspond to these periods.

46.4 By-law stipulated remuneration in 2017

At the proposal of the Remuneration Committee, the Board of Directors unanimously resolved to freeze, for the 2017 year, directors' compensation in the form of fixed annual remuneration based on position and meeting attendance fees, as it has done since 2008.

47. INFORMATION REGARDING COMPLIANCE WITH ARTICLE 229 OF THE SPANISH COMPANIES LAW

As established in article 229 of the Spanish Companies Law (*Ley de Sociedades de Capital*) introduced by the Royal Decree-Law 1/2010 of 2 July 2010 and in the Law 31/2014, of 3 December 2014, modifying the Spanish Companies Law for the improvement of corporate governance, the conflicts of interest, direct or indirect, that the members of the Board have had with the Company, and the treatment thereof, are indicated below.

The Board of Directors deliberated about the reelection, the requalification, the appointment of the members of the committee, the cease of members of their duties, their appointment as members of the Board of other companies. They also deliberated about the exemption of the prohibition contemplated in the Board of Directors' Regulation of providing services to other companies with a totally or partially same social purpose than their own, or any competitor, or any company of the Group, without the intervention of the affected people in each case.

The chairman and chief executive officer absented himself from the deliberation about his remuneration system and insurance method.

Finally, Mr. Sagredo Ormazá absented himself during the deliberation that concerned Kutxabank, S.A.

48. REMUNERATION OF SENIOR EXECUTIVES

Senior executives are those who answer directly to the Company's Board of Directors, chairman and chief executive officer and, in all cases, the Internal audit director, apart from any other director recognised as senior executive.

At the date of these Consolidated financial statements such condition has not been recognized to any director by the Board of Directors.

At 31 December 2016 and 2015, the Company has 6 senior executives.

The staff costs relating to senior executives amounting to EUR 10,657 thousand and EUR 9,751 thousand in 2016 and 2015, respectively, are recognised under the "Staff costs" heading in the Consolidated income statements of the mentioned years.

The remuneration and other compensation received by senior executives in 2016 and 2015 are detailed below:

Thousands of euros	12.31.2016 ⁽¹⁾	12.31.2015
Monetary remuneration	5,447	4,569
Variable remuneration	3,193	2,537
Compensation in kind	453	418
Payments to account not charged	58	60
Social Security	86	80
Promotor contribution pension plan / social foreseen insurance	41	41
Complementary policy accrual	979	1,647
Complementary policy risk	400	399
Total	10,657	9,751

Number of shares	12.31.2016	12.31.2015
Share-based payment plan, Strategic Bonus ⁽²⁾	364,173	340,381

(1) Includes the remuneration of Mr. Julián Martínez-Simancas Sánchez from 1 January 2016 to 9 January 2016 and the remuneration of Mr. Santiago Matías Martínez Garrido from 9 January 2016, when he was appointed as Director of Legal Services.

(2) During the years 2016 and 2015, 364,173 and 340,381 shares were delivered to senior executives, respectively, for the Strategic Bonus 2011-2013, described in Note 20, for which senior executives received shares of IBERDROLA in equal parts for the years from 2014 to 2016.

A maximum of 2,008,691 shares are to be delivered to senior executives under the 2014-2016 Strategic Bonus (Note 20), tied to their success in achievement of objectives. As of 31 December 2016 and 2015, EUR 6,853 thousand and EUR 8,211 thousand have been provisioned for these commitments, respectively.

For senior executives, including executive directors, there are clauses providing guarantees or protection against different cases of contract termination. These contracts have been approved by the Board of Directors of IBERDROLA and are described in Note 46.

The amount of termination benefits is based on the length of service at the Company and the causes of cease, with a maximum payment of five annuities. Since 2011, for contracts with senior executives, the maximum will be two annuities.

On one hand, the contracts for senior executives set in any case an obligation not to compete in relation to companies and activities similar in nature to those of IBERDROLA and the Group for a period not less than one year after its termination.

On the other hand, during 2016 and 2015 there were no other transactions with the executives outside the normal course of the business.

49. BALANCES AND TRANSACTIONS WITH OTHER RELATED PARTIES

The transactions detailed below are specific to the ordinary business activity and have been carried out on an arm's-length basis:

Transactions carried out by IBERDROLA with significant shareholders

The main transactions carried out during 2016 and 2015 are the following:

Thousands of euros	Major shareholders ⁽²⁾			
	2016		2015	
	Kutxabank, S.A.	Qatar Investment Authority	Kutxabank, S.A.	Qatar Investment Authority
Transaction type				
Expenses and income				
Finance cost	–	–	15	–
Finance income	–	–	28	–
Other transactions				
Dividends and other distributed profit ⁽¹⁾	–	21,571	32,835	21,571

(1) The amounts registered as dividends and other distributed profits correspond to the free allocation rights arising from the paid-up capital increase granted by the General Shareholders' Meetings of 8 April 2016, 27 March 2015 and 28 March 2014, respectively, which have been sold to IBERDROLA at the guaranteed fixed price in accordance with the terms of the capital increases mentioned, as well as the General Meeting attendance fee received by the related party if applicable.

(2) IBERDROLA treats as a major shareholder any shareholder who exerts a significant influence on the company's financial and operating decisions. Significant influence is defined as having at least one director on the Board of Directors.

This also applies to those significant shareholders whose ownership interest in the company enables them to exercise the proportional representation system.

Therefore, in 2015, the amounts relating to major shareholders reflect transactions with Kutxabank and Qatar Investment Authority, these being the only shareholders who satisfied that condition at the date of issue of these financial statements. At the date of preparation of these Financial statements only Qatar Investments Authority satisfies this condition so the amounts related to 2016 are transactions with this shareholder.

Transactions of other IBERDROLA Group companies with major shareholders

The most noteworthy transactions in 2016 and 2015 were as follows:

Thousands of euros	Major shareholders ⁽²⁾			
	2016		2015	
	Kutxabank, S.A.	Qatar Investment Authority	Kutxabank, S.A.	Qatar Investment Authority
Transaction type				
Expenses and income				
Finance cost	–	–	223	–
Received services	–	–	24	–
Other transactions				
Financing agreements: loans and capital contributions (received) ⁽¹⁾	–	–	6,962	–
Guarantees provided	–	–	2,246	–

(1) It includes, inter alia, deposits, debt derivatives, promissory notes, etc.

(2) IBERDROLA treats as a significant shareholder any shareholder who exerts a significant influence on the company's financial and operating decisions. Significant influence is defined as having at least one director on the Board of Directors.

This also applies to those significant shareholders whose ownership interest in the company enables them to exercise the proportional representation system.

Therefore, in 2015, the amounts relating to major shareholders reflect transactions with Kutxabank and Qatar Investment Authority, these being the only shareholders who satisfied that condition at the date of issue of these financial statements. At the date of preparation of these Financial statements only Qatar Investments Authority satisfies this condition so the amounts related to 2016 are transactions with this shareholder.

Transactions with companies integrated by the equity method

The breakdown of transactions with companies accounted for using the equity method which are related parties that were not eliminated in consolidation (Note 2.b) is as follows:

Thousands of euros	2016					2015				
	Asset acquisition	Trade payables	Trade receivables	Sales and services provided	Received services	Asset acquisition	Trade payables	Trade receivables	Sales and services provided	Received services
GAMESA	483,113	356,036	8,961	3,127	63,306	275,436	272,216	63,185	35,272	61,852
Amara, S.A.U.	11,635	4,737	–	2,169	14,160	12,494	5,520	1	2,125	11,121
East Anglia Offshore Wind, Ltd.	18,328	7,407	740	203	–	4,395	6,489	27,849	3,508	5,470
Societa Energie Rinnovabili, S.p.A. (Note 13.a)	–	–	–	774	1,923	2,313	–	60,345	136	–
Societa Energie Rinnovabili 1, S.p.A. (Note 13.a)	–	–	–	172	2,132	–	–	–	–	–
Nuclenor, S.A.	–	27,719	27	586	87	136	32,251	118	453	–
NGET/SPT Upgrades Ltd. (Note 13.a)	63,707	(285)	699	3,109	–	68,447	2,283	3,001	2,737	–
Bidelek Sareak, S.L.	5,952	18,671	–	1,562	–	13,627	36,272	734	7,643	–
Termopernambuco, S.A.	–	–	7,324	21,715	–	–	1,199	12,405	34,213	–
Neoenergía, S.A.	–	665	266,274	205	–	–	790	176,934	287	–
Iberdrola Renovables de la Rioja, S.A.	–	774	54	535	8,017	–	460	105	–	–
Morecambe Wind, Ltd.	–	606	–	1,151	14,605	–	2,619	–	–	–
Other companies	22	39,383	30,337	15,801	10,861	2,594	18,449	15,682	12,204	31,687
Total	582,757	455,713	314,416	51,109	115,091	379,442	378,548	360,359	98,578	110,130

On 21 December 2011, IBERDROLA and Gamesa Eólica, S.L.U (a company belonging to the GAMESA Group) entered into a framework agreement for the supply and maintenance of wind turbines whereby:

- IBERDROLA undertakes to acquire from GAMESA a minimum amount of megawatts equal to 50% of the total fleet of onshore wind turbines acquired by IBERDROLA for its renewables business unit during the term of the framework agreement.
- This commitment will remain in effect from 1 January 2013 until 31 December 2022 or until the number of megawatts acquired by IBERDROLA from GAMESA under the framework agreement reaches 3,800, whichever occurs first.
- IBERDROLA and GAMESA will work closely together on new opportunities relating to the offshore wind power business.
- IBERDROLA and GAMESA will work together in the area of maintenance services to enable GAMESA to become the benchmark company in the maintenance of wind farms for IBERDROLA's entire scope of activity. In particular, the two companies agreed:
 - o To establish new areas of study and analysis in the provision of maintenance services by GAMESA to IBERDROLA and, in particular, in the provision of maintenance services in the United States, the sale and installation of reliability improvements in wind turbines, the extension of their useful life, and the conversion and upgrade of wind turbines.
 - o The extension of the current maintenance services, in the following terms and conditions:
 - § Technology Contract G4X and G5X (Spain): in force on the 1 January 2015 and will maintain its validity during a 3 year period. IBERDROLA could extend the lengthening of the Master Agreement during two consecutive periods of one year each. The minimum number of wind turbines in maintenance will be 1,136 G5X wind turbines / 1,188 G4X wind turbines, although during the validity of the contract, IBERDROLA would have the possibility to take out to third parties a maximum accumulated of 200 MW.
 - § Technology contract G8X (Spain and Portugal): in force on 1 January 2014 and remaining effective during a period of four years. It will maintain its validity for four years. IBERDROLA could extend the lengthening of the Master Agreement for two consecutive additional periods of one year each. The minimum number of wind turbines in maintenance it would be:

Minimum number of wind turbines in maintenance				
	First year	Second year	Third year	Fourth year (and expansions 1 and 2)
Risk Service scope ⁽¹⁾	2,168 MW (92 MW in Portugal)	1,800 MW	1,600 MW	1,400 MW
AT+R scope ⁽²⁾	338 MW	Rest of wind farms	Rest of wind farms	Rest of wind farms

(1) *Risk Service* scope includes the preventive maintenance, as well as the Technical Assistance, for a fixed annual price per turbine.

(2) AT+R scope refers to the Technical Assistance and refill supplies (optional).

- § Spare Parts and Repair Supply Contract (GPRSA): entered into effect from 1 January 2016 and will remain in effect during a period of five years. Supply and repair of spare parts, small and large, for the GAMESA technology fleet in Spain.

- § **Energy Thrust technical improvement:** On 1 October 2015 and 22 December 2016, IBERDROLA and GAMESA have signed two contracts under which IBERDROLA will incorporate in its G8X wind turbines the Energy Thrust technical improvement in 2,220 MW in Spain, Portugal, Italy, Romania, Greece and Cyprus, with the aim of increasing the average production of its wind turbines, as it enables that the turbines adapt perfectly to the specific conditions of the site, which improves the energy delivered to the net in all wind conditions and increase the efficiency and performance of the machines. These contracts are valid for five years.

Transactions with directors and senior executives

Thousands of euros	2016		2015	
	Directors	Executives	Directors	Executives
Type of transactions				
Expenses and Income				
Services received ⁽¹⁾	648	–	1,287	–
Other transactions				
Dividends and other distributed benefits ⁽²⁾	649	81	467	67

(1) The contracts to which this amount is related to in 2015, were allocated respecting the provisions of the Procedure, regarding conflicts of interest and transactions related to directors, significant shareholders and senior managers. Those contracts gather the billing of the company Seaplace S.L., related to the Director Manuel Moreu Munaiz, amounting to EUR 312 thousand approximately, and Soil Tratamiento de Aguas Industriales S.L. company's billing was USD 1,083 thousand (approximately EUR 975 thousand), linked to the Director Iñigo Víctor de Oriol Ibarra, contractor for the supply, transport, assembly and start-up of Cogeneración Ramos en México S.A.'s water treatment plant.

During 2016 there were no transactions related to Seaplace, S.L. and Soil Tratamiento de Aguas Industriales S.L.'s billing was USD 722 thousand (approximately EUR 648 thousand).

(2) The amounts considered dividends and other distributed profit correspond to the free allocation rights arising from the paid up capital increase agreed upon by the Shareholders General Meetings of 8 April 2016, 27 March 2015 and 28 March 2014, respectively have been sold to IBERDROLA at a guaranteed fixed price in accordance with the terms and conditions of the aforementioned increases.

50. FINANCIAL POSITION AND SUBSEQUENT EVENTS AFTER 31 DECEMBER 2016

Financial position

In 2017, the IBERDROLA Group expects to face the regular investment programs with cash flows generated from its operations and access to capital bank funding markets, to capital markets and supranational lenders (such as EIB) although the Group has cash, credit facilities and enough loans available to deal with such investments.

As indicated in Note 25, at 31 December 2016 the IBERDROLA Group had undrawn loans and credit facilities of approximately EUR 6,583,500 thousand.

As indicated in Note 19, at 31 December 2016 the IBERDROLA Group had EUR 181,692 thousand in cash and equivalents and EUR 1,250,994 thousand in short-term deposits.

The IBERDROLA Group's liquidity position exceeds EUR 8,000 million, which is equivalent to more than 24 months of the Group's financing needs.

Thousands of euros	Available
Maturity of credit facility	
2017	266,219
2018	760
2019 on	6,316,521
Total	6,583,500
Cash and cash equivalents	1,432,686
Total adjusted liquidity	8,016,186

Subsequent events

Iberdrola flexible dividend

On 3 January 2017, the facts in relation to the first implementation of the second paid-up capital increase (*Iberdrola flexible dividend*) approved at the IBERDROLA General Shareholders' Meeting on 8 April 2016, under item B and 1 to 11 (both inclusive), point six of the agenda, were determined and were as follows:

- The maximum number of new shares to be issued under the capital increase is 141,379,533.
- The number of free allocation rights required to receive one new share is 45.
- The maximum nominal value of the capital increase amounts to EUR 106,034,650.
- The acquisition price of the free allocation rights under the purchase commitment made by IBERDROLA is EUR 0.135.

At the end of the trading period for free allocation rights:

- The holders of 1,956,083,947 free allocation rights have accepted the irrevocable commitment to purchase assumed by IBERDROLA. Accordingly, IBERDROLA will acquire such rights for a gross amount of EUR 264,071 thousand.
- The final number of new ordinary shares with a nominal value of EUR 0.75 to be issued will be 97,911,000, giving a nominal capital increase from this implementation of EUR 73,433 thousand. This will add 1.539% to IBERDROLA's pre-issue share capital.
- As a result, the share capital of Iberdrola after the capital increase amounts to EUR 4,844,992,500, represented by 6,459,990,000 ordinary shares of EUR 0.75 par value each, fully subscribed and paid.
- Subject to compliance with on legal requirements (and verification of compliance by the Spanish National Security Market Commission), the new shares are expected to be admitted for trading on the continuous market of the Madrid, Barcelona, Bilbao and Valencia Stock Exchanges on 31 January 2017. The ordinary trading of new shares is expected to start on 1 February 2017.

Transactions with treasury shares

At the date of authorization for issue of these Consolidated financial statements, all accumulators on treasury shares have matured (Note 20) and the liquidation has resulted in the acquisition of 20,612,235 treasury shares amounting to EUR 119,561 thousand (18,988,014 shares have been accumulated out of the 31,870,828 maximum potential shares to accumulate at 31 December 2016).

Finally, from the 2016 year-end until the date of authorization for issue of these Consolidated financial statements 17,134,761 treasury shares have been acquired amounting to EUR 91,190 thousand and 7,984 shares have been delivered to Scottish Power amounting to EUR 47 thousand. At the date of authorization for issue of these financial statements, Iberdrola, S.A. had 188,963,789 in treasury shares.

Bond Issue in the Euromarket

On 20 February 2017, the IBERDROLA Group through its subsidiary Iberdrola Finanzas, S.A. has closed two bond issues in the Euromarket, with the guarantee of IBERDROLA for an amount of EUR 100 and 50 million and maturing on 20 February 2024 and 2029, respectively.

Banking Market

On 13 February 2017, the IBERDROLA Group has extended the term for syndicated loans for an amount of EUR 4,187,500 thousand lengthening the maturity from 2021 to 2022.

On 15 February 2017, the IBERDROLA Group signed a green loan amounting to EUR 500,000 thousand over a period of 18 months with the possibility of extending the maturity 12 additional months, giving IBERDROLA the option.

51. FEES FOR SERVICES PROVIDED BY THE STATUTORY AUDITOR

The fees resulted from the services provided in 2016 and 2015 by the statutory auditor are detailed in the table below:

Thousands of euros	TO IBERDROLA			To the rest of the Group Companies			Total		
	Main auditor	Other auditors	Total	Main auditor	Other auditors	Total	Main auditor	Other auditors	Total
2016									
Auditing services	2,553	–	2,553	21,082	61	21,143	23,635	61	23,696
Other audit related services	918	–	918	1,523	111	1,634	2,441	111	2,552
	3,471	–	3,471	22,605	172	22,777	26,076	172	26,248
Other profesional services	–	3,204	3,204	60	5,220	5,280	60	8,424	8,484
Total	3,471	3,204	6,675	22,665	5,392	28,057	26,136	8,596	34,732

Thousands of euros	To IBERDROLA			To the rest of the Group Companies			Total		
2015	Main auditor	Other auditors	Total	Main auditor ⁽¹⁾	Other auditors ⁽¹⁾	Total	Main auditor	Other auditors	Total
Auditing services	2,681	–	2,681	15,894	2,898	18,792	18,575	2,898	21,473
Other audit related services ⁽¹⁾	1,087	–	1,087	7,569	680	8,249	8,656	680	9,336
	3,768	–	3,768	23,463	3,578	27,041	27,231	3,578	30,809
Other professional services	–	824	824	75	2,346	2,421	75	3,170	3,245
	3,768	824	4,592	23,538	5,924	29,462	27,306	6,748	34,054

(1) Other audit related services to the audit include fees arising from the AVANGRID's initial public offering of EUR 5,890 thousand of the main auditor and EUR 1,621 thousand of other auditors.

52. EARNING PER SHARE

The weighted average number of ordinary shares used in the calculation of the basic and diluted earnings per share at 31 December 2016 and 2015 (Note 4.ab) is as follows:

	2016	2015
Average number of shares during the year	6,510,671,000	6,665,596,526
Average number of treasury shares held	(83,102,299)	(87,975,070)
Average number of shares outstanding	6,427,568,701	6,577,621,456

Basic and diluted earnings per share for 2016 and 2015 are as follows:

	2016	2015
Net profit for the year (thousands of euros)	2,704,983	2,421,578
Average number of shares outstanding	6,427,568,701	6,577,621,456
Basic and diluted earnings per share (euros)	0.421	0.368

As described in Note 20 and 50 of these Consolidated financial statements, in July 2015 and January 2016 two paid up capital increases took place in the context of the "Iberdrola flexible dividend" programme. According to IAS 33: "Earning per share" these paid up capital increases have resulted in the correction of the earnings per share corresponding to the 2015 year end included in the Consolidated financial statements for that year, and they have been taken into account to calculate the 2016 year share basic and diluted earnings per share.

53. AUTHORIZATION FOR ISSUE OF THE CONSOLIDATED FINANCIAL STATEMENTS

The Consolidated financial statements for the year ended on 31 December 2016 have been formally prepared by the directors of IBERDROLA on 21 February 2017.

54. EXPLANATION ADDED FOR TRANSLATION TO ENGLISH

These Consolidated financial statements are presented on the basis of IFRS, as adopted by the European Union. Certain accounting practices applied by the Group that conform to IFRS may not conform to other generally accepted accounting principles in other countries.

APPENDIX

YEAR 2016 ADDITIONAL INFORMATION RELATED TO GROUP COMPANIES, JOINTLY-CONTROLLED COMPANIES AND ASSOCIATES OF THE IBERDROLA GROUP

Below is the detail of the proportion of direct or indirect ownership that Iberdrola, S.A. holds in its subsidiaries in its different businesses. The proportion of decision-making votes in the bodies of these companies controlled by Iberdrola basically corresponds with the proportion of ownership.

(*) The consolidation method by company is detailed as follows:

F: Full consolidation

E: Integration by equity method

Company	Address	Activity	Percentage of direct or indirect participation		Auditor	Method(*)
			12.31.16	12.31.15		
<u>DEREGULATED BUSINESS</u>						
Spain and Portugal						
Cobane, A.I.E.	Spain	Energy	100.00	100.00	EY	F
Cogeneración Gequiza, S.A.	Spain	Energy	50.00	50.00	EY	E
Enercrisa, S.A.	Spain	Energy	50.00	50.00	KPMG	E
Energía Portátil Cogeneración, S.A.	Spain	Energy	50.00	50.00	EY	E
Energyworks Aranda, S.L.	Spain	Energy	99.00	99.00	EY	F
Energyworks Carballo, S.L.	Spain	Energy	99.00	99.00	EY	F
Energyworks Cartagena, S.L.	Spain	Energy	99.00	99.00	EY	F
Energyworks Fonz, S.L.	Spain	Energy	100.00	100.00	EY	F
Energyworks Milagros, S.L.	Spain	Energy	100.00	100.00	EY	F
Energyworks Monzón, S.L.	Spain	Energy	100.00	100.00	EY	F
Energyworks San Millán, S.L.	Spain	Energy	100.00	100.00	EY	F
Energyworks Villarrobledo, S.L.	Spain	Energy	99.00	99.00	EY	F
Energyworks Vit-Vall, S.L.	Spain	Energy	99.00	99.00	EY	F
Fudepor, S.L.	Spain	Energy	50.00	50.00	PWC	E
Fuerzas Eléctricas de Navarra, S.A.	Spain	Energy	100.00	100.00	EY	F
Hidroeléctrica Ibérica, S.L.U.	Spain	Energy	100.00	100.00	EY	F
Iberdrola Clientes, S.A.U.	Spain	Wholesale/Retail	100.00	100.00	EY	F
Iberdrola Cogeneración, S.L.U.	Spain	Holding	100.00	100.00	EY	F
Iberdrola Comercialización de Último Recurso, S.A.U.	Spain	Wholesale/Retail	100.00	100.00	EY	F
Iberdrola Generación España, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Iberdrola Generación Nuclear, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Iberdrola Generación, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Iberdrola Operación y Mantenimiento, S.A.U.	Spain	Services	100.00	100.00	EY	F
Iberdrola Servicios Energéticos, S.A.U.	Spain	Services	100.00	100.00	EY	F
Iberduero, S.L.U.	Spain	Energy	100.00	100.00	-	F
Intermalta Energía, S.A.	Spain	Energy	50.00	50.00	EY	E
Nuclenor, S.A.	Spain	Energy	50.00	50.00	EY	E
Peninsular Cogeneración, S.A.	Spain	Energy	50.00	50.00	EY	E
Productos y Servicios de Confort, S.A.	Spain	Services	100.00	100.00	-	F
S.E.D.A. Cogeneración, S.A.	Spain	Energy	50.00	50.00	-	E
Subgrupo Tirme	Spain	Energy	20.00	20.00	Deloitte	E
Tarragona Power, S.L.U.	Spain	Energy	100.00	100.00	EY	F
Tecnomat, S.A. ⁽⁵⁾	Spain	Services	30.00	30.00	-	-
Iberdrola Clientes Portugal, Unipessoal Ltda.	Portugal	Services	100.00	100.00	-	F
United Kingdom						
Manweb Energy Consultants, Ltd.	United Kingdom	Energy	100.00	100.00	EY	F
Scotash, Ltd.	United Kingdom	Others	50.00	50.00	EY	E
Scottish Power Generation Holdings, Ltd.	United Kingdom	Holding	100.00	100.00	EY	F
ScottishPower (DCL), Ltd.	United Kingdom	Energy	100.00	100.00	EY	F
ScottishPower (DCOL), Ltd.	United Kingdom	Inactive	100.00	100.00	-	F

Company	Address	Activity	Percentage of direct or indirect participation		Auditor	Method(*)
			12.31.16	12.31.15		
ScottishPower (SCPL), Ltd.	United Kingdom	Energy	100.00	100.00	EY	F
ScottishPower Energy Management (Agency), Ltd.	United Kingdom	Services	100.00	100.00	EY	F
ScottishPower Energy Management, Ltd.	United Kingdom	Energy	100.00	100.00	EY	F
ScottishPower Energy Retail, Ltd.	United Kingdom	Energy	100.00	100.00	EY	F
ScottishPower Generation, Ltd.	United Kingdom	Energy	100.00	100.00	EY	F
SMW, Ltd.	United Kingdom	Others	100.00	100.00	EY	F
SP Dataserve, Ltd.	United Kingdom	Data Management	100.00	100.00	EY	F
SP Gas Transportation Cockenzie, Ltd.	United Kingdom	Inactive	100.00	100.00	-	F
SP Gas Transportation Hatfield, Ltd.	United Kingdom	Inactive	100.00	100.00	-	F
Rest of Europe						
Iberdrola Energie Deutschland, GmbH. ⁽⁵⁾	Germany	Services	100.00	100.00	-	-
Iberdrola Energie France, S.A.S. ⁽⁵⁾	France	Services	100.00	100.00	EY	-
Iberdrola Clienti Italia, S.R.L. (before Iberdrola Energía Italia, S.R.L.) ⁽⁵⁾	Italy	Services	100.00	100.00	-	-
Iberdrola Energie Romania, S.R.L. ⁽⁵⁾	Romania	Energy	100.00	100.00	-	-
Mexico						
Hidro I, S.L.U.	Spain	Holding	100.00	100.00	EY	F
Cinergy, S.R.L. de C.V.	Mexico	Services	100.00	100.00	EY	F
Electricidad de Veracruz, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Enertek, S.A. de C.V.	Mexico	Energy	99.99	99.99	EY	F
Iberdrola Clientes, S.A. de C.V.	Mexico	Wholesale/Retail	100.00	100.00	EY	F
Iberdrola Cogeneración Altamira, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Cogeneración Bajío, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Cogeneración Ramos, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Energía Altamira de Servicios, S.A. de C.V.	Mexico	Services	100.00	100.00	EY	F
Iberdrola Energía Altamira, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Energía Baja California, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Energía del Golfo, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Energía Escobedo, S.A. de C.V.	Mexico	Energy	100.00	100.00	-	F
Iberdrola Energía La Laguna, S.A. de C.V.	Mexico	Energy	99.99	99.99	EY	F
Iberdrola Energía Monterrey, S.A. de C.V.	Mexico	Energy	99.99	99.99	EY	F
Iberdrola Energía Norte, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Energía Noroeste, S.A. de C.V.	Mexico	Energy	100.00	-	EY	F
Iberdrola Energía Tamazunchale, S.A. de C.V.	Mexico	Energy	99.99	99.99	EY	F
Iberdrola Generación, S.A. de C.V.	Mexico	Services	100.00	100.00	EY	F
Iberdrola Generación México, S.A. de C.V.	Mexico	Holding	100.00	100.00	EY	F
Iberdrola México, S.A. de C.V.	Mexico	Holding	100.00	100.00	EY	F
Iberdrola Servicios Corporativos, S.A. de C.V.	Mexico	Services	100.00	100.00	EY	F
Servicios Administrativos Tamazunchale, S.A. de C.V.	Mexico	Services	100.00	100.00	EY	F
Servicios de Operación La Laguna, S.A. de C.V.	Mexico	Services	100.00	100.00	EY	F
Servicios Industriales y Administrativos del Noreste, S.R.L. de C.V.	Mexico	Gas	51.12	51.12	EY	F
United States and Canada						
Iberdrola Canada Energy Services, Ltd.	Canada	Energy	100.00	100.00	EY	F

Company	Address	Activity	Percentage of direct or indirect participation		Auditor	Method (*)
			12.31.16	12.31.15		
RENEWABLE BUSINESS						
Spain						
Anselmo León Hidráulica, S.L. (1)	Spain	Energy	100.00	100.00	-	E
Biocantaber, S.L.	Spain	Energy	50.00	50.00	-	E
Bionor Eólica, S.A.	Spain	Energy	57.00	57.00	EY	F
Biovent Energía, S.A.	Spain	Energy	95.00	95.00	EY	F
Cantaber Generación Eólica, S.L.	Spain	Energy	69.01	69.01	EY	F
Ciener, S.A.U.	Spain	Holding	100.00	100.00	EY	F
Desarrollo de Energías Renovables de La Rioja, S.A.	Spain	Energy	40.51	40.51	EY	E
Ecobarcial, S.A.	Spain	Energy	43.78	43.78	EY	E
Electra de Malvana, S.A.	Spain	Energy	48.00	48.00	-	E
Electra Sierra de los Castillos, S.L.	Spain	Energy	97.00	97.00	-	F
Electra Sierra de San Pedro, S.A.	Spain	Energy	80.00	80.00	-	F
Eléctricas de la Alcarria, S.L.	Spain	Energy	90.00	90.00	-	F
Eme Hueneja Cuatro, S.L.	Spain	Energy	100.00	100.00	-	F
Energías de Castilla y León, S.A.	Spain	Energy	85.50	85.50	EY	F
Energías Ecológicas de Tenerife, S.A. (3)	Spain	Energy	50.00	50.00	-	F
Energías Eólicas de Cuenca, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Energías Renovables de la Región de Murcia, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Eólica Campollano, S.A.	Spain	Energy	25.00	25.00	KPMG	E
Eólica 2000, S.L.	Spain	Holding	51.00	51.00	EY	F
Eólicas de Euskadi, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Iberdrola Energía Solar de Puertollano, S.A.	Spain	Energy	90.00	90.00	EY	F
Iberdrola Renewables Solutions, S.A.U.	Spain	Energy	100.00	100.00	-	F
Iberdrola Renovables Galicia, S.A.U.	Spain	Holding	100.00	100.00	EY	F
Iberdrola Renovables Andalucía, S.A.U.	Spain	Holding	100.00	100.00	EY	F
Iberdrola Renovables Aragón, S.A.U.	Spain	Holding	100.00	100.00	EY	F
Iberdrola Renovables Canarias, S.A.U.	Spain	Holding	100.00	100.00	-	F
Iberdrola Renovables Castilla – La Mancha, S.A.U.	Spain	Holding	100.00	100.00	EY	F
Iberdrola Renovables Castilla y León, S.A.	Spain	Holding	95.00	95.00	EY	F
Iberdrola Renovables Energía, S.A.U.	Spain	Holding	100.00	100.00	EY	F
Iberdrola Renovables La Rioja, S.A. (2)	Spain	Holding	63.55	63.55	EY	E
Ibernova Promociones, S.A.U.	Spain	Holding	100.00	100.00	EY	F
Iberjalón, S.A.	Spain	Energy	80.00	80.00	-	F
Minicentrales del Tajo, S.A.	Spain	Energy	66.58	66.58	EY	F
Molinos de La Rioja, S.A.	Spain	Energy	42.37	42.37	EY	E
Molinos del Cidacos, S.A.	Spain	Energy	31.78	31.78	EY	E
Parque Eólico Cruz del Carrutero, S.L.	Spain	Energy	76.00	76.00	EY	F
Peache Energías Renovables, S.A.	Spain	Energy	95.00	95.00	-	F
Producciones Energéticas Asturianas, S.L.	Spain	Energy	80.00	80.00	EY	F
Producciones Energéticas de Castilla y León, S.A. (2)	Spain	Energy	85.50	85.50	EY	E
Renovables de la Ribera, S.L. (5)	Spain	Energy	50.00	50.00	-	-
Sistemas Energéticos Altamira, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Sistemas Energéticos Chandrexa, S.A.	Spain	Energy	96.07	96.07	EY	F
Sistemas Energéticos del Moncayo, S.A.	Spain	Energy	75.00	75.00	EY	F
Sistemas Energéticos La Gomera, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Sistemas Energéticos La Higuera, S.A.	Spain	Energy	55.00	55.00	EY	F
Sistemas Energéticos de la Linera, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Sistemas Energéticos La Muela, S.A.	Spain	Energy	80.00	80.00	EY	F
Sistemas Energéticos Mas Garullo, S.A.	Spain	Energy	78.00	78.00	EY	F
Sistemas Energéticos Nacimiento, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Sistemas Energéticos Tacica de Plata, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Sistemas Energéticos Torralba, S.A.	Spain	Energy	60.00	60.00	EY	F

Company	Address	Activity	Percentage of direct or indirect participation		Auditor	Method (*)
			12.31.16	12.31.15		
Sistemas Energetics Savalla del Comtat, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Sociedad Gestora de Parques Eólicos de Andalucía, S.A.	Spain	Energy	63.91	63.91	EY	F
Sotavento Galicia, S.A. ⁽⁴⁾	Spain	Energy	8.00	8.00	Others	E
United Kingdom						
Celtpower, Ltd.	United Kingdom	Energy	50.00	50.00	KPMG	E
Coldham Windfarm, Ltd.	United Kingdom	Energy	80.00	80.00	EY	F
East Anglia Offshore Wind, Ltd.	United Kingdom	Energy	50.00	50.00	EY	E
East Anglia One, Ltd.	United Kingdom	Energy	100.00	100.00	-	F
East Anglia Three, Ltd.	United Kingdom	Energy	100.00	50.00	-	F
Morecambe Wind, Ltd.	United Kingdom	Energy	50.00	50.00	EY	E
ScottishPower Renewable Energy, Ltd.	United Kingdom	Holding	100.00	100.00	EY	F
ScottishPower Renewables (WODS), Ltd.	United Kingdom	Energy	100.00	100.00	EY	F
ScottishPower Renewables UK, Ltd.	United Kingdom	Energy	100.00	100.00	EY	F
Rest of the World						
Iberdrola Renovables Offshore Deutschland, GmbH.	Germany	Energy	100.00	100.00	EY	F
Iberdrola Renovables Deutschland, GmbH.	Germany	Energy	100.00	100.00	EY	F
ScottishPower Hazelwood, Pty. Ltd.	Australia	Holding	100.00	100.00	-	-
Iberdrola Renewables Bulgaria, EOOD.	Bulgaria	Energy	100.00	100.00	-	F
Iberdrola Renewables Canada, Ltd.	Canada	Holding	100.00	100.00	-	F
Rokas Aeoliki Cyprus, Ltd.	Cyprus	Energy	74.82	74.82	EY	F
Ailes Marine, S.A.S.	France	Energy	70.00	70.00	EY	F
Iberdrola Renovables France, S.A.S.	France	Energy	100.00	100.00	EY	F
C. Rokas Industrial Commercial Company, S.A.	Greece	Holding	99.76	99.76	EY	F
PPC Renewables Rokas, S.A.	Greece	Energy	50.88	50.88	EY	F
Rokas Aeoliki Achladotopos, S.A.	Greece	Energy	99.63	99.63	EY	F
Rokas Aeoliki Macedonia I, S.A.	Greece	Energy	99.76	99.76	EY	F
Rokas Aeoliki Macedonia II, S.A.	Greece	Energy	99.76	99.76	EY	F
Rokas Aeoliki Peloponnisos I, S.A.	Greece	Energy	99.76	99.76	EY	F
Rokas Aeoliki Peloponnisos II, S.A.	Greece	Energy	99.76	99.76	EY	F
Rokas Aeoliki Thraki III, S.A.	Greece	Energy	99.61	99.61	EY	F
Rokas Aeoliki Vorios Ellas I, S.A.	Greece	Energy	99.76	99.76	EY	F
Rokas Aeoliki Vorios Ellas II, S.A.	Greece	Energy	99.76	99.76	EY	F
Rokas Aeolos, Ltd.	Greece	Energy	99.76	99.76	EY	F
Rokas Construction, S.A.	Greece	Energy	99.76	99.76	EY	F
Rokas Energy, S.A.	Greece	Energy	99.72	99.72	EY	F
Rokas Hydroelectric, S.A.	Greece	Energy	99.76	99.76	EY	F
Iberdrola Renovables Magyarorszag, KFT.	Hungary	Holding	75.00	75.00	EY	F
Eólica Lucana, S.R.L.	Italy	Energy	100.00	100.00	EY	F
Iberdrola Renovables Italia, S.p.A.	Italy	Holding	100.00	100.00	-	F
Societa Energie Rinnovabili 2, S.p.A.	Italy	Energy	50.00	50.00	-	E
Uppm-Rokas Cranes, S.I.A. ⁽⁵⁾	Latvia	Energy	49.88	49.88	-	-
Iberdrola Renovables Portugal, S.A.	Portugal	Holding	100.00	100.00	EY	F
Parque Eólico da Serra do Alvao, S.A.	Portugal	Energy	100.00	100.00	EY	F
Eolica Dobrogea One, S.R.L.	Romania	Energy	100.00	100.00	EY	F
Iberdrola Renewables Romania, S.R.L.	Romania	Holding	100.00	100.00	EY	F

Company	Address	Activity	Percentage of direct or indirect participation		Auditor	Method (*)
			12.31.16	12.31.15		
Mexico						
BII NEE Stipa Energía Eólica, S.A. de C.V.	Mexico	Energy	99.99	99.99	EY	F
Corporativo Iberdrola Renovables México, S.A. de C.V.	Mexico	Services	100.00	100.00	EY	F
Energías Renovables Venta III, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Eólica Dos Arbolitos, S.A.P.I. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Renovables Centro, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Renovables del Bajío, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Renovables del Irapuato, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Renovables del Zacatecas, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Renovables México, S.A. de C.V.	Mexico	Holding	100.00	100.00	EY	F
Iberdrola Renovables Noroeste, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Iberdrola Renovables Norte, S.A. de C.V.	Mexico	Energy	100.00	100.00	EY	F
Parque Industrial de Energía Renovables, S.A. de C.V.	Mexico	Energy	51.00	51.00	-	F
Parques Ecológicos de México, S.A. de C.V.	Mexico	Energy	99.99	99.99	EY	F
Pier II Quecholac Felipe Angeles, S.A. de C.V.	Mexico	Energy	51.00	51.00	EY	F
Pier IV, S.A. de C.V.	Mexico	Energy	51.00	51.00	-	F
Proyecto Alternativa Energética de México, S.A. de C.V.	Mexico	Energy	100.00	-	EY	-
Servicios Operación Eoloeléctrica de México, S.A. de C.V.	Mexico	Services	100.00	100.00	EY	F
Brazil						
Arizona 1 Energia Renovável, S.A.	Brazil	Energy	69.50	69.50	EY	F
Caetité 1 Energia Renovável, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Caetité 2 Energia Renovável, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Caetité 3 Energia Renovável, S.A.	Brazil	Energy	69.50	69.50	EY	F
Calango 1 Energia Renovável, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Calango 2 Energia Renovável, S.A.	Brazil	Energy	69.50	69.50	EY	F
Calango 3 Energia Renovável, S.A.	Brazil	Energy	69.50	69.50	EY	F
Calango 4 Energia Renovável, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Calango 5 Energia Renovável, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Calango 6 Energia Renovável, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Canoas Energia Renovável, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Elektro Renováveis do Brasil, S.A. (previously Iberdrola Renováveis do Brasil, S.A.)	Brazil	Energy	100.00	100.00	EY	F
Energias Renováveis do Brasil, S.A.	Brazil	Energy	100.00	100.00	EY	F
FE Participações, S.A.	Brazil	Energy	69.50	69.50	EY	F
Força Eolica do Brasil 1, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Força Eolica do Brasil 2, S.A.	Brazil	Energy	69.50	69.50	EY	F
Força Eolica do Brasil, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Lagoa I, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Lagoa II, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Mel 2 Energía Renovável, S.A.	Brazil	Energy	69.50	69.50	EY	F
Santana 1, Energía Renovável, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Santana 2, Energía Renovável, S.A. ⁽²⁾	Brazil	Energy	69.50	69.50	EY	E
Innovation						
Algaenergy, S.A. ⁽⁵⁾	Spain	Energy	17.81	19.32	KPMG	-
Arborea Intellbird.S.L. ⁽⁴⁾	Spain	Services	18.89	18.89	-	E
Atten2 Advanced Monitoring Technologies, S.L.	Spain	Services	21.22	18.29	-	E
GDES Technology for services, S.L.	Spain	Services	40.00	40.00	-	E
Iberdrola Servicios de Innovación, S.L.	Spain	Services	100.00	100.00	-	F
Inversiones Financieras Perseo, S.L.	Spain	Holding	100.00	100.00	EY	F
Oceantec Energías Marinas, S.L.	Spain	Energy	44.39	44.39	EY	E
Iberdrola QSTP, LLC	Qatar	Energy	100.00	-	-	F

Company	Address	Activity	Percentage of direct and indirect participation		Auditor	Method(*)
			12.31.16	12.31.15		
NETWORK BUSINESS						
Spain						
Anselmo León Distribución, S.L. ⁽¹⁾	Spain	Energy	100.00	100.00	-	E
Anselmo León, S.A.U. ⁽¹⁾	Spain	Holding	100.00	100.00	-	E
Bidelek Sareak, A.I.E. ⁽²⁾	Spain	Others	54.00	54.00	EY	E
Distribuidora de Energía Eléctrica Enrique García Serrano, S.L. ⁽¹⁾	Spain	Energy	100.00	100.00	-	E
Distribuidora Eléctrica Navasfrías, S.L. ⁽¹⁾	Spain	Energy	100.00	100.00	-	E
Eléctrica Conquense Distribución , S.A.	Spain	Energy	53.59	53.59	EY	F
Eléctrica Conquense, S.A.	Spain	Energy	53.59	53.59	EY	F
Electro-Distribuidora Castellano-Leonesa, S.A. ⁽¹⁾	Spain	Energy	100.00	100.00	-	E
Empresa Eléctrica del Cabriel, S.L. ⁽¹⁾	Spain	Energy	100.00	100.00	-	E
Herederos María Alonso Calzada – Venta de Baños, S.L. ⁽¹⁾	Spain	Energy	100.00	100.00	-	E
San Cipriano de Rueda Distribución, S.L. (previously Hidroeléctrica de San Cipriano de Rueda, S.L.)	Spain	Energy	100.00	100.00	-	E
Iberdrola Distribución de Gas, S.A.U.	Spain	Inactive	100.00	100.00	-	F
Iberdrola Distribución Eléctrica, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Iberdrola Infraestructuras y Servicios de Redes, S.A. ⁽⁵⁾	Spain	Inactive	100.00	100.00	-	-
Iberdrola Redes España, S.A.U.	Spain	Energy	100.00	100.00	EY	F
Sociedad Distribuidora de Electricidad de Elorrio, S.A. ⁽¹⁾	Spain	Energy	97.95	96.86	-	E
United Kingdom						
Manweb Services, Ltd.	United Kingdom	Energy	100.00	100.00	EY	F
NGET/SPT Upgrades, Ltd.	United Kingdom	Energy	50.00	50.00	EY	E
Scottish Power Energy Networks Holdings, Ltd.	United Kingdom	Holding	100.00	100.00	EY	F
SP Distribution, Plc.	United Kingdom	Energy	100.00	100.00	EY	F
SP Gas, Ltd.	United Kingdom	Inactive	100.00	100.00	-	F
SP Manweb, Plc.	United Kingdom	Energy	100.00	100.00	EY	F
SP Network Connections, Ltd.	United Kingdom	General Asset Networking	100.00	100.00	EY	F
SP Power Systems, Ltd.	United Kingdom	Asset Management Services	100.00	100.00	EY	F
SP Transmission, Plc.	United Kingdom	Energy	100.00	100.00	EY	F
Brazil						
Afluente Geraçao de Energia Elétrica, S.A.	Brazil	Energy	42.76	42.76	EY	E
Afluente Transmissao de Energia Elétrica, S.A.	Brazil	Energy	42.76	42.76	EY	E
Baguari Geraçao de Energia Elétrica, S.A.	Brazil	Energy	39.00	39.00	EY	E
Bahia PCH I, S.A.	Brazil	Energy	39.00	39.00	EY	E
Bahia PCH II, S.A. Bahía Pequeña C. Hidroeléctrica	Brazil	Energy	39.00	39.00	PWC	E
Bahia PCH III, S.A. Bahía Geraçao de Energia	Brazil	Energy	39.00	39.00	PWC	E
Belo Monte Participações, S.A.	Brazil	Energy	39.00	39.00	EY	E
Capuava Energy, Ltda.	Brazil	Energy	39.00	39.00	-	E
Companhia de Eletricidade do Estado do Bahia, S.A.	Brazil	Energy	37.57	37.57	EY	E
Companhia Energética de Pernambuco, S.A.	Brazil	Energy	34.96	34.96	EY	E
Companhia Energetica do Rio Grande do Norte, S.A.	Brazil	Energy	35.67	35.67	EY	E
Companhia Hidreletrica Teles Pires, S.A. ⁽⁴⁾	Brazil	Energy	19.89	19.54	EY	E
Elektro Comercializadora de Energia Ltda.	Brazil	Energy	100.00	100.00	EY	F
Elektro Holding, S.A. (previously Iberdrola Brasil, S.A.)	Brazil	Holding	100.00	100.00	EY	F
Elektro Operação e Manutenção, Ltda. (previously Iberdrola Operação e Manutenção, Ltda.)	Brazil	Services	99.99	99.99	EY	F
Elektro Redes, S.A. (previously Elektro Electricidade e Serviços, S.A.)	Brazil	Energy	99.68	99.68	EY	F

Company	Address	Activity	Percentage of direct and indirect participation		Auditor	Method(*)
			12.31.16	12.31.15		
Energetica Aguas da Pedra, S.A. ⁽⁴⁾	Brazil	Energy	19.89	19.89	PWC	E
Energética Corumba III, S.A. ⁽⁴⁾	Brazil	Energy	9.75	6.08	Others	E
Energyworks do Brasil, Ltda.	Brazil	Energy	39.00	39.00	EY	E
Geração Ceu Azul, S.A.	Brazil	Energy	39.00	39.00	EY	E
Geração CIII, S.A.	Brazil	Energy	39.00	39.00	EY	E
Goiás Sul Geração de Energia, S.A.	Brazil	Energy	39.00	39.00	EY	E
Itapebí Geração de Energia, S.A.	Brazil	Energy	39.00	39.00	EY	E
Lanmóvil Amara Celular da Bahia Ltd. (Lanmara) ⁽¹⁾	Brazil	Wholesale/ Retail	65.00	65.00	-	-
Meridiano 1 Energia renovavel, S.A.	Brazil	Energy	39.00	39.00	PWC	E
Meridiano 2 Energia renovavel, S.A.	Brazil	Energy	39.00	39.00	PWC	E
Meridiano 3 Energia renovavel, S.A.	Brazil	Energy	39.00	39.00	PWC	E
Meridiano 4 Energia renovavel, S.A.	Brazil	Energy	39.00	39.00	PWC	E
Meridiano 5 Energia renovavel, S.A.	Brazil	Energy	39.00	39.00	PWC	E
Meridiano 6 Energia renovavel, S.A.	Brazil	Energy	39.00	39.00	PWC	E
NC Energia, S.A.	Brazil	Energy	39.00	39.00	EY	E
Neenergia Investimentos, S.A.	Brazil	Services	39.00	39.00	EY	E
Neenergia Operação e Manutenção, S.A.	Brazil	Services	39.00	39.00	EY	E
Neenergia Servicios, Ltd.	Brazil	Services	39.00	39.00	EY	E
Neenergia, S.A.	Brazil	Holding	39.00	39.00	EY	E
Norte Energia, S.A. ⁽⁴⁾	Brazil	Energy	3.90	3.90	PWC	E
PCH Alto do Rio Grande, S.A.	Brazil	Energy	39.00	39.00	-	E
Potiguar Sul Transmissão de Energia, S.A.	Brazil	Energy	39.00	39.00	EY	E
Rio PCH I, S.A.	Brazil	Energy	27.30	27.30	PWC	E
S.E. Narandiba, S.A.	Brazil	Energy	39.00	39.00	EY	E
Sever RJ Participacoes S.A.	Brazil	Energy	39.00	39.00	PWC	E
Soumaya RJ Participacoes S.A.	Brazil	Energy	39.00	39.00	PWC	E
Tacca RJ Participacoes S.A.	Brazil	Energy	39.00	39.00	PWC	E
Titanum RJ Participacoes S.A.	Brazil	Energy	39.00	39.00	PWC	E
Teles Pires Participações, S.A. ⁽⁴⁾	Brazil	Holding	19.72	19.72	PWC	E
Termopernambuco, S.A.	Brazil	Energy	39.00	39.00	PWC	E
Garter Properties, Inc.	Brit. Virgin Islands	Inactive	39.00	39.00	PWC	E

Company	Address	Activity	Percentage of direct or indirect participation		Auditor	Method(*)
			12.31.16	12.31.15		
AVANGRID						
Deregulated Business						
Caledonia Energy Partners, LLC	USA	Energy	81.50	81.50	-	F
E.O. Resources, LLC	USA	Energy	81.50	81.50	-	F
Enstor Energy Services, LLC (previously Iberdrola Energy Services, LLC)	USA	Energy	81.50	81.50	-	F
Enstor Gas, LLC (previously Iberdrola Energy Holding, LLC)	USA	Holding	81.50	81.50	-	F
Enstor Grama Ridge Storage and Trasportation, LLC.	USA	Energy	81.50	81.50	-	F
Enstor Houston Hub Storage and Transportation, Ltd.	USA	Energy	81.50	81.50	-	F
Enstor Inc.	USA	Holding	81.50	81.50	-	F
Enstor Katy Storage and Transportation, LLC	USA	Energy	81.50	81.50	-	F
Enstor Louisiana, LLC	USA	Energy	81.50	81.50	-	F
Enstor Operating Company, LLC	USA	Holding	81.50	81.50	-	F
Enstor Sundance Storage and Transportation, LLC	USA	Energy	81.50	81.50	-	F
Enstor Waha Storage and Transportation, LLC	USA	Energy	81.50	81.50	-	F
Freebird Assets Inc.	USA	Holding	81.50	81.50	-	F
Freebird Gas Storage, LLC	USA	Energy	81.50	81.50	-	F
Gemini Capital, LLC	USA	Energy	81.50	81.50	-	F
Renewable Business						
Aeolus Wind Power II, LLC ⁽⁶⁾	USA	Holding	61.13	61.13	EY	F
Aeolus Wind Power III, LLC ⁽⁶⁾	USA	Holding	61.13	61.13	EY	F
Aeolus Wind Power IV, LLC ⁽⁶⁾	USA	Holding	61.13	61.13	EY	F
Atlantic Renewable Energy Corporation	USA	Holding	81.50	81.50	-	F
Atlantic Renewable Projects II, LLC ⁽⁶⁾	USA	Holding	61.13	61.13	-	F
Atlantic Renewable Projects, LLC ⁽⁶⁾	USA	Holding	61.13	61.13	-	F
Atlantic Wind, LLC	USA	Holding	81.50	81.50	-	F
Aurora Solar, LLC	USA	Energy	81.50	81.50	-	F
Avangrid Arizona Renewables, LLC (previously Iberdrola Arizona Renewables, LLC)	USA	Energy	81.50	81.50	-	F
Avangrid Logistic Services, LLC (previously Iberdrola Logistic Services, LLC)	USA	Holding	81.50	81.50	-	F
Avangrid Renewables Holdings, Inc. (previously Iberdrola Renewables Holdings, Inc.)	USA	Holding	81.50	81.50	-	F
Avangrid Renewables, LLC (previously Iberdrola Renewables, LLC)	USA	Holding	81.50	81.50	-	F
Avangrid Texas Renewables, LLC (previously Iberdrola Texas Renewables, LLC)	USA	Energy	81.50	81.50	-	F
Bakeoven Wind, LLC	USA	Energy	81.50	81.50	-	F
Barton Windpower, LLC	USA	Energy	81.50	81.50	-	F
Big Horn II Wind Project, LLC	USA	Energy	81.50	81.50	-	F
Big Horn Wind Project, LLC ⁽⁶⁾	USA	Energy	61.13	61.13	-	F
Blue Creek Wind Farm, LLC	USA	Energy	81.50	81.50	-	F
Buffalo Ridge I, LLC	USA	Energy	81.50	81.50	-	F
Buffalo Ridge II, LLC	USA	Energy	81.50	81.50	-	F
Buffalo Ridge III, LLC	USA	Energy	81.50	81.50	-	F
Casselman Wind Power, LLC ⁽⁶⁾	USA	Energy	61.13	61.13	-	F
Deerfield Wind, LLC	USA	Energy	81.50	81.50	-	F
Desert Wind Farm, LLC	USA	Energy	81.50	81.50	-	F
Dillon Wind, LLC	USA	Energy	81.50	81.50	-	F
El Cabo Wind, LLC	USA	Energy	81.50	81.50	-	F
El Cabo Wind Holdings	USA	Holding	81.50	81.50	-	F
Elk River Wind Farm, LLC ⁽⁶⁾	USA	Energy	61.13	61.13	-	F
Elm Creek Wind II, LLC	USA	Energy	81.50	81.50	-	F
Elm Creek Wind, LLC	USA	Energy	81.50	81.50	-	F

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Company	Address	Activity	Percentage of direct or indirect participation		Auditor	Method(*)
			12.31.16	12.31.15		
Farmers City Wind, LLC	USA	Energy	81.50	81.50	-	F
Flat Rock Windpower II, LLC ⁽⁶⁾	USA	Energy	30.56	30.56	EY	E
Flat Rock Windpower, LLC ⁽⁶⁾	USA	Energy	30.56	30.56	EY	E
Flying Cloud Power Partners, LLC	USA	Energy	81.50	81.50	-	F
Goodland Wind, LLC	USA	Energy	81.50	81.50	-	F
Groton Wind, LLC	USA	Energy	81.50	81.50	-	F
Hardscrabble Wind Power, LLC	USA	Energy	81.50	81.50	-	F
Hay Canyon Wind, LLC	USA	Energy	81.50	81.50	-	F
Hazelwood Australia, Inc. ⁽⁵⁾	USA	Holding	81.50	81.50	-	-
Hazelwood Ventures, Inc. ⁽⁵⁾	USA	Holding	81.50	81.50	-	-
Heartland Wind, LLC	USA	Energy	81.50	81.50	-	F
Helix Wind Power Facility, LLC	USA	Energy	81.50	81.50	-	F
Juniper Canyon Wind Power II, LLC	USA	Energy	81.50	81.50	-	F
Juniper Canyon Wind Power, LLC	USA	Energy	81.50	81.50	-	F
Klamath Energy, LLC	USA	Energy	81.50	81.50	-	F
Klamath Generation, LLC	USA	Energy	81.50	81.50	-	F
Klondike Wind Power II, LLC	USA	Energy	81.50	81.50	-	F
Klondike Wind Power III, LLC ⁽⁶⁾	USA	Energy	61.13	61.13	-	F
Klondike Wind Power, LLC	USA	Energy	81.50	73.35	-	F
Lakeview Cogeneration, LLC	USA	Energy	81.50	81.50	-	F
Leaning Juniper Wind Power II, LLC	USA	Energy	81.50	81.50	-	F
Leipsic Wind, LLC	USA	Energy	81.50	81.50	-	F
Lempster Wind, LLC	USA	Energy	81.50	81.50	-	F
Locust Ridge II, LLC	USA	Energy	81.50	81.50	-	F
Locust Ridge Wind Farms, LLC ⁽³⁾	USA	Energy	37.74	37.74	EY	F
Loma Vista, LLC	USA	Energy	81.50	81.50	-	F
Manzana Power Services, Inc.	USA	Services	81.50	81.50	-	F
Manzana Wind, LLC	USA	Energy	81.50	81.50	-	F
Midland Wind, LLC	USA	Energy	81.50	81.50	-	F
Minndakota Wind, LLC ⁽⁶⁾	USA	Energy	61.13	61.13	-	F
Montague Wind Power Facility, LLC	USA	Energy	81.50	81.50	-	F
Moraine Wind II, LLC	USA	Energy	81.50	81.50	-	F
Moraine Wind, LLC	USA	Energy	81.50	73.35	-	F
Mount Pleasant Wind, LLC	USA	Energy	81.50	81.50	-	F
Mountain View Power Partners III, LLC	USA	Energy	81.50	73.35	-	F
New England Wind, LLC	USA	Energy	81.50	81.50	-	F
New Harvest Wind Project, LLC	USA	Energy	81.50	81.50	-	F
Northern Iowa WindPower II, LLC ⁽⁶⁾	USA	Energy	61.13	61.13	-	F
Otter Creek Wind Farm, LLC	USA	Energy	81.50	81.50	-	F
Pacific Harbor Capital, Inc.	USA	Others	81.50	81.50	-	F
Pacific Solar Investments, Inc.	USA	Energy	81.50	81.50	-	F
Pacific Wind Development, LLC	USA	Energy	81.50	81.50	-	F
Pebble Springs Wind, LLC	USA	Energy	81.50	81.50	-	F
Phoenix Wind Power, LLC	USA	Energy	81.50	81.50	-	F
PPM Colorado Wind Ventures, Inc.	USA	Holding	81.50	81.50	-	F
PPM Roaring Brook, LLC	USA	Energy	81.50	81.50	-	F
PPM Technical Services, Inc.	USA	Services	81.50	81.50	-	F
PPM Wind Energy, LLC	USA	Holding	81.50	81.50	-	F
Providence Heights Wind, LLC	USA	Energy	81.50	81.50	-	F
Rugby Wind, LLC	USA	Energy	81.50	81.50	-	F
San Luis Solar, LLC	USA	Energy	81.50	81.50	-	F
ScottishPower Financial Services, Inc.	USA	Holding	81.50	81.50	-	F
ScottishPower Group Holdings Company	USA	Holding	81.50	81.50	-	F
ScottishPower International Group Holdings Company	USA	Holding	81.50	81.50	-	-
Shiloh I Wind Project, LLC ⁽⁶⁾	USA	Energy	61.13	61.13	-	F
South Chestnut, LLC	USA	Energy	81.50	81.50	-	F

Company	Address	Activity	Percentage of direct or indirect participation		Auditor	Method(*)
			12.31.16	12.31.15		
Start Point Wind Project, LLC	USA	Energy	81.50	81.50	-	F
Streator Cayuga Ridge Wind Power, LLC	USA	Energy	81.50	81.50	-	F
Streator Deer Run Wind Farmer, LLC	USA	Energy	81.50	81.50	-	F
Trimont Wind I, LLC ⁽⁶⁾	USA	Energy	61.13	61.13	-	F
Tule Wind, LLC	USA	Energy	81.50	81.50	-	F
Twin Buttes Wind, LLC ⁽⁶⁾	USA	Energy	61.13	61.13	-	F
Twin Buttes Wind II, LLC	USA	Energy	81.50	81.50	-	F
West Valley Leasing Company, LLC	USA	Services	81.50	81.50	-	-
Winnebago Windpower II, LLC	USA	Energy	81.50	81.50	-	F
Winnebago Windpower, LLC	USA	Energy	81.50	81.50	-	F
Network Business						
Avangrid, Inc.	USA	Holding	81.50	81.50	EY	F
Avangrid Enterprises, Inc. (previously Iberdrola USA Enterprises, Inc.)	USA	Holding	81.50	81.50	-	F
Avangrid Management Company, LLC (previously Iberdrola USA Group, LLC)	USA	Holding	81.50	81.50	-	F
Avangrid Service Company (previously Iberdrola USA Management Corporation)	USA	Services	81.50	81.50	-	F
Avangrid New York TransCo, LLC (previously Iberdrola USA Networks New York TransCo, LLC)	USA	Holding	81.50	81.50	-	F
Avangrid Networks, Inc. (previously Iberdrola USA Networks, Inc.)	USA	Holding	81.50	81.50	EY	F
Avangrid Solutions, Inc. (previously Iberdrola USA Solutions, Inc.)	USA	Marketing	81.50	81.50	-	F
Berkshire Energy Resources	USA	Holding	81.50	81.50	PWC	F
Cayuga Energy, Inc.	USA	Energy	81.50	81.50	-	F
Central Maine Power Company	USA	Electricity	81.50	81.50	EY	F
Chester SVC Partnership ⁽³⁾	USA	Electricity	40.75	40.75	EY	F
CMP Group, Inc.	USA	Holding	81.50	81.50	-	F
CNE Energy Services Group, LLC	USA	Services	81.50	81.50	-	F
CNE Peaking, LLC	USA	Services	81.50	81.50	-	F
Connecticut Energy Corporation	USA	Holding	81.50	81.50	PWC	F
Connecticut Natural Gas Corporation	USA	Gas	81.50	81.50	-	F
CTG Resources, Inc.	USA	Holding	81.50	81.50	PWC	F
GCE Holding, LLC	USA	Holding	40.75	40.75	-	-
GenConn Devon, LLC	USA	Generation	40.75	40.75	-	-
GenConn Energy, LLC	USA	Generation	40.75	40.75	-	-
GenConn Middletown, LLC	USA	Generation	40.75	40.75	-	-
Maine Electric Power Company, Inc.	USA	Energy	63.80	63.80	-	F
Maine Natural Gas Corporation	USA	Gas	81.50	81.50	EY	F
Maine Yankee Atomic Power Company ⁽⁵⁾	USA	Electricity	30.97	30.97	-	-
MaineCom Services	USA	Telecommunications	81.50	81.50	-	F
New York State Electric & Gas Corporation	USA	Electricity and Gas	81.50	81.50	EY	F
NORVARCO	USA	Holding	81.50	81.50	-	F
Nth Power Technologies Fund I, LP. ⁽⁵⁾	USA	Others	21.92	21.92	-	-
RGS Energy Group, Inc.	USA	Holding	81.50	81.50	-	F
Rochester Gas and Electric Corporation	USA	Electricity and Gas	81.50	81.50	EY	F
South Glens Falls Energy, LLC ⁽⁵⁾	USA	Energy	69.28	69.28	-	-
TEN Transmission Company	USA	Gas	81.50	81.50	-	F
The Berkshire Gas Company	USA	Gas	81.50	81.50	-	F
The Southern Connecticut Gas Company (SCG)	USA	Gas	81.50	81.50	-	F
The Union Water Power Company	USA	Services	81.50	81.50	-	F
The United Illuminating Company	USA	Energy	81.50	81.50	PWC	F
Thermal Energies, Inc	USA	Inactive	81.50	81.50	-	-
Total Peaking Services, LLC	USA	Services	81.50	81.50	-	F

Company	Address	Activity	Percentage of direct or indirect participation		Auditor	Method(*)
			12.31.16	12.31.15		
UIL Distributed Resources	USA	Services	81.50	81.50	-	F
UIL Group, LLC	USA	Holding	81.50	-	-	F
UIL Holdings Corporation	USA	Holding	81.50	81.50	PWC	F
United Capital Investments	USA	Inactive	81.50	81.50	-	F
United Resources, Inc.	USA	Holding	81.50	81.50	-	F
WGP Acquisition, LLC	USA	Inactive	81.50	81.50	-	-
Xcelcom, Inc.	USA	Inactive	81.50	81.50	-	F
Xcal Services, Inc.	USA	Inactive	81.50	81.50	-	-

OTHER BUSINESSES

Engineering

Adícora Servicios de Ingeniería, S.L.U.	Spain	Engineering	100.00	100.00	-	F
Empresarios Agrupados Internacional, S.A.	Spain	Engineering	25.46	25.46	PWC	E
Empresarios Agrupados, A.I.E.	Spain	Engineering	25.46	25.46	PWC	E
Ghesa Ingeniería y Tecnología, S.A.	Spain	Engineering	41.18	41.18	PWC	E
Iberdrola Ingeniería de Explotación, S.A.U.	Spain	Engineering	100.00	100.00	-	F
Iberdrola Ingeniería y Construcción, S.A.U.	Spain	Engineering	100.00	100.00	EY	F
Ingeniería, Estudios y Construcciones, S.A.	Spain	Engineering	100.00	100.00	-	F
Iberdrola Engineering and Construction Saudi Arabia, LLC	Saudi Arabia	Engineering	100.00	100.00	-	F
Iberdrola Construção e Serviços, Ltd.	Brazil	Engineering	100.00	100.00	-	F
Iberdrola Energy Projects Canada Corporation	Canada	Engineering	100.00	100.00	-	F
Iberdrola Ingeniería y Construcción Costa Rica, S.A. ⁽⁵⁾	Costa Rica	Engineering	100.00	100.00	-	F
Iberdrola Energy Project, Inc.	USA	Engineering	100.00	100.00	-	F
Iberinco Hellas Techniki kai Kataskevastiki EPE	Greece	Engineering	100.00	100.00	-	F
Iberdrola Ingegneria e Costruzioni Italia, SRL.	Italy	Engineering	100.00	100.00	-	F
Enermón S.A. de C.V.	Mexico	Engineering	100.00	100.00	EY	F
Iberdrola Ingeniería y Construcción México, S.A. de C.V.	Mexico	Engineering	100.00	100.00	EY	F
Iberservicios, S.A. de C.V.	Mexico	Engineering	100.00	100.00	EY	F
Iberdrola Engineering and Construction Poland, SP Z.O.O.	Poland	Engineering	100.00	100.00	EY	F
Iberdrola Engenharia e Construção Portugal, Unipessoal Lda.	Portugal	Engineering	100.00	100.00	-	F
Iberdrola Engineering and Construction Networks, Ltd.	United Kingdom	Engineering	100.00	100.00	EY	F
Iberdrola Engineering and Construction UK, Ltd.	United Kingdom	Engineering	100.00	100.00	EY	F
Iberdrola Engineering and Construction Ro, SRL.	Romania	Engineering	100.00	100.00	-	F
Iberdrola Inzhiniring I Stroiteistvo, LLC	Russia	Engineering	100.00	100.00	EY	F
Iberdrola Engineering and Construction South Africa	South Africa	Engineering	100.00	100.00	EY	F
Iberdrola Ingeniería y Construcción Venezuela, S.A.	Venezuela	Engineering	99.81	99.81	EY	F

Real Estate

Arrendamiento de Viviendas Protegidas Siglo XXI, S.L.	Spain	Real Estate	100.00	100.00	-	F
Camarate Golf, S.A.	Spain	Real Estate	26.00	26.00	Deloitte	E
Fiuna, S.A.	Spain	Real Estate	100.00	70.00	PWC	F
Iberdrola Inmobiliaria Patrimonio, S.A.U.	Spain	Real Estate	100.00	100.00	EY	F
Iberdrola Inmobiliaria, S.A.	Spain	Real Estate	100.00	100.00	EY	F
Promotora la Castellana de Burgos, S.A.	Spain	Real Estate	100.00	100.00	EY	F
Urbanizadora Marina de Cope, S.L.	Spain	Real Estate	80.00	80.00	EY	F
Iberdrola Inmobiliaria Real State Investment, EOOD	Bulgaria	Real Estate	100.00	100.00	-	F
Desarrollos Inmobiliarias Laguna del Mar, S.A. de C.V.	Mexico	Real Estate	100.00	100.00	EY	F
Promociones La Malinche, S.A. de C.V.	Mexico	Real Estate	50.00	50.00	-	E

Company	Address	Activity	Percentage of direct or indirect participation		Auditor	Method(*)
			12.31.16	12.31.15		
Other Businesses						
Amara, S.A.U. ⁽¹⁾	Spain	Services and material merchandising	100.00	100.00	EY	E
Subgrupo Corporación IBV Participaciones Empresariales	Spain	Inactive	50.00	50.00	Deloitte	E
Gamesa Corporación Tecnológica, S.A. ⁽⁴⁾	Spain	Holding	19.69	19.69	EY	E
Iberdrola Inversiones 2010, S.A.U.	Spain	Holding	100.00	100.00	-	F
Iberdrola Participaciones, S.A. (previously Iberdrola Redes, S.A.)	Spain	Holding	100.00	100.00	-	F
Investigación y Desarrollo de Equipos Avanzados, S.A.U. ⁽¹⁾	Spain	Services	100.00	100.00	-	E
Keytech Sistemas Integrales, S.A.	Spain	Security Systems	37.00	37.00	-	E
Amara Brasil, Ltd. ⁽¹⁾	Brazil	Services	100.00	100.00	EY	E
Ergytech Inc. ⁽¹⁾	USA	Purchase agent	100.00	100.00	EY	E
Amergy Mexicana, S.A. de C.V. ⁽¹⁾	Mexico	Wholesale /Retail	100.00	100.00	EY	E
Amergy Servicios de México S.A. de C.V. ⁽¹⁾	Mexico	Services	99.00	99.00	EY	E
CORPORATION						
CarteraPark, S.A.U. ⁽⁵⁾	Spain	Inactive	100.00	100.00	-	-
Iberdrola Corporación, S.A. ⁽⁵⁾	Spain	Inactive	100.00	100.00	-	-
Iberdrola España, S.A.U.	Spain	Holding	100.00	100.00	EY	F
Iberdrola Energía, S.A.U.	Spain	Holding	100.00	100.00	EY	F
Iberdrola Financiación, S.A.U.	Spain	Finance	100.00	100.00	EY	F
Iberdrola Finanzas, S.A.U.	Spain	Finance	100.00	100.00	EY	F
Iberdrola Corporate Services, Inc.	USA	Services	100.00	100.00	-	F
Iberdrola International, B.V.	Netherlands	Finance	100.00	100.00	EY	F
Iberdrola Finance Ireland, DAC	Ireland	Finance	100.00	100.00	EY	F
Iberdrola Re, S.A.	Luxembourg	Insurance	100.00	100.00	EY	F
Iberdrola Portugal Electricidade e Gas, S.A.	Portugal	Energy	100.00	100.00	EY	F
Clubcall Telephone Services, Ltd.	United Kingdom	Inactive	100.00	100.00	-	-
Clubline Services, Ltd.	United Kingdom	Inactive	100.00	100.00	-	-
Demon Internet, Ltd.	United Kingdom	Inactive	100.00	100.00	-	-
Manweb Nominees, Ltd.	United Kingdom	Inactive	100.00	100.00	-	-
Manweb Pensions Trustee, Ltd.	United Kingdom	Inactive	100.00	100.00	-	-
Manweb Share Scheme Trustees, Ltd.	United Kingdom	Inactive	100.00	100.00	-	-
Scottish Power UK Holdings, Ltd.	United Kingdom	Holding	100.00	100.00	EY	F
Scottish Power UK, Plc	United Kingdom	Holding	100.00	100.00	EY	F
Scottish Power, Ltd.	United Kingdom	Holding	100.00	100.00	EY	F
ScottishPower Investments, Ltd.	United Kingdom	Holding	100.00	100.00	EY	F
ScottishPower Overseas Holdings, Ltd.	United Kingdom	Holding	100.00	100.00	EY	F
SPW Investments Ltd.	United Kingdom	Holding	100.00	100.00	EY	F
Teledata (Holdings), Ltd.	United Kingdom	Inactive	100.00	100.00	-	-
Teledata (Outsourcing), Ltd.	United Kingdom	Inactive	100.00	100.00	-	-
Teledata Scotland, Ltd.	United Kingdom	Inactive	100.00	100.00	-	-
The CallCentre Service Limited	United Kingdom	Others	100.00	100.00	EY	-
The Information Service, Ltd.	United Kingdom	Inactive	100.00	100.00	-	-

JOINT OPERATIONS OF THE GROUP STRUCTURED THROUGH AN INDEPENDENT VEHICLE FOR THE YEARS 2015 AND 2016

Company	Address	Activity	Percentage of direct or indirect participation	
			12.31.16	12.31.15
<u>DEREGULATED BUSINESS</u>				
Asociación Nuclear Ascó – Vandellós, A.I.E.	Spain	Energy	14.59	14.59
Centrales Nucleares Almaraz – Trillo, A.I.E.	Spain	Energy	51.44	51.44
<u>RENEWABLE BUSINESS</u>				
Infraestructuras de Medinaceli, S.L.	Spain	Energy	39.69	39.69
Sistema Eléctrico de Conexión Hueneja, S.L.	Spain	Energy	47.36	47.36
Colorado Green Holdings, LLC	USA	Energy	40.75	40.75
Colorado Wind Ventures, LLC	USA	Holding	40.75	40.75
<u>OTHER BUSINESSES</u>				
Torre Iberdrola, A.I.E.	Spain	Real Estate	68.10	68.10

GROUP COMPANIES AT 31 DECEMBER 2015 WHICH HAVE LEFT THE PERIMETER IN 2016 AS A RESULT OF DISPOSAL, MERGER OR LIQUIDATION

Company	Address	Activity	Percentage of direct or indirect participation	
			12.31.16	12.31.15
<u>DEREGULATED BUSINESS</u>				
Cofrusa Cogeneración, S.A.	Spain	Energy	-	50.00
Italcogeneración, S.A	Spain	Energy	-	50.00
Caledonian Gas, Ltd.	United Kingdom	Inactive	-	100.00
Manweb Gas, Ltd.	United Kingdom	Inactive	-	100.00
ScottishPower (SOCL), Ltd.	United Kingdom	Inactive	-	100.00
Sterling Collections, Ltd.	United Kingdom	Inactive	-	100.00
<u>RENEWABLES BUSINESS</u>				
Energías Ecológicas de Fuencaliente, S.L.(3)	Spain	Energy	-	50.00
Energías Ecológicas de La Palma, S.A. (3)	Spain	Energy	-	50.00
Iberdrola Renovables Asturias, S.A.U.	Spain	Holding	-	100.00
Productora de Energía Eólica, S.A.U.	Spain	Energy	-	95.00
Haute Marne Energies, S.A.S.	France	Energy	-	51.00
Societa Energie Rinnovabili 1, S.p.A.	Italy	Energy	-	100.00
Societa Energie Rinnovabili, S.p.A.	Italy	Energy	-	100.00
East Anglia Four, Ltd.	United Kingdom	Energy	-	50.00
Eolica Dobrogea (Schweiz) I, GmbH.	Switzerland	Energy	-	100.00
Mugla Ruzgar Enerjisinden Elektrik Uret (5)	Turkey	Energy	-	100.00
Yaprak Ruzgar Enerjisinden Elektrik Uret (5)	Turkey	Energy	-	100.00
<u>NETWORK BUSINESS</u>				
SPD Finance UK, Plc	United Kingdom	Inactive	-	100.00
<u>AVANGRID</u>				
Aeolus Wind Power I, LLC	USA	Holding	-	81.50
Aeolus Wind Power V, LLC	USA	Holding	-	81.50
Aeolus Wind Power VI, LLC	USA	Holding	-	81.50
<u>OTHER BUSINESS</u>				
Iberdrola Engineering and Construction Germany GmbH.	Germany	Engineering	-	100.00
Iberdrola Ingeniería y Construcción Chile, S.A.	Chile	Engineering	-	100.00
Iberdrola Engineering and Construction Middle East, Ltd.	Dubai	Inactive	-	100.00
Iberdrola Magyarország Mernoki es Epitő Korlatolt	Hungary	Engineering	-	100.00
Iberdrola Ingeniería y Construcción Panamá, S.A.	Panama	Engineering	-	100.00
Oceanic Center, S.L.	Spain	Real Estate	-	50.00
<u>CORPORATION</u>				
Camjar Plc	United Kingdom	Inactive	-	100.00
Manweb Contracting Services, Ltd.	United Kingdom	Inactive	-	100.00
Scottish Power Trustees, Ltd.	United Kingdom	Inactive	-	100.00
ScottishPower Share Scheme Trustees, Ltd.	United Kingdom	Inactive	-	100.00
ScottishPower Sharesave Trustees, Ltd.	United Kingdom	Inactive	-	100.00
Scottish Power UK Group, Ltd.	United Kingdom	Holding	-	100.00
SPPT, Ltd.	United Kingdom	Inactive	-	100.00
Telephone Information Services, Plc	United Kingdom	Inactive	-	100.00
Telephone International Media Holding, Ltd.	United Kingdom	Inactive	-	100.00
Telephone International Media, Ltd.	United Kingdom	Inactive	-	100.00
TIM, Ltd.	United Kingdom	Inactive	-	100.00

- (1) Companies that are controlled by the Group but due to their immateriality have been integrated using the equity method. At 31 December 2016, the total aggregate assets value and the profit for the year corresponding to these companies amounts to EUR 87,244 thousand and EUR 6,587 thousand, respectively. On 31 December 2015, the aggregate total assets and results of the corresponding period of such companies amounted to EUR 83,348 thousand and EUR 4,844 thousand, respectively.
- (2) Companies considered joint ventures, accounted for the equity method, where shareholders agreements just grant the right to the net assets of the business.
- (3) Companies, where despite holding a percentage of voting rights less than 51%, the Group holds the control through shareholders agreements.
- (4) Companies where the Group has significant influence despite holding a percentage of voting rights less than 20%, since it is represented theses companies' Board of Directors.
- (5) Companies where the Group holds the control, joint control or significant influence, but given its limited relevance, they have not been included in the consolidation scope.
- (6) The ownership percentage in these companies corresponds to voting rights.

CONSOLIDATED MANAGEMENT REPORT 2016

This management report has been prepared taking into consideration the "Guide of recommendations for the development of management reports of listed companies", published by the CNMV in July 2013.

1. COMPANY'S STANDING

The company has undergone a major transformation over the last 15 years, staying clearly ahead of the energy transition in order to tackle the challenges posed by climate change and the need for clean electricity.

Boasting a track record that spans over 170 years, today Iberdrola is a multinational group leading the energy sector: the company produces and supplies electricity to some 100 million people in the countries in which it operates. Furthermore, the company has become the leader in clean energy —Iberdrola is the first renewable producer amongst European utilities and the cleanest power company in the USA, with almost zero emissions—, it is pioneering the rollout of smart grids and has an energy storage capacity in excess of 4 GW.

This is the result of the combination of its corporate vision —which in 2001 led the company to look ahead to future trends in the sector—, the strategy followed to make this vision a reality, its successful implementation, and the ethical values that have always guided all the group's actions. On this basis, Iberdrola is now embarking on a new stage of growth, supported by a strong investment drive between 2016 and 2020, essentially in regulated businesses or with long-term contracts, which will provide the security, stability and visibility that are the hallmarks of the company's business model. Likewise, Iberdrola will continue maintaining its social commitments, acting as a driver for the growth and generation of employment in the countries where it operates, and creating sustainable value for all its stakeholders.

1.1 Governance system

The purpose of the IBERDROLA Group's business model is the "supply of reliable, high-quality and environment-friendly electricity", by means of a sustainable long-term industrial project.

The model is based on three pillars: a framework of trust based on an advanced governance model; the Mission, Vision and Values of the Iberdrola Group approved by the Board and distinguishing features which make Iberdrola a different company.

The model is made competitive by responsible management of the Company's tangible and intangible assets. To operate with this model, Iberdrola has defined the activities in which it wishes to be a proactive operator, and organises its management on the basis of three global lines of business: Network business, Generation and Sales business and Renewables business, with a Corporation as a central organisational body for the group.

The Corporation formulates the group's strategy and supervises its fulfilment.

Mission, Vision and Values of the Iberdrola Group

The Mission, Vision and Values of the Iberdrola Group constitute its corporate philosophy, inspire and take form in the Corporate Policies Company's By-Laws and in the other rules of the Corporate Governance System, govern the day-to-day activities of the companies of the Group thereof, channel its leadership role in all of its areas of activity, focus its strategy of maximising social dividends, and guide their strategy and all of their actions. The ethical behaviour of all personnel participating in the daily construction of the Company's corporate enterprise.

Mission

The Group's mission is to create value sustainably in carrying out its activities for society, citizens, customers, employees, shareholders, and other stakeholders, as the leading multinational group in the energy sector providing a quality service through the use of environmentally-friendly energy sources, which engages in innovation, leads the process of digital transformation in its area of activity, and is committed to the fight against climate change through all of its business activities, with a social dividend and the generation of employment and wealth, considering its employees to be a strategic asset. Along these lines, we foster their development, training, and measures of reconciliation, favouring a good working environment and equal opportunity. All of the foregoing is within the framework of our strategy of social responsibility and compliance with tax rules. It is what modern business social responsibility calls Shared Value, the sum of all the economic and social values that a company generates.

This mission goes hand in hand with a vision based on the ambition to lead a better future, creating sustainable value with a top-quality service for people and communities in which the Group operates, incorporating twelve values: the creation of sustainable value, ethical principles, good corporate governance and transparency, development of the Group's human resources, social commitment, a sense of belonging, safety and reliability, quality, innovation, protection of the environment, a focus on the customer and institutional loyalty.

The Group's mission, vision and values inspire the contents of the Corporate governance system, a set of internal regulations which, in accordance with current legislation and utilising the corporate autonomy permitted by this legislation, furthers the Company's corporate purpose at the head of a multinational energy leader operating across a range of social and economic contexts, satisfaction of social interests, understood as the common interests of all the shareholders of an independent company determined to carry out its corporate purpose in a sustainable fashion and create long-term value, with a wide-ranging non-controlling and institutional shareholding structure.

To achieve a rules-based system ensuring that the Company's commitment to the Mission, Vision, and Values of the Iberdrola group governs all of its activities, focused on maximising social dividends by generating value in a sustainable manner, Iberdrola has provided itself with a Corporate Governance System, its internal system of rules, which is configured in accordance with applicable law in the exercise of corporate autonomy supported thereby and applies to the entire Group as a whole.

The Corporate Governance System is made up of five blocks of rules, each grouped into a book: the By-Laws, the Mission, Vision, and Values of the Iberdrola group, the Corporate Policies, the governance rules of the corporate decision-making bodies and other internal committees, and the other codes, regulations, and procedures making up and elaborating upon Iberdrola's regulatory compliance system.

This structure ensures the articulation of the rules and principles governing the organisation, operation, and conduct of the Company and its Group under the form of a true regulatory system, which is subject to periodic review and update by the Board of Directors.

The corporate governance system is based on the following principles:

1. Social Dividend and Sustainability
2. Shareholder Engagement
3. Commitment to the Legitimate Interests of Other Stakeholders
4. Plural and balanced composition of the Board of Directors
5. A corporate and governance structure combining decentralised management with proper Group coordination
6. Dedication of the Board of Directors to Setting the Strategy of the Company and of the Group
7. An Efficient System of Checks and Balances
8. Prudent and Balanced Management of Risks
9. Proactive Regulatory Compliance Function

Vision

"We want to be the leading multinational group in the energy sector at the forefront of a better future, sustainably creating value with a quality service for people: customers, citizens, and shareholders (whom we care for and engage in our corporate life) and for the communities in which we carry out our activities, generating employment and wealth (with whom we engage in a constructive dialogue), known for our firm commitment to ethical principles, good corporate governance, and transparency, the safety of people and supply, operational quality and excellence, innovation, protection of the environment, and customer focus. Making it possible thanks to the work of our employees and the people working at our suppliers and collaborators, whom we care for by offering all of our training resources and reconciliation measures for their development and to strengthen equality of opportunity".

Values

The mission and vision of the Group is configured based on a firm commitment to twelve values that all of the Corporate Policies, internal rules, and other internal codes and procedures must follow:

- The sustainable creation of value
- Ethical principles
- Good corporate governance and transparency
- Development of our workforce
- Social commitment
- Sense of belonging
- Safety and reliability
- Quality
- Innovation
- Respect for the environment

- Customer focus
- Institutional loyalty

1.2 IBERDROLA's corporate governance model

Corporate governance system

Iberdrola is a leading multinational group in the energy sector which pursues the creation of value in a sustainable way in the development of its activities for the society, citizens, customers and shareholders, providing quality service by using energy sources that respect the environment, innovating and considering its employees a strategic asset, committed to social return throughout its business, generating employment and wealth in their environment and all of these, going together with its strategy of social responsibility and compliance of tax rules.

The Corporate Governance System is made up of the Mission, Vision, and Values of the Iberdrola group, the By-Laws, the Corporate Policies, the internal corporate governance rules, and the other internal codes and procedures, each of them available on www.iberdrola.com.

The contents are inspired by and based on commitment to best practices in relation to good governance, business ethics and social responsibility in all areas of its activity.

Governance model

This duly makes a distinction between the functions of strategy and supervision and those of management and control:

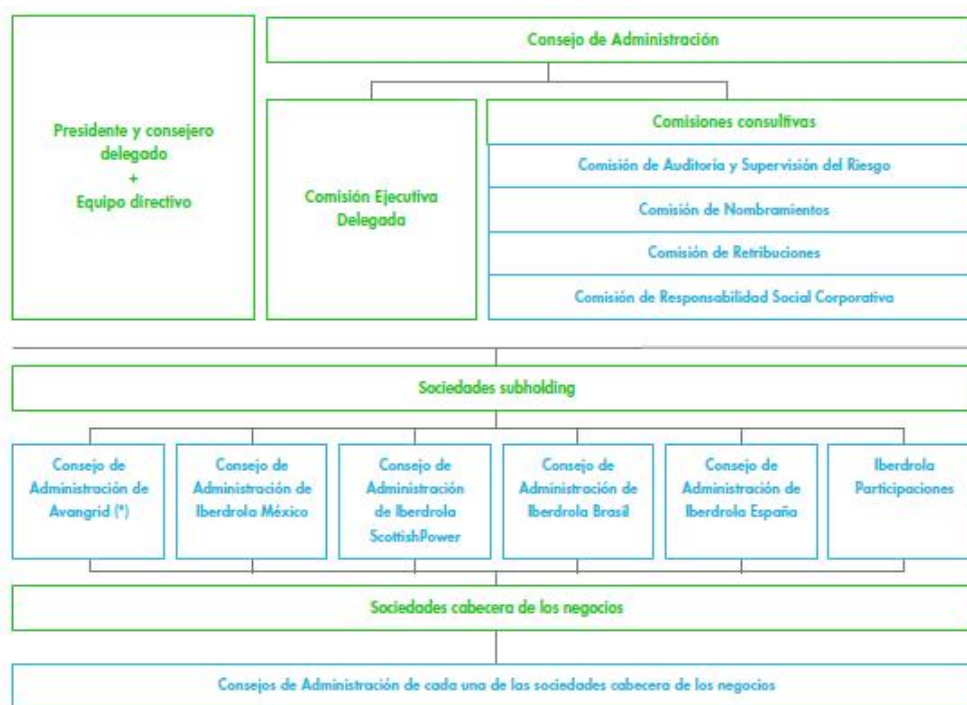
- The Iberdrola Board, composed of a large majority of independent directors, focuses on defining, supervising and monitoring the policies, strategies and guidelines to which the group must adhere.
- The chairman of the Board, the chief executive officer and the rest of the management team are responsible for the group's strategic coordination and organisation, through the distribution, implementation and monitoring of the general strategy and its basic guidelines.
- In all countries in which the group operates, business is organised and strategically coordinated through subholding companies, which group investments in energy business operating in the country concerned and centralise the provision of common services to these companies. The group also has a subholding to handle all non-energy business.

The subholdings have boards with independent directors, and their own Audit and Compliance Committees, Internal Audit departments and Compliance units or departments.

- Parent companies are tasked with ordinary management and effective administration of all lines of business. They also have boards with independent directors and specific management teams.

This structure, which operates along with the group's business model, fosters global integration of the lines of business (Networks, Generation and Sales and Renewables), and focuses on maximising operational efficiency, by implementing best market practices.

Corporate and governance structure of Iberdrola, S.A.



(*) Sociedad cotizada en la Bolsa de Nueva York.

1.3 Scope of activities, sectors and geographical areas

The IBERDROLA Group's economic-financial and operational information has been grouped in the following lines of business: Network business, Generation and Retail businesses, Renewables business, and other businesses. The Corporation includes the costs of the Group's structure (Single Corporation), of the administration services of the corporate areas that are subsequently invoiced to the other companies through specific service agreements.

Given the nature of the activities carried out by the IBERDROLA Group, its organization responds to the strategic business units, rather than product and service lines. These businesses are managed independently, as they respond to different technologies, regulations, and geographic markets (Note 7).

Corporate Structure

The IBERDROLA Group has a decentralised structure and management model to approximate the decision taking to places where they should have effect, through the subholding companies and parent companies of the businesses. In addition, the independence and listed subholding companies' reinforced autonomy are guaranteed.

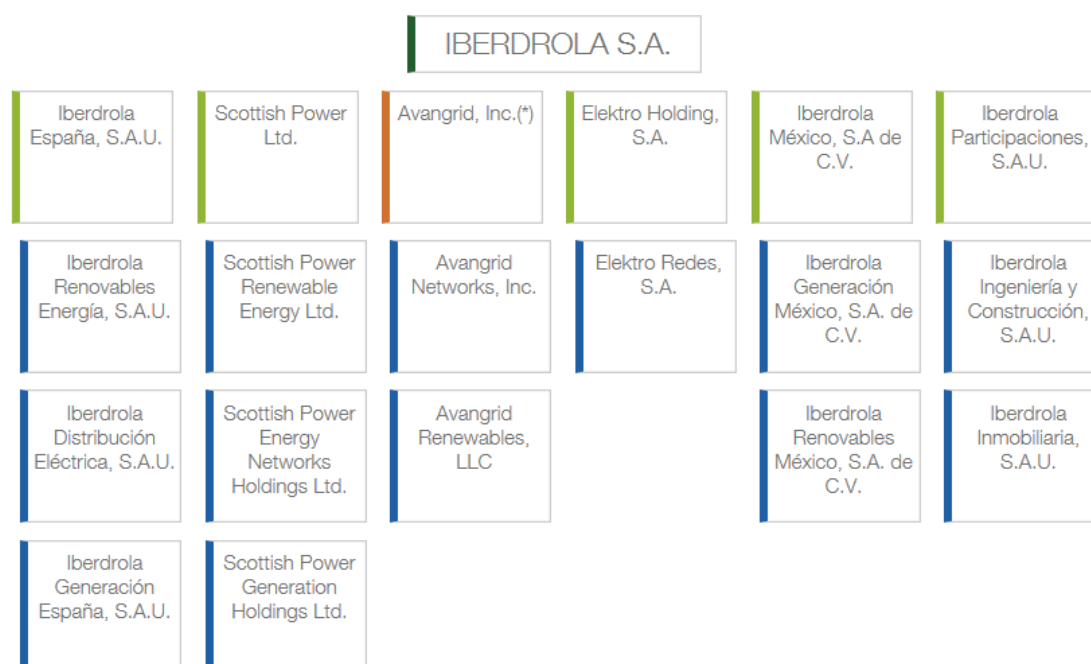
The corporate structure encompasses the Company (IBERDROLA, S.A.), subholding companies and business parent companies.

IBERDROLA, which performs exclusively the function of the parent company, is the company holding the stake of the subholding companies. Such entities group together equity stakes in the energy head of business companies carrying out their activities within the various countries in which the Group operates. This structure is rounded out with a country subholding company that groups together certain equity interests in other entities, including the non-energy head of business companies. One of the main functions of the subholding companies is the centralization of the common services provided to one another, always in accordance with the provisions of the applicable law.

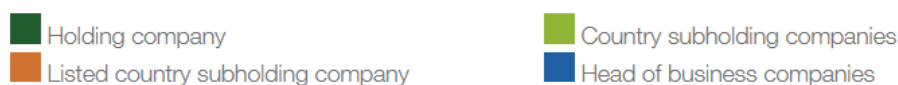
This corporate structure has been successfully deployed in Spain, Mexico, Brazil and the UK, and produces a rapid streamlined process for ordinary management decisions to be taken by business parents, and introduces proper Group coordination, in exercise of the supervisory functions of subholding companies and IBERDROLA.

In the United States of America, the Company holds a majority stake in the subholding company listed on the New York Stock Exchange, Avangrid, Inc. For this company the Corporate governance system contemplates a special system of greater autonomy to properly protect the interests of non-controlling shareholders, boosting vigilance of operations in connection with other Group companies, and this gives it a greater measure of independence to coordinate its investees and run businesses.

Simplified scheme of the corporate structure of the Group



(*) Avangrid, Inc. is 81.50% owned by Iberdrola, S.A.



The Company's and the Group's governance conforms to the structure described above: separates the duties relating to strategy, oversight, and control of the Group as a whole, the duties of organisation and coordination of the businesses in each country and the multinational no-energetic business, as well as those of day-to-day administration and effective management of each business.

It is established on the following bases:

- a) The Board of Directors of the Company, which exclusively exercises holding company duties, has assigned powers relating to the establishment of the Group's policies and strategies and of the basic guidelines for the management thereof, as well as general oversight of the development of such policies, strategies and guidelines and of decisions on matters that are strategically significant at the Group level.

- b) The chairman of the Board of Directors & chief executive officer of the Company, with the technical support of the Operating Committee, the Group's Business CEO and the rest of the management team, assumes the duty of organisation and strategic coordination of the Group through the dissemination, implementation and monitoring of the overall strategy and of the basic management guidelines established by the Board of Directors.
- c) This organisation and coordination duty is strengthened through the boards of directors of country subholding companies, which includes independent directors, and their own audit committees, internal audit areas, and compliance units or divisions.
- d) The business subholding companies of the Group assume decentralised executive responsibilities. They carry out the day-to-day administration and effective management of each of the businesses, and are responsible for the day-to-day control thereof. These business subholding companies are organised through their respective boards of directors and their own decision-making bodies.

The corporate and governance structure of the Group described above operates jointly with the Group's Business Model, which entails the global integration of the businesses and aims to maximise the operational efficiency of the different units. The Business Model ensures the dissemination, implementation and monitoring of the overall strategy and of the basic management guidelines established for each business, primarily through the exchange of best practices among the various companies of the Group, without detracting from their independence in decision-making.

In any case, the Company and the Group assume the commitments established by law in connection with the legal and functional separation of the companies carrying out regulated activities, while the country subholding companies ensure compliance with the law on this matter.

1.4 Organization of the Board, or bodies in which it delegates its decision, including control functions and the policy followed with minority interests.

A comprehensive description of the governance structure of the Company, functions and internal regulations of the committees can be seen in Appendix C of the Annual Corporate Governance Report, which forms part of this Management Report.

1.5 Regulatory framework of the activities

A comprehensive description of sector regulation and operation of electric and gas system in the markets in which the Group operates can be seen in section 4 of this report.

1.6 Main products and services, production processes

The main products that IBERDROLA offers to its customers are power and natural gas, both in the wholesale and retail markets reaching the final consumer. Also offers a wide range of products, services and solutions in the fields of:

- Improving the quality of life, calm and safety of the consumer.
- Efficiency and energy services.
- Caring for the environment: renewable energy and sustainable mobility.
- Power quality and safety of the facilities.
- Installation of electrical infrastructure.
- Global management of facilities and energy supplies.

Through its subsidiaries it also provides engineering and construction services of power generation facilities, distribution and control; operation and maintenance of power generation facilities, management and promotion of the ground; and sale and rental of housing, offices and commercials. More detailed information can be found in www.iberdrola.com, in "customers" section.

As a general rule, companies directly manage the activities that belong to its core business, and outsource other estimated to be developed more efficiently by other specialized companies, which IBERDROLA requires certain quality standards and responsible behaviour in environmental, social and labour fields.

This information can be extended with corresponding indicators described in the Sustainability Report.

1.7 Strategic principles for the 2016-2020 period

Market conditions

The energy scenario on which Iberdrola will be operating in the years ahead notched up considerable progress towards a more sustainable energy model following the introduction of the Paris Climate Change Agreement on 4 November last year, barely eleven months after it was signed. In the same line, the European Commission ratified its target of reducing CO₂ emissions by 40% by 2030 and its wish for the EU to lead energy transition with its "Clean energy for all Europeans" package.

In due consideration of the technological potential of our sector to assist decarbonisation by using renewable energies, the economy must be electrified to a greater extent in order to meet international commitments in relation to emissions, and simultaneously to service growing world energy demand.

In this context, in the years ahead Iberdrola intends to step up its focus on the solutions energy sustainability requires, which have already made it the "energy company of the future": more renewable energy, more storage capacity, more networks and more smart facilities.

Iberdrola's current business model combines geographic diversification with a focus on activities linked to the energy transition:

- In the United States the company is taking up a position to home in on opportunities for investment in energy infrastructures and renewables through the platform operated by its subsidiary AVANGRID, which has eight regulated energy distribution companies in New York, Connecticut, Maine and Massachusetts, and is the country's second largest wind energy producer.
- The company will continue to expand in the United Kingdom in terms of networks and consolidate its leadership in renewable energies, especially offshore wind power plants on the current platform.
- In continental Europe it will bolster its position in network digitalisation, and its reputation as one of the energy companies with the fewest emissions, a leader of the renewables sector in Spain, and a consolidated platform in Germany and France to develop new offshore wind plants.
- In Mexico, its status as the largest private electricity generator will enable it to take up the opportunities arising from deregulation in the sector.
- In Brazil it is well placed for potential restructuring of the sector as the country's largest distributor in terms of numbers of customers, geographic diversification (Bahía, Río Grande do Norte, Pernambuco and São Paulo states) and renewables capacity.

Strategic Pillars

Iberdrola's 2016-2020 strategy will maintain a focus of currency-diversified growth, with most organic growth opportunities concentrated in A-rating countries, to enable dividend policy to be boosted on the strength of higher earnings, maintaining financial solvency.

Balanced growth

The strategic basis presented by IBERDROLA establishes a net investment programme of EUR 25,000 million in its main geographic and business areas with stable and predictable regulatory frameworks.

Iberdrola will allocate 42% of total investment to electricity and distribution networks. The allocation to renewable energies and regulated generation will be the 39% and 7% of the total amount forecast, respectively. 12% of total investment will be earmarked for generation and commercial business.

88% of the investment scheduled will target regulated business –networks, renewable energies and long-term contracts-.

Geographically, Iberdrola will concentrate most investment in A-rating countries - 48% in Dollars, 29% in Sterling Pounds, 20% in the Eurozone and 3% in Brazilian Reals.

Main projects

- United States: Through AVANGRID, the Group will continue to invest in network infrastructures in the states of New York, Maine, Connecticut and Massachusetts, and hopes to add new transmission projects to the portfolio. IBERDROLA is also building four wind power plants in the US with a combined power output of 743 MW which jointly with two photovoltaic plants of 66 MW results in a total of 809 MW in construction.
- United Kingdom: IBERDROLA will continue to implement network infrastructures under the regulatory frameworks already approved for transmission and distribution (RIIO-T1 and RIIO-ED1). With respect to renewable energy projects in the UK, and is continuing its East of Anglia project in the North Sea which, along with the Wiking offshore wind farm in the Baltic Sea (Germany), will add 1,100 MW to IBERDROLA's offshore installed power output.
- Mexico: IBERDROLA's investment packages will focus on regulated generation and renewable energies, on the strength of the energy reform introduced in this country. The Company is building three combined-cycle plants and two cogeneration plants on long-term contracts, with a combined power output of 2,700 MW, and has plans for further investment in renewable energies in the years ahead.
- Spain: investment will focus on networks, where the distribution regulatory framework has been approved up to 2019.
- Portugal: the company has begun work on construction of about 1,200 MW hydroelectric storage facility at the Tâmega River, which should be up and running by 2023.
- Brazil: IBERDROLA is building eight wind plants with a combined power output of 245 MW, and is also involved on hydroelectric projects such as Belo Monte and Baixo Iguaçu along with NEOENERGÍA. In terms of networks, tariff frameworks have been approved for ELEKTRO (up to 2019), CELPE (up to 2017), COELBA and COSERN (up to 2018).

Operating efficiency in every activity area

IBERDROLA, one of Europe's most efficient major electricity companies, will continue to boost its operating efficiency on the strength of technical progress in terms of the automation and digitalisation of all its businesses and processes, as well as the homogenization of processes through the implementation of the best practices of the group in all its businesses.

Earnings performance

In the years ahead, efficient operation of ongoing assets, along with the aforementioned investment plan, will lead to sustainable growth in Company earnings, with an estimated average annual increase in gross operating profit (EBITDA) of more than 6% up to 2020, or EUR 10,000 million, with better exposure to regulated business or long-term contracts up to 81%. The average annual increase in net profit is expected to be around 7.5%, or EUR 3,500 million by 2020, representing an increase of two percentage points in the net profit/EBITDA ratio to 35%.

Shareholder remuneration

The trend forecast for the period will enable the company to increase long-term remuneration for shareholders, in keeping with results, with a payout in the region of 65-75%, which would result in a dividend per share of EUR 0.37-0.40 in 2020. In any case, a floor of EUR 0.31 per share is established during the period.

At the same time, IBERDROLA intends to maintain the scrip dividend formula used in recent years, and the current number of shares - around 6,240 million - is kept steady through repurchase operations.

Financial solvency

The Company will continue to hold a solid financial position compatible with the investment plans and the remuneration provided to shareholders.

- The average annual operating cash flow, EUR 6,900 million, will comfortably outstrip annual average investment, which stands at EUR 4,800 million. By areas of business, cash generation in Deregulated business and Networks will outstrip investment, while Renewables business will be slightly down against investment.
- Maintenance of the current financial model, giving subsidiaries a capital structure which sends out the right economic signals and is consistent with an investment-grade rating, while adhering to current structural subordination guidelines.
- Optimisation of the liquidity position (around EUR 8,000 - 9,000 million) in current market conditions, in order to improve the cost of borrowing, maintaining 18 months of coverage even in stress scenarios.

This caption of the management report of IBERDROLA contains forward-looking information, including financial projections and estimates and their underlying assumptions, statements regarding plans, objectives and expectations with respect to future operations, capital expenditures, synergies, products and services and statements regarding future performance or administrators estimates which are based on assumptions that are considered reasonable by them.

Although IBERDROLA believes that the expectations reflected in such forward-looking statements are reasonable, investors are cautioned that forward-looking information and statements are subject to various risks and uncertainties, many of which are difficult to predict and generally beyond the control of IBERDROLA, risks that could cause actual results and developments to differ materially from those expressed in, or implied or projected by, the forward-looking information and statements.

Forward-looking statements are not guarantees of future performance and have not been reviewed by the auditors of IBERDROLA. You are cautioned not to place undue reliance on the forward-looking statements, which speak only as of the date they were made. All subsequent oral or written forward-looking statements included in this report are expressly qualified in their entirety by the cautionary statement above. All forward looking statements included herein are based on the information available on the date hereof. Except for required by applicable law, IBERDROLA undertakes no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

2 BUSINESS EVOLUTION AND RESULTS

2.1 Operating highlights for the period

Iberdrola's results for the period must be framed within the implementation of the corporate strategy announced on Investor Day 2016, defined by the growing weight of regulated activities (transmission and distribution of electricity and gas) and the renewables business, both in terms of utilising investment opportunities and contributing to the Group's profit, with a growing weight of the United States and Mexico businesses on said contribution.

The results of financial year 2016 are affected by the performance of Iberdrola's reference currencies compared to 2015. The depreciation of the Sterling Pound and the Brazilian Real has not been offset by the US Dollar, which hardly varied compared to 2015.

In this respect, the following is remarkable:

- In Spain, the period is characterised by high renewable production (40.8% of the total) due to the strong increase in hydroelectric production (+25.3%) especially during the first half of the year. Demand has risen slightly compared to 2015 (+0.7%), with no variation in terms adjusted to number of working days and temperature. The evolution of electricity consumption of the group companies and industries shows that over the last 12 months, consumption has remained at levels similar to 2015.
- In the United Kingdom, electricity demand dropped by 1.3% compared to 2015. However, customers' gas demand (not including generation consumption) increased by 2.6%.
- Avangrid's area of influence on the East Coast of the United States saw a 0.8% and 2.3% drop in electricity demand and gas demand, respectively.
- On the other hand, demand in the markets of Iberdrola in Brazil grows 1% compared to the same period of the previous year, mainly in the Northwest markets of the country covered by Neoenergía, due to the demand of Elektro falls slightly affected by the smaller Industrial activity in this area.

During financial year 2016, commodities international markets of raw materials evolved as follows:

- The average price of Brent oil was steady at USD 43.7 per barrel compared to USD 52.8 per barrel last year (-16.8%).
- The average price of gas (TTF) over the period dropped to EUR 14.0/MWh, compared to EUR 19.8/MWh in 2015 (-29.3%).
- The average price of API2 coal was USD 59.8/MT, compared to USD 55.9/MT (+7.0%) last year.
- The average cost of CO₂ rights dropped from EUR 7.7/MT in 2015 to EUR 5.3/MT in 2016 (-31.2%).

The average performance of Iberdrola's main reference currencies against the Euro in 2016 compared to last year was as follows: the Sterling Pound and the Brazilian real depreciated by 12.7% and 4.6%, respectively, and the USD remained at levels similar to the previous FY (+0.3%).

The following highlights should be noted regarding the period analysed, in comparison to the previous financial year:

- First full year of consolidation of UIL in the United States, an effect registered in the Networks Business of said country.

- Consolidated EBITDA increased by 5.5 % compared to 2015, reaching EUR 7,807.7 million.
- The Net Financial Result improved by 11.7%, as a result of the financial cost drop and the exchange rate hedges carried out at the start of the year, mainly on Sterling Pound, despite an increase in average debt.

In this context, IBERDROLA Group's total production in this period increased by 1.4% to 132,414 GWh (130,594 GWh in 2015). The distribution by geographical areas is the following:

Net Production (GWh)	2016	2015	% change
Spain	61,725	54,453	13.4
United Kingdom	13,531	18,448	(26.7)
United States	17,436	17,015	2.5
Mexico	37,717	38,866	(3.0)
Brazil	639	441	44.9
Rest of the world	1,366	1,371	(0.4)
Total	132,414	130,594	1.4

At the end of 2016, IBERDROLA had 43,277 MW installed generation capacity, of which 65.5% produces emission-free energy while operating at a very low variable cost. In the table below, distribution classified by countries and technologies is shown:

Countries	2016	2015	MW var (16-15)
Spain	25,605	25,607	(2)
United Kingdom	4,522	6,450	(1,928)
United States	6,502	6,294	208
Mexico	5,840	5,415	425
Brazil	187	187	-
Rest of the world	621	621	-
Total power (MW)	43,277	44,574	(1,297)

Technologies	2016	2015	MW var (16-15)
Hydraulic	10,392	10,392	-
Nuclear	3,166	3,166	-
Coal	874	3,178	(2,304)
Gas Combined Cycles	13,778	13,353	425
Cogeneration	299	299	-
Wind power, mini-hydraulic and other renewables	14,768	14,186	582
Total power (MW)	43,277	44,574	(1,297)

The following exceptional highlights should be noted with regard to the period analysed, compared with the previous fiscal year:

- UIL's first full consolidation exercise in the United States, which is integrated in the Network business in that country. The integration of Iberdrola USA and UIL, and its subsequent incorporation into AVANGRID took place on 16 December 2015.
- Reclassification results of capital grants.

Since May 2016, the capital gains attributed to results are classified as "Other operating income" and not reducing the amortizations as previously. Correlated comparative information for 2015 has been corrected with this effect. The increase in revenues in 2016 and 2015 amounted to EUR 82 million and EUR 91 million respectively. The effect on the Group's Net Profit is null, since it is corrected with higher depreciation for the same amount.

The optimisation of financial soundness and liquidity as strategic priorities are summarized as follows:

- Net Debt stood at EUR 29,414 million, with an improvement in leverage to 42.0% compared to 40.7% in 2015.
- Funds Generated from Operations at the end of 2016 had increased by 6.8% and reached EUR 6,311 million.
- Solvency ratios had slightly improved as at December 2016.

2.2 Business evolution

2.2.1 Analysis of the profit and loss account

The key figures for the financial year 2016 are as follows:

Millions of euros	2016	2015	% change
Net revenue	29,215	31,419	(7.0)
Gross margin ⁽¹⁾	12,916	12,843	0.6
EBITDA ⁽²⁾	7,808	7,397	5.6
EBIT ⁽³⁾	4,554	3,829	18.9
Net profit	2,843	2,460	15.6

(1) Gross Margin: Revenue – Procurements

(2) EBITDA: Operating profit+ Amortisation and provisions

(3) EBIT: Operating profit

2.2.1.1 Gross Margin

Gross Margin was at EUR 12,916 million with a 0.6% increase compared to what was obtained in financial year 2015, supported by the contribution of UIL (EUR +770 million), which more than compensates for the performance of the average reference currencies (EUR -339 million).

Millions of euros	2016	2015	% change
Network Business	6,161	5,514	11.7
Deregulated Business	4,634	4,841	(4.3)
Renewable Business	2,179	2,361	(7.7)
Other Businesses	106	235	(54.9)
Corporation and adjustments	(164)	(108)	(51.9)
Gross Margin	12,916	12,843	0.6

– Network business

The Network business increased its contribution by 11.7% to EUR 6,161 million (EUR 5,514 million in 2015).

Millions of euros	2016	2015	% change
Spain	2,028	1,952	3.9
United Kingdom	1,267	1,472	(13.9)
United States	2,537	1,698	49.4
Brazil	329	392	(16.1)
Total Network business	6,161	5,514	11.7

The Network business increased 11.7% compared to 2015, amounting to EUR 6,161 million, with positive developments in Spain and the United States and reductions in the United Kingdom and Brazil. As noteworthy events in the period we can highlight:

- In Spain, it reached EUR 2,028 million, as a result of the definitive approval of the regulatory framework of Distribution.
- In the United Kingdom, it came to EUR 1,267 million (-13.9%), mainly due to the depreciation of the Sterling Pound (+10%) and the revenue profile defined in the new regulatory framework for Distribution (RIIO ED1) which came into force in April 2015.
- The contribution of the United States for the period totalled EUR 2,537 million (+49.4%) due to the consolidation of UIL.
- Gross Margin for Brazil (Elektro) was at EUR 329 million (-16.1%) affected by the depreciation of the Brazilian Real, a decrease in circulated energy and the different composition of the demand with regard to last year.

- Deregulated Business

The Deregulated Business (Generation and Retail) decreased by 4.3% to EUR 4,634 million (EUR 4,841 million in 2015).

Millions of euros	2016	2015	% change
Spain and Portugal	3,071	2,971	3.4
United Kingdom	1,000	1,306	(23.4)
Mexico	509	584	(12.8)
Brazil	6	—	100.0
United States	48	(20)	340.0
Total Deregulated Business	4,634	4,841	(4.3)

- In Spain, it reached EUR 3,071 million (+3.4%) thanks to the different production mix compared to 2015 and to the greater volume of sales to customers.
- Gross Margin for the United Kingdom was EUR 1,000 million, negatively affected by the depreciation of the Sterling Pound, the increase of regulatory costs both in Generation and in Retail and the lower sales as a result of warmer period.
- Mexico contributed EUR 509 million to the Gross Margin (-12.8%), due to the lower margins in contracts with CFE as they are linked to certain macroeconomic variables (this impact is compensated at EBITDA level as Net Operated Expenses is also linked to those variables) and also with private customers and to the delay in putting in operation of several plants that are already in operation.

– Renewables business

The Renewable business decreased its Gross Margin by 7.7% to EUR 2,179 million (EUR 2,361 million in 2015).

Millions of euros	2016	2015	% change
Spain and Portugal	764	751	1.7
United Kingdom	385	572	(32.7)
United States	802	822	(2.4)
Brazil	36	36	–
México	69	57	21.1
Rest of the world	123	123	–
Total Renewable business	2,179	2,361	(7.7)

The main causes of this trend are:

- In Spain, it increased to EUR 764 million (+1.7%) due to greater production.
- Gross margin decline in United Kingdom, dropped by EUR 385 million, due to the effect of the depreciation of the Sterling Pound, the lower production (-16.8%) resulting from the lower wind power of the period, lower market prices and the LECs elimination in the third quarter of 2015.
- A contribution from the US of EUR 802 million (-2.4%) as a result of the non-renewable gas business that had a positive result in 2015 due to the derivatives in electricity and gas (EUR 31 million) that has not been repeated this year. The greater production (+5.2%) offsets the drop in the average price.
- Latin America contribute to EUR 105 million (+12.9%) with Mexico improving by 21.1% thanks to the new capacity in operation, and Brazil was practically flat.

– Other businesses

The contribution of Other Businesses reached EUR 106 million, a decrease of 54.9% (EUR 235 million in 2015).

2.2.1.2 Gross Operating result – EBITDA

Consolidated EBITDA increased by 5.6% to EUR 7,808 million (EUR 7,397 million in 2015), which improved the Network business (+12.5%) and decreased Generation and Customers (-3.0%) and Renewables (-8.9%).

Millions of euros	2016	2015	% change
Network Business	4,082	3,627	12.5
Deregulated Business	2,253	2,323	(3.0)
Renewable Business	1,500	1,647	(8.9)
Other Businesses	(111)	(10)	(1,010.0)
Corporation and adjustments	84	(190)	144.2
EBITDA	7,808	7,397	5.6

Contribution of non-recurring elements at EBITDA level was EUR 54 million, given that the positive impact of the Social tariff ruling (EUR +142 million) was partially offset by another set of effects (EUR -88 million in total), which include favourable rulings in Spain, efficiency measures, extraordinary IFRS losses in the Networks US business and the compensation to customers imposed by OFGEM.

– Net operating expenses

In addition to the above-mentioned trend of the Gross Margin, Net Operating Expenses dropped by 4.5% to EUR 3,572 million (EUR 3,739 million in 2015), impacted by the control of costs and the incorporation of UIL.

Millions of euros	2016	2015	% change
Network Business	1,441	1,385	4.0
Deregulated Business	1,504	1,565	(3.9)
Renewable Business	537	560	(4.1)
Other Businesses	216	242	(10.7)
Corporation and adjustments	(126)	(13)	(869.2)
Net operating expenses	3,572	3,739	(4.5)

– Levies

The Taxes item dropped by 9.95% to EUR 1,537 million, with the impact of the incorporation of UIL (EUR -138 million) offset by the positive net impact of EUR 217 million related to favorable judgments in Spain in both 2016 and 2015.

2.2.1.3. Net Operating result – EBIT

EBIT totalled EUR 4,554 million, 18.9% higher in comparison with 2015 (EUR 3,829 million).

Millions of euros	2016	2015	% change
Network Business	2,649	2,485	6.6
Deregulated Business	1,313	962	36.5
Renewable Business	703	659	6.7
Other Businesses	(125)	(30)	(316.7)
Corporation and adjustments	14	(247)	105.7
EBIT	4,554	3,829	18.9

– Amortisations and provisions

Amortisations and Provisions dropped by -8.8%, totalling EUR 3,254 million:

- The Amortisations item remained stable (+0.1%), totalling EUR 3,076 million, the lower amortisation following the write-off in 2015 of the Longannet Plant (EUR +132 million), and the effect of the extension to 40 years of useful life of the towers and the civil works of the onshore wind farms in accordance with industry standards (EUR +147 million), offset the incorporation of UIL (EUR -188 million) and the increase due to new investments.
- The Provisions item totalled EUR 178 million (-64.0%), decreasing EUR 316 million, mainly due to the fact that in the fourth quarter of 2015 the Longannet power plant was repaired in an amount of EUR 288 million.

2.2.1.4. Financial Result

The net financial profit/(loss) was EUR -903 million, improving by 11.7% compared to that registered in 2015 (EUR 1,023 million).

The reduction in the average cost to 3.49% (57 b.p. lower than last year) has contributed with a EUR 64.8 million (6%) on the improvement of the result associated to debt, despite the fact that average net debt increased by EUR 2,365 million.

The result for DVMEs and derivatives improved by EUR 115.6 million, greatly because of the coverage on net profit that generated a positive valuation for the evolution of Sterling Pound after Brexit.

Several non-recurring contingencies recorded in 2016 (mainly interests accrued in legal decisions and sale of the stake in Euskaltel) resulted in a lower financial revenue of EUR 60.8 million.

2.2.1.5 Results of Companies Consolidated by the Equity Method

The Result of Companies Method of Participation reached EUR 49 million (-11.9% compared to 2015, EUR 55 million). The improvement in Gamesa's results is offset by the lower contribution from Neoenergia and the effect of the sale of wind farm participation in Italy.

2.2.1.6 Income from Non-Current Assets

Income from Non-Current Assets amounted to EUR 48 million with a decrease of EUR 77 million compared to 2015 (EUR 125 million). In 2016 the most significant transactions have been the sale of Iriquois (minority stake in a local gas network) in the United States, and the sale of the stake in the real estate company Oceanic Center.

2.2.1.7 Net Profit

Lastly, Net Profit came to EUR 2,705 million, an increase of 11.7% compared to that obtained in 2015 (EUR 2,422 millions).

Recurring Net Profit reached EUR 2,531.7 million (EUR 2,261.4 million in 2015) (+12%) as a result of the good performance of the business and the year-on-year comparison of specific items in each year.

The balancing of the Recurring Net Profit and the Reported Net Profit is as follows:

Millions of euros	2016	2015
Recurring Net Profit	2,531.7	2,261.4
Extraordinary writte-off	30.5	-275.5
Income from non-current assets	40.7	140.6
Non-recurring taxes	102.1	295.1
Reported Net Profit	2,705.0	2,421.6

Tax expenses increased by 71.6% to EUR 904.6 million, mainly due to non-recurring tax effects recorded in 2015. The lower tax rate in Spain (from 28% to 25%) is offset by income in countries with higher tax rates, such as the US.

2.3 Operative evolution of the period

2.3.1 Network business

A. Spain

IBERDROLA has approximately 10.9 million managed supply points and total distributed energy 93,736 GWh, a decrease of 0.4% compared to the same period of the previous year (94,113 GWh in 2015).

TIEPI's quality of supply indicator for fiscal year 2016 was 54.1 minutes, with an improvement of 12% over the previous year (61.9 minutes in 2015).

The table shows the values of the TIEPI (interruption time) and NIEPI (number of interruptions) in relation to the previous year:

Year	Accumulated TIEPI	Accumulated NIEPI
2015	61.9	1.20
2016	54.1	1.04

The investment made during the year has allowed the following facilities to be put into operation:

Physical Units	2016	Total
Lines	Overhead (km)	185
	Underground (km)	573
Substations	Transformer (units)	4
	Capacity increase (MVA)	788
	Substation (units)	10
Secondary sub-stations	Centres (units)	411
	Capacity increase (MVA)	130

In addition, during this year, 2.3 million smart meters with a remote management system were installed, within the STAR smart network project.

It is noteworthy that the regulatory requirement to replace 70% of smart-meters before 31 December 2016 has been fulfilled.

B. United Kingdom

IBERDROLA has more than 3.5 million supply points in the United Kingdom. The volume of energy distributed during 2016 was 33,482 GWh (34,009 GWh in 2015), a decrease of 1.5% compared to the year 2015.

The average Customer Minutes Lost (CML) and the number of consumers affected by interruptions per every 100 customers (Customer Interruptions, CI) are:

	2016		2015	
	CML	CI	CML	CI
Scottish Power Distribution (SPD)	30.7	45.3	34.7	46.6
Scottish Power Manweb (SPM)	37.2	38.9	35.2	31.5

Although Scottish Power Energy Networks' (SPEN) quality indicators have increased due to four incidents that have affected 100,000 consumers in aggregate, the indicators of both companies comply with regulatory limits.

C. United States

- Distribution

In the United States IBERDROLA has 2.2 million electricity supply points. The volume of energy distributed in the year was 37,027 GWh, which represents an increase of 15.5% compared to 2015 (32,047 GWh) due to the integration of UIL.

The System Average Interruption Frequency Index (SAIFI) and the Customer Average Interruption Duration Index (CAIDI) are as follows:

	2016		2015	
	SAIFI	CAIDI	SAIFI	CAIDI
Central Maine Power (CMP)	1.78	1.89	0.72	1.70
NY State Electric & Gas (NYSEG)	1.19	2.02	0.56	2.08
Rochester Gas & Electric (RG&E)	0.58	1.79	0.41	1.79
United Illuminating Company (UI)	0.53	0.42	-	-

The three companies comply with all their quality of service indicators within the limits required by the corresponding commission.

– Gas

The number of gas users in the United States at the end of 2016 is approximately one million, which has been supplied with 53,460 GWh, a 68.9% increase over the same period of last year due to the integration of the UIL gas distributors. Discounted this effect, the gas distribution has been 2.3% lower than the previous year, which is due to the mild temperatures recorded in the winter of 2016.

D. Brazil

The evolution of the demand of distributors in Brazil, COELBA, COSERN, CELPE and ELEKTRO in 2016 has remained at levels similar to those of the previous year, reaching 54,530 GWh (54,000 GWh in 2015).

Energy distributed (GWh) 100% of business	2016	2015	% Change
COELBA	19,549	18,871	3.6
COSERN	5,582	5,512	1.3
CELPE	13,410	13,426	(0.1)
ELEKTRO	15,962	16,191	(1.4)
Total	54,503	54,000	0.9

The number of customers served by the distributors at the end of the year reaches 13.4 million.

Number of customers (million) 100%	2016	2015
COELBA	5.8	5.7
COSERN	1.4	1.3
CELPE	3.6	3.5
ELEKTRO	2.6	2.5
Total	13.4	13.0

Regarding regulated electricity generation, the power of the projects in operation at the end of 2016 is 5,653 MW (1,059 MW in the IBERDROLA percentage).

As for the projects under construction, the pace of construction follows the planned schedule, so that the scheduled finish dates are maintained. In 2016, several of the groups that account for 78 MW attributable have entered operation in Belomonte.

Plant	MW	Attributable MW	Year
Baixo Iguaçu	350	137	2018
Belo Monte	9,245	360	2016-2018
Total	9,595	497	

2.3.2 Deregulated business

A. Spain and Portugal

A.1. Generation

Installed capacity in Spain (without renewables) reaches 19,745 MW, the same as in 2015.

Installed capacity (MW)	2016	2015	Change
Hydroelectric	9,713	9,713	–
Nuclear	3,166	3,166	–
Coal	874	874	–
Gas combines cycles	5,694	5,694	–
Cogeneration	298	298	–
Total	19,745	19,745	–

On the other hand, the Energy Balance of the Spanish peninsular system in 2016, is characterized by a high renewable production (40.8% of the total) due to the increase in hydraulic production (+25.3%), especially in the first half of the year, because has been specially rainy. As a consequence, coal production has been reduced comparing to the year 2015, (-30.9%), although gas production rises slightly (+2.3%). In adjusted terms of labor and temperature, the evolution is at 0%.

According to IBERDROLA, during the twelve months of 2016, production increased by 16.7% until reaching 43,338 GWh.

The evolution of the year by technologies is as follows:

GWh	2016	2015	% change
Hydroelectric	18,510	12,488	48.2
Nuclear	24,335	23,082	5.4
Coal	2,115	3,684	(42.6)
Gas combines cycles	3,724	2,293	62.4
Cogeneration	1,875	1,791	4.7
Total net production	50,559	43,338	16.7

- Hydraulic production reached 18,510 GWh, an increase of 48.2% over the previous year. The level of water reserves stood at 42% (equivalent to 4,774 GWh) at 31 December 2016.
- Nuclear production stands at 24,335 GWh, an increase of 5.4%.
- Coal-fired power stations reached 2,115 GWh, compared to 3,684 GWh the previous year, representing a reduction of 42.6%.
- Production of combined cycle plants, for their part, increased by 62.4%, until reaching 3,724 GWh.
- Cogeneration plants increase their production by 4.7%, until reaching 1,875 GWh.

A.2 Retailing

Supplied energy (electricity and gas) in Spain came to 60,367 GWh (58,282 GWh in 2015), 51,614 GWh of electricity and 8,753 GWh of gas.

Electricity sales on the deregulated market in 2016 increased by 5.8% amounting to 43,405 GWh compared to 41,008 GWh supplied in the same period of 2015. Regarding the electricity supplied at the PVPC, it amounts to 8,209 GWh.

The gas retailed in the free market in 2016 increased by 4.5% to 8,702 GWh compared to 8,364 GWh supplied in 2015.

In Portugal, IBERDROLA supplied 7,343 GWh during 2016, compared to 6,718 GWh supplied in 2015 (+9.3%), being the second seller in the Medium Voltage industrial clients.

B. United Kingdom

B.1. Generation

At 31 December 2016 and 2015, UK installed capacity amounts to 2,531 MW and 4,835 MW, respectively, as a result of the closure of the Longannet coal plant (2,304 MW) at the end of March.

(MW)	2016	2015	% change
Hydroelectric	563	563	–
Coal	–	2,304	(100.0)
Gas combined cycles	1,967	1,967	–
Cogeneration	1	1	–
UK Total	2,531	4,835	(47.7)

With regard to production from traditional electricity generation, in 2016 it decreased by 29.1% to 10,456 GWh compared to the 14,754 GWh of the previous year, due to the aforementioned impact of the closure of the Longannet power plant.

The market share of the generation business in 2016 was 4.2%, compared to 6% in the previous year. By technologies, the most outstanding aspects are the following:

GWh	2016	2015	% change
Hydroelectric	585	704	(16.9)
Coal	1,636	7,813	(79.1)
Gas combined cycles	8,234	6,235	32.1
Cogeneration	1	2	(50.0)
UK Total	10,456	14,754	(29.1)

B.2. Retailing

Regarding sales, during 2016 customers have been supplied with 20,951 GWh of electricity and 31,974 GWh of gas (20,458 GWh of electricity and 32,055 GWh of gas supplied during 2015). At 31 December 2016, SCOTTISH POWER had 3.2 million electricity customers and 2.1 million gas customers.

C. Mexico

IBERDROLA remains the leading private producer in the country with 5,473 MW (5,048 MW in 2015) in installed capacity.

There are in process of execution five new plants, and as an important milestone there must be highlighted the beginning of the commercial operation of the Dulces Nombres 2 plant in Monterrey of 300 MW in the last quarter. This year the 53.3 MW Ramos cogeneration plant has been put in operation, as the extension of 57 MW of Altamira III and IV and the extension of Monterrey I and II 16 MW.

With all that, in 2018 and 2019 in totally consolidated projects and in the operative thermic power of Iberdrola in Mexico will reach the 7,600 MW, where apart from the long term contracted capacity, already indicated by the CFE, long term contracts with private customers are hold by the company.

The electric energy supplied from the combined cycle and cogeneration plant has been 35,598 GWh (38,128 GWh in 2015), which supposes a charge factor of the 80%, because the generation with natural gas the base of the electric generation in Mexico. The accumulated availability of the plants in Mexico has been 95.8%.

D. Gas storage in US and Canada

Gas storage facilities operated by the Company in 2016 totalled 2.4 bcm. In addition, the Company had 1.6 bcm of contracted or managed capacity.

2.3.3. Renewable business

At the end of 2016, the renewables business had an installed capacity of 14,768 MW (14,184 MW in 2015).

The renewable production increased by 2.2% to 31.917 GWh (31.228 GWh in 2015).

During the last 12 months, IBERDROLA installed 582 MW in new renewable installations.

Installed MW	2016	2015	MW change
Wind Energy Spain	5,508	5,508	–
Wind Energy USA	5,692	5,484	208
Wind Energy United Kingdom	1,991	1,614	377
Onshore	1,797	1,420	377
Offshore	194	194	–
Wind Energy Mexico	367	367	–
Wind Energy Brazil	187	187	–
Wind Energy Rest Of The World	615	615	–
Total wind energy	14,360	13,775	585
Other renewables	408	409	(1)
Total installed capacity	14,768	14,184	584

A. Onshore Wind Energy

During the last 12 months, Iberdrola has increased its total installed power in 581.81 MW: 585 MW were installed and 2.23 MW dismantled (0.85 MW of wind and 1.38 MW of mini-hydraulic in Spain).

Iberdrola has reached a power of land wind energy of 14,166 MW after 585 MW wind land had been added during the last 12 months.

- Spain

The installed power at the end of 2016 has reached to an amount of 5,508 MW and manages 244 MW throw non-consolidated participated companies.

A work of two wind parks with a total capacity of 32.2 MW in the Tenerife island has been approved: Chimiche II (18.4 MW) and Las Aulagas (13.8 MW).

– USA

The Company has presence in 19 states with a total of 5,692 MW eolians installed and 161 MW additional are managed through participated companies.

The constructions Desert Wind (208 MW) with a PPA signed by Amazon in Northern California (all the aerogenerators had been installed, and only the last 8 MW are still missing to start so as to get into their commercial operation), El Cabo (298.2 MW) in Nuevo Mexico, Deerfield (30 MW) in Vermont and Tule (131.1 MW) in California, and the prior phase to the beginning of works in Twin Buttes II (75 MW) in Colorado are in progress.

– United Kingdom and Republic of Ireland

The wind land power is 1,796 MW in United Kingdom and 15 MW are managed through participated companies.

During the year, work has been done on the construction of 473.78 MW that are subject to ROCs' system. From this project portfolios, works had been finished for a total amount of 146.23 MW: 13.8 MW in Ewe Hill Phase 1, 45.6 MW in Black Law Ext. Phase 1.69 MW in Dersalloch and 18.37 MW in Black Law Ext. Phase 2, and works of: 327.55 MW of the wind parks of Killgallioch (239 MW from which 167.5 MW have been installed), Hare Hill extension (29.75 MW from which 23.35 MW have been installed), EWE Hill Phase 2 (36.8 MW from which 25.3 have been installed) and Glen App (22MW from which 14 MW have been installed) they are now in the course phase.

– Brasil

Six projects for a total of 174 MW eolians were finally winners in the "Leilões" (competition) which had taken place during 2014. There are in progress the works of the following wind farms: Calango 6 (30 MW), Santana I (30 MW) and Santana II (25 MW).

In Brasil, Iberdrola has 187 MW consolidated and 59 MW managed through Neoenergia.

In addition, six projects for a total amount of 178.5 MW winds were finally winners in the "Leilões" (competition) which had taken place during 2014. There are finished the works of the following wind farms: Calango 6 (30 MW), Santana I (30 MW) and Santana II (24 MW), even if they will not be consolidated until the first trimester of 2017.

– Mexico

In Mexico, the installed power is 367 MW.

Works for additional 325.5 MW have been approved: wind Santiago (105 MW) in Guanajuato and Pier (220.5 MW) in Puebla.

B. Offshore Wind Energy

Currently, the renewables business is developing offshore wind projects mainly in the United Kingdom, Germany and France.

In the United Kingdom, in 2014, the Company went into operation of the West of Duddon Sands project located in the Irish Sea with a capacity of 389 MW which is being jointly developed at 50% with Dong Energy (194.5 MW correspond to IBERDROLA).

IBERDROLA continues the Wikinger offshore project development, up to 350 MW in the Baltic Sea (Germany). Pilot installation and jacketing campaigns have been completed.

The cable laying works of the wind farm are also at its completion and are progressing with completion and testing works. The OSS (marine substation) is already installed and is in the phase of completion of the start-up and termination. At the same time, offshore turbine installation operations are underway to start up in 2017.

Iberdrola is developing in the United Kingdom the "East Anglia" project in the North Sea. In February 2015, the East Anglia I project secured a Contract for Difference in the first auction of its kind in the United Kingdom, for a maximum capacity of 714 MW, whose investment of GBP 2,600 million was approved by the Company in February 2016. The project has made progress during 2016, with most of the contracts for the supply of the main packages signed.

It is noted that the contract with Siemens for the supply of 102 wind turbines of 7 MW, contracts with Navantia for the supply of the offshore substation and 42 jackets on which the wind turbines will be based, the contract with Lamprell for the supply of 60 jackets and with Nexans for the supply of the evacuation cable between the substation of the wind farm and the substation onshore. The signing with The Crown Estate of the leasing contract of the maritime domain for the settlement of the farm during its useful life is also remarkable in 2016.

On the other hand, Iberdrola and Vattenfall (partner in the initial development process) finalized the negotiation with The Crown Estate in the first quarter of 2016 for the distribution of the remaining projects in East Anglia. As a result, Iberdrola owns 100% of the rights over 3 projects in different stages of development of accumulative capacity 2,800 MW.

In April 2012, the consortium formed by IBERDROLA and the French company EOLE-RES was awarded by the French Government the exclusive rights for the operation of the offshore wind farm of Saint-Brieuc, with a capacity of 500 MW. In 2013, the project was technically redefined with the aim of using a more modern machine, 8 MW of unit power, made by ADWEN (Joint venture between Areva and Gamesa). In October 2015, the project submitted its application for a construction license. In 2016, the Company will work towards answering the requests from the French administration within the process for approval of the license, as well as on the consolidation of the main supply agreements for the future farm.

C. Other technologies

The Renewable business has facilities of other renewable technologies in various countries making a total of 409 MW, which breakdown is presented in the following table:

MW instalados	2016	2015	Country
Mini-hydraulic special regime	130	130	Spain
Mini-hydraulic ordinary regime	172	173	Spain
Solar thermal hybrid	50	50	Spain
Photovoltaic	56	56	USA (50MW) Greece (6MW)
Waves	–	–	UK
Other Renewables	408	409	

– USA-Avangrid

The construction of a 66 MW with photovoltaic technology has been approved: Gala (56 MW) and W'y East (10 MW), aboth in the Oregon state.

– Mexico

The construction of a 270 MW with photovoltaic technology has been approved: Santiago photovoltaic (170 MW) in San Luis de Potosí and Hermosillo (100 MW) in Sonora.

3 LIQUIDITY AND EQUITY RESOURCES

3.1 Leverage

Adjusted net financial debt at 31 December 2016 increased by EUR 1,347 million to EUR 29,414 million compared to the EUR 28,067 million at 31 December 2015, as a result of the anticipation of renewable investments (off-shore advanced payments and Safe Harbour). As a result, financial leverage increases to 42% compared to 40.7% in 2015.

	2016	2015
Equity	40,687	40,956
Gross Debt	32,026	30,340
Efectivo y equivalentes (Nota 19)	(1,433)	(1,153)
Derivados activos y otros	(1,179)	(1,120)
Net debt	29,414	28,067
Leverage	42.0%	40.7%

3.2 Credit rating of IBERDROLA senior debt

Agency	Rating ⁽¹⁾	Outlook	Date
Moody's	Baa1	Positive	04/25/2016
Fitch	BBB+	Stable	03/25/2014
Standard & Poors	BBB+	Stable	04/22/2016

(1) Warning: The above ratings may be revised, suspended or withdrawn by the rating agency at any time

3.3 Debt structure

Regarding the evolution of the financing cost of the Company, at 31 December 2016 it stood at 3.17% compared to 3.57% in the same period of the previous year (Note 25 of the Consolidated financial statements).

The structure of the debt by interest rate and currency can be seen in Notes 5 and 25 of the Consolidated financial statements.

In accordance with the policy of minimizing the financial risks of the Company, foreign currency risk has continued to be mitigated through the financing of international businesses in local currencies (Sterling Pound, Brazilian Real, US Dollar, etc.) or in their functional currencies (US Dollar, in the case of Mexico).

IBERDROLA has a strong liquidity position at the end of 2016 exceeding EUR 8,000 million, equivalent to more than 24 months of the Company's financing needs (Note 50 of the Consolidated financial statements).

(Millions of euros)	
Credit line maturities	Available
2017	266
2018	1
2019 and onwards	6,317
Total	6,584
Cash and Short Term Fin. Invest.	1,432
Total adjusted liquidity	8,016

IBERDROLA has a varied debt maturity profile, with an average maturity of approximately six years, as a result, among other factors, of the active management of liabilities carried out during this financial year. IBERDROLA's debt maturity profile at the end of 2016 can be seen in Note 25 of the Consolidated financial statements.

3.4 Working capital

Working capital shows a decrease of EUR 109 million since December 2015 as a result mainly due to several different effects partially offsetting one another:

- A decrease of "Inventories" of EUR 163 million reduce the working capital.
- The increase in both the "Commercial debtors and creditors" result, all together, in a decrease of working capital of EUR 37 million.
- A decrease of "Provisions" of EUR 102 million, increase de working capital.

	12.31.2016	12.31.2015	Change
Assets held for sale	–	44	(44)
Nuclear fuel	323	350	(27)
Inventories	1,634	1,797	(163)
Current trade and other receivables	5,862	6,048	(186)
Current financial assets	781	688	93
Asset derivative financial instruments (1)	322	339	(17)
CURRENT ASSETS ⁽¹⁾	8,922	9,266	(344)
Provisions	144	245	(101)
Liability derivative financial instruments	339	324	15
Trades and other payables (2)	8,434	8,583	(149)
CURRENT LIABILITIES ⁽²⁾	8,917	9,152	(235)
NETWORKING CAPITAL	5	114	(109)

(1) It does not include cash or debt asset derivatives.

(2) It does not include financial debt and debt liabilities derivatives.

4 INDUSTRY REGULATION AND FUNCTIONING OF THE ELECTRICITY AND GAS SYSTEM

Both IBERDROLA and some of the fully or proportionately consolidated subsidiaries engage in electricity business activities in Spain and abroad (see the Appendix to these Consolidated financial statements) that are heavily affected by the respective regulatory frameworks. Below there is a description of the main regulations affecting the IBERDROLA Group.

4.1 European Union

In the member states of the European Union in which IBERDROLA is present, particularly in the UK and Spain, it should comply with EU regulations.

The aim of the European legislation is the implementations of the single gas and electricity markets in order to facilitate the exchange of energy flows and allow any consumer in the European Union to deal freely with any supplier in the EU. In this respect, there are two types of legislation: the directives, which set out common criteria to be observed in internal markets and which the member states should transpose into national legislation; and the Regulations, which establish norms for the supranational issues, especially those related to the transit of gas and electricity, and are applicable directly.

Another set of regulations that indirectly affects the energy sector are those arising from the energy and climate policy agreed in 2007. It involves the triple objective of reducing emissions of greenhouse gases (GHGs) by 20%, setting a quota of renewable energy of 20% and a target for reducing consumption by 20% vs. "Business as Usual" case, all by 2020. To meet these objectives by 2020 there have been four documents accompanying the legislation: the reform of the Emissions Trading System, EU (EU-ETS), the national targets for emissions from non-EU ETS, and the national objectives on renewable energy.

Since 2009, the EU institutions and Member States have worked to implement the regulation approved in that year related to, on one hand, the internal gas and electricity markets and, on the other hand, to promote renewable energy and to combat climate change. This regulation will be reviewed from 2016 to 2020.

The legislation on infrastructures is also relevant. The European Union has powers with regards to trans-European networks, specifically those of energy. During the last few years, various regulations and programmes have been created to promote a greater connectivity among the Member States. Specifically, programmes like the Trans-European Energy Networks (TEN-E), the European Energy Programme for Recovery (EEPR) and the Connecting Europe Facility (CEF). Lastly, in December 2014, the European Council approved the creation of a Strategic Investment Plan for the European Union, to mobilize EUR 315,000 million in 2015 – 2017. It will be structured as a European Fund for Strategic Investments allocated to investments in infrastructure, including energy and renewable energy networks. In January 2015, the European Commission submitted the proposal of a Regulation on the European Fund for Strategic Investments to create the required legal framework. On 27 May 2015, an agreement was reached between the Council, the Parliament and the European Commission on the proposed Regulation.

In October 2014, the European Council agreed new targets for 2030: a 40% reduction in GHGs compared to 1990, a share of 27% for renewable energy and a reduction in consumption, also of 27% (to be potentially upgraded to 30% following new proposals as explained below regarding the *Clean Energy for all Europeans* package). It also agreed to ensure that in 2020 the electricity exchange capacity among countries was at least 10% of the installed capacity.

On 25 February 2015, the European Commission launched a framework strategy for a resilient Energy Union with a Forward-Looking Climate Change Policy, that includes fifteen action points to be implemented during the mandate of the current European Commission, including, among others, setting out the goals of an energy union and the steps the Commission will take to achieve it, a new legislation to redesign and reform the electricity market, ensure the supply for electricity and gas, EU funding for energy efficiency, a new renewables energy package and a structural reform of EU-ETS, facilitating the compliance of 2030 Targets set by the European Council in October 2014. On 18 November 2015, the European Commission presented its first State of Energy Union reporting advances achieved in 2015 and steps to be undertaken in 2016. A guidance on Governance of the Energy Union process was also provided.

On 15 July 2015, the European Commission (EC) has published a package of documents that anticipated legislative action in the field of energy markets and emissions trading. Through the Communication on Market Design, the EC analysed the functioning of the EU electricity markets, arose key proposals for improvement and opened the discussion on capacity mechanisms. The Communication on retail market ("New Deal" for customers) made proposals to fully liberalise retail markets and facilitate more interaction with customers. It also attached a document on "best practices" in self-consumption.

Regarding the emissions trading, in July 2015 the EC sent its legislative proposal to reform the ETS Directive to the European Parliament and the Council, covering, inter alia, the Market Stability Reserve (MSR) and the protection of sectors in leak of carbon.

As set out in Decision 2015/1814 of the European Union and of the Council, the MSR (Market Stability Reserve) will come into operation on 1 January 2019. The MSR was established to reduce 900 million allowances of the auctioned volumes during the period 2014-2016, reintroducing them in the auctions of 2019 and 2020. Beginning in 2019, an amount of allowances corresponding to 12 % of the number of allowances in circulation should be deducted each year from the auction volumes and placed in the Reserve. If the total number of allowances in the market is less than 400 million, then the MSR releases 100 million into the market.

This mechanism is intended to stabilize the EU ETS (EU Emissions Trading System) and strengthen the carbon price signal reducing gradually the surplus allowances. The MSR is included in the EU ETS review currently in discussion.

Discussions on the review of ETS have been held since July 2015 and overlap debate on Non-ETS sectors (transport, buildings, agriculture, waste, land-use and forestry) since 20 July 2016, when the EC has sent to EU legislative bodies its draft on the Effort Sharing Regulation

On 30 November 2016 the EC has published the package Clean Energy for all Europeans, containing the legislative proposals to complete the implementation of the energy internal market and to achieve the environmental 2030 Targets, materialising the ideas drafted in July 2015 communications. November 2016 package involves the wholesale and retail markets and the frameworks for renewable energy sources and energy efficiency. It assesses the implementation of capacity mechanisms fully compatible with EU State Aid Guidelines on Energy and Environment.

The full package represents over 70 documents of which 8 are legislative proposals of high impact on energy markets to be discussed by the European Parliament and Council over the next two years. Practical implementation to market operation is expected to take in place by 2020.

4.2 Other EU regulation

The following regulations of significance to the energy sector were approved in 2015 and 2016:

- On 28 November, the Directive 2015/2193 on the limitation of emissions of certain pollutants into the air from medium combustion plants. This Directive establishes the mandatory register of this units, specific limit for certain components (sulphur dioxide, nitrogen oxides, ammonia and volatile organic compounds) and rules to control other pollutants (carbon monoxide). The maximum deadline of adaptation contemplated in the Directive for certain existing plants is 2030.
- In January, the OJEU published *Delegated Regulation 2016/89 amending Regulation 347/2013, concerning the Union's list of projects of common interest*. It is an update of the first list of Projects of Common Interest of 2013. New projects are added and others disappear (basically those for which implementation has begun). This list was published for the first time by the European Commission on 18 November 2015, at the time of the State of the Energy Union Report.
- Paris Agreement: On 11 April, Decision (EU) 2016/590 of the Council was published, regarding the signing, on behalf of the European Union, of the Paris Agreement approved by virtue of the United Nations Framework Convention on Climate Change. The signing took place in New York on 22 April 2016.

Following the vote of the Plenary Session of the European Parliament of 3 October backing the decision of the Environmental Council of 30 September, the Paris Agreement adopted at COP21 was ratified. On 7 October, the Slovak Presidency submitted the instrument of ratification to the UN. Thus, the EU can attend the summit of Marrakesh from 7 to 18 November (COP22) with full capacity to take part in the conversations regarding the implementation of the Agreement. Notwithstanding, the ratification should be backed by all Member States, a step that has so far only been taken by seven countries (Hungary, France, Slovakia, Austria, Malta, Portugal and Germany). The Paris Agreement enters into force 30 days after being ratified by 55% of countries that make up at least 55% of emissions. Prior to this ratification, 62 countries representing 52% of global CO₂ emissions had ratified it.

- On 17 November 2016, the OJEU published the Regulation 2016/1952/EU on European statistics on natural gas and electricity prices and it repeals the Directive 2008/92/EC. This legislation establishes a harmonised framework to elaborate and disclose the statistics on gas and electricity prices, both for residential customers and for companies. The new rules allow more transparent understanding of the different price components, splitting energy, networks and “taxes and other”. This last component reflects, inter alia the VAT, other taxes and support to policies through customer charges, particularly the support to renewable energies.
- On 19 December 2016, the OJEU published the Directive (EU) 2016/2284 on the reduction of national emissions of certain atmospheric pollutants, amending Directive 2003/35/EC and repealing Directive 2001/81/EC. This new Directive establishes stricter emission limits for each Member State in the period 2020 – 2030 for five pollutants: sulphur dioxide (SO₂), nitrogen oxides (NO_x), non-methane volatile organic compounds (NMVOC) and ammonia (NH₃). Levels for 2020 are equivalent to the adopted by the UE in previous regulations but levels for 2030 are significantly reinforced. The Directive shall be transposed to local regulation by 30 June 2018. Each Member State shall develop a national air pollution control programme by 2019 to ensure the compliance of the targets of this Directive regarding transport, agriculture and energy sectors.

4.3 Industry regulation in Spain

The National Commission for Market and Competition (CNMC) is as a public body attached to the Ministry of Energy, Tourism and Digital Agenda and is subjected to parliamentary scrutiny. It has the functions of market regulation and supervision.

Industry regulation and functioning of the electric system in Spain

The electric sector is regulated by the Electric Industry Law 24/2013, of 26 December 2013.

The following summarises the principles that rule Law 24/2013.

1. Activity separation

The regulation prescribes a separation between the activities carried out in the competitive sector and others that are considered to be regulated activities. Companies that carry out any activities defined by the law as regulated (economic and technical management of the system, transmission and distribution) must have these as their sole corporate purpose and cannot, therefore, engage in unregulated activities (generation, wholesale and retail or other activities unrelated to electricity or activities abroad). However, a group of companies can carry out incompatible activities provided that these are performed by different companies within it and meet independence criteria. In addition, it prescribes a separation between regulated and deregulated activities for accounting purposes.

2. Competition in power generation activity through the following measures

- The production of electricity is developed in a free competition environment.
- Generation dispatch is determined by the daily market. The producers of electricity, except for special cases and exception foreseen by law, tender hourly bids for the selling price of electricity of each of the production units owned by them. The operating order of the production units is established on the basis of the lowest bids made until demand is satisfied in each programming period and the energy produced in each programming period is remunerated at the price matched between supply and demand. There is also the option of going to the intraday markets (six every day), where operators can adjust their positions with respect to their daily programmes. Meanwhile, the production plants contribute to the provision of whatever additional services may be necessary to guarantee supply, obtaining additional remuneration for such services.
- In addition to the market remuneration, the Ministry of Energy, Tourism and Digital Agenda may establish remuneration entailing payment for capacity. In this regard, Orders ITC 2794/2007, ITC 3860/2007 and ITC 3127/2011 regulate payments for capacity, which consist of an investment incentive, an environmental incentive and an availability service. The Royal Decree-law 13/2012 temporarily modifies the investment incentive and the environmental incentive until a new capacity payment system is developed.
- The installation of new generating facilities is considered to be deregulated, without prejudice to the obtainment of the necessary authorisations.
- Producers are entitled to use in their generating facilities the primary energy sources that they deem most appropriate, subject to such restrictions with respect to the environment, as might be established in the legislation in force.

- On 10 June 2014, the Royal Decree 413/2014 on electricity generation by means of renewable, cogeneration and waste facilities was published, confirming a new remuneration scheme for those installations that are not able to achieve the minimum level necessary to recover the costs and compete in a equality manner with the rest of the technologies of the market, obtaining a “reasonable rate of return”. The new specific remuneration scheme consists of the sum of:
 - o “investment remuneration” (EUR/MW) to cover, where applicable, the investment costs that cannot be recovered from the sale of electricity in market; and
 - o “operation remuneration” (EUR/MWh) to cover, where applicable, the difference between the operating costs and income obtained in the electric market.
- This new specific remuneration scheme will be calculated on the basis of a standard installation during its useful regulatory lifetime and referenced to the activity carried out by an “efficient and well-run company” according to the following standards:
 - o the revenues from the sale of power;
 - o the operation costs needed for the activity; and
 - o the value of the initial investment.

This remuneration regime will be based on a reasonable rate of return of the investments, defined on the basis of the average yield on 10 year government bonds plus a differential, initially fixed at 300 basis points for the first regulatory period ending on 31 December 2019 (that is, 7.398% before taxes).

Six year regulatory periods and three year regulatory sub-periods have been set. The remuneration parameters related to the market price forecasts may be changed every three years, including the deviations produced in the sub-period. The standard parameters of the installations may be changed every six years, except for the standard initial investment value and the regulatory lifetime, which will remain unchanged during the installations’ regulatory lifetime. The reasonable rate of return may be changed by law every six years, but only for remuneration in the future. The return on operation in circumstances where the operating cost of a technology is dependent on fuel prices may be changed at least once a year. The last Order published regarding to update this operational costs is the Order IET/1345/2015.

The standard value of the investment for new installations will be set through a competitive tendering process.

On the other hand, the Royal Decree 413/2014 established that an order from the Ministry of Industry, Energy and Tourism will establish a classification of standard installations in terms of the technology, installed capacity or any another characteristic that may be considered necessary for the application of this remunerative scheme. Hence, on 20 June 2014, the Ministry published the Order IET/1045/2014, of 16 June 2014 approving the remuneration parameters for standard installations already in operation.

The Royal Decree 947/2015 stipulates a call for the granting of the specific remuneration regime to new biomass-based electricity production plants within the peninsular power system and to wind technology farms. A maximum of 200 MW of biomass and 500 MW of wind will be assigned (new or repowered). The allocation procedure and the remuneration parameters are set out in the Ministerial Order IET/2212/2015, of 23 October 2015. The auction was called by the State Secretariat for Energy’s resolution of 30 November 2015.

Said auction was held on 14 January 2016. All of the MW, both wind and biomass, were allocated, with the peculiarity that in both technologies, the discount proved to be 100%, so that no awardee will receive remuneration for investment costs.

To date, new auctions of renewable capacity have not yet been called, although it is expected that in 2017 new calls may be made, with the objective of meeting the commitments of 2020.

3. Guarantee of the proper functioning of the system, by using the following measures

- Functioning of the system: Red Eléctrica de España, S.A. carries on the transmission management and system operation activities. As system operator, it is responsible for managing the adjustment markets to guarantee a balance between energy demand and generation.
- Functioning of the market: With the creation of the Iberian Electricity Market (MIBEL), since July 2006 the Portuguese and Spanish forward markets operate on an integrated way, and since July 2007 so have the short-term daily and intra-day markets. Currently the Iberian Market Operator (OMI) is responsible for the operation of MIBEL. OMI originated in the fusion of OMI-Spain, responsible for the management of the daily and intra-day markets, and OMI-Portugal, responsible for the forward market.

4. Legislation in force for regulated activities

Law 24/2013 establishes that distribution and transmission are classified as regulated activities that are not subject to the free competition and market regime.

The Royal Decree-law 9/2013 fixes the transitory methodology that will rule the transmission and distribution activities until the new royal decrees for these activities are approved. On one hand, it established that, for the revenue of these activities, an “*efficient and well-run company*” will be considered applying uniform criteria throughout the Spanish territory. On the other hand, it established that these economic regimes allow adequate revenue of a low-risk activity. The methodology used to calculate the revenue for the distribution activity defines a “regulatory assets base” for the activity that evolves upwards according to the investments made and downwards according to the related depreciation, in order to fix its revenue. In the application of these principles it established a rate of return on assets linked to government bonds plus a spread.

Subsequently, Law 24/2013, published on 26 December 2013, introduced the following amendments:

- Introduction of the “*efficient and well-run company*” concept, considering these activities as low risk.
- The regulatory periods extend to six years.
- For regulatory purposes, the accrual and collection of the remuneration generated by the installations that entered into operation in the year n starts in the year $n+2$.
- The assets in operation not fully depreciated will receive an investment remuneration considering their net value for the financial remuneration. The financial remuneration rate will be based on ten year government bonds plus an appropriate spread for a low risk activity.

On 30 December 2013 two royal decrees regulating the new remuneration methodology of the transmission (Royal Decree 1047/2013) and distribution (Royal Decree 1048/2013) activities were published, following the regulatory and tax measures that started in the second half of 2013.

The methodology set out in the Royal Decree 1048/2013 is based on new standard investment and operation costs. The aim is to reduce costs by introducing efficiency mechanisms and limitations concerning the annual investment volume. The recalculation of the base remuneration will be carried out during its first year of implementation, which includes the initial regulatory asset of the companies that can vary with respect to the one recognised in the Royal Decree-law 9/2013. Investment limits are also established (sector's maximum 0.13% of Gross Domestic Product). The financial remuneration rate of the asset embodies the principles established in Law 24/2013, referenced to ten year government bonds plus an appropriate spread for a low risk activity.

The Royal Decree 1048/2013 includes changes in the existing incentives; in quality (it may fluctuate between +2% and -3% of the company's remuneration) and losses (it may fluctuate between +1% and -2%). A new incentive regarding fight against fraud has been created, which may reach 1.5% of the company's remuneration. For the application of the new remuneration model contained in the Royal Decree 1048/2013, its regulatory development must be published; until then, as established in the Royal Decree 1048/2013, the remuneration scheme of the Royal Decree-law 9/2013 will be maintained.

The remuneration system culminates with Orders IET/2659/2015 for electricity transmission and IET/2660/2015 for electricity distribution, published on 12 December 2015, which determine the type of installations and unit values to consider when calculating the remuneration for 2016 onwards.

Given that the order was approved during December 2015, it was not possible to make the remuneration calculations resulting from the application of the unit values approved in the Order IET/2660/2015, of 11 December. For this reason, the Order IET/2735/2015, of 17 December –by which tariffs for access to electrical energy are established for 2016, and specific standard facilities and remuneration parameters for electrical energy installations from renewable energy, cogeneration and waste sources are approved– established an amount as payment on account until company remuneration was established under the mentioned the royal decree.

Lastly, the Order IET/980/2016, of 10 June, was published, by which remuneration of electrical energy distribution companies is established for 2016. This remuneration, with the exception of the incentive or penalisation for reduction of losses, will be definitive for the year 2016, and will amount to EUR 5,162.6 million, of which the amount of EUR 1,655.5 million corresponds to Iberdrola Distribución Eléctrica.

Transmission Remuneration: That same day, the Order IET/981/2016, of 15 June, was published, by which remuneration of companies owning electrical energy transmission installations is established for 2016. Final remuneration for 2016 for companies that own transmission facilities will amount to EUR 1,710 million.

5. Access tolls

Access tolls are uniform across the country and are collected by the distributors, which act as the collector agents of the electric system.

The Royal Decree-law 14/2010, of 23 December 2010, extended the application of access tolls to electricity producers and established that the producers would be regulated taking into consideration the energy fed into the grid. In addition, prior to further tolls being implemented, the Royal Decree-law 14/2010 established that an access toll of EUR 0.5 per MWh fed into the grid will be applied to producers that are connected to the grid.

Subsequently, the Royal Decree 1544/2011, of 31 October 2011 implemented the aforementioned regulation of access tolls for electricity producers.

Law 32/2014, of 22 December 2014, on metrology, modifies Law 24/2013, clarifying that the legal authority to establish the structure and conditions applicable to the access tolls for transmission and distribution networks corresponds to the Government.

The Order IET/2735/2015, of 17 December 2015, establishes the access tolls for 2016.

6. Progressive deregulation of electricity supply and introduction of wholesale and retailing activity

The supply of electric power is completely deregulated and all consumers must contract their supply of electricity with a trader. From 1 July 2009, those consumers who fulfil certain criteria have been able to opt to contract the electricity supply with a Last Resort Trader (CUR), which from July 2014 became a Reference Trader (COR), with the Last Resort Rate (TUR), now the Voluntary Price for the Small Consumer (PVPC). The TUR has been maintained for vulnerable consumers and those who do not fulfil the requirements for the PVPC and who temporarily do not have a current contract with a free market trader.

Law 3/2014, of 27 March 2014, obliges CORs to offer contracts in which the price of electric power is fixed for a specific period for consumers with a right to the PVPC.

The Royal Decree 216/2014, of 28 March 2014, established the methodology for calculating the PVPC and their legal regimen for contracting. It determines the structure of the PVPC that will be applicable to low voltage consumers with a contracted capacity up to 10 kW. Similarly, it determines the procedure for calculating the production cost of electric power on the basis of the hourly price in the daily market during the billing period. In addition, as established by Law 3/2014, it provides the option for consumers to contracting an electricity price fixed for a year with the reference trader.

This legislation provides the Spanish electricity sector with three ways in which traders can supply power to consumers:

- Reference supply:
 - o PVPC: the method that has been applied by default from 1 July 2014 if the consumer was subject to the previous TUR.
 - o Annual fixed price in a regulated market offered by the reference trader.
- Contracting in the deregulated market with a reference trader.
- Last Resort Supply: a form of supply applicable to vulnerable consumers and those who do not fulfil the requirements for the PVPC and temporarily do not have a current contract with a free market trader.

The Resolution of 2 June 2015 of the State Secretariat for Energy, approved six procedures necessary for billing hourly to those consumers covered by the PVPC. This resolution establishes a period of adaptation of IT systems until 1 October 2015. From this date onwards, all consumers having an hourly meter should be billed according to the hourly consumption and price.

On 6 February 2016, the Supreme Court issued a judgment (dated on 3 November 2015) that cancels the commercial fix margin used to establish the PVPC, which is the Reference Trader's remuneration. The Supreme Court overturns the current value of 4 EUR/kW/year with effect from 1 April 2014 and orders the Government to set a new value after establishing a new methodology. Until then, the current value will be used for billing as a temporary value, as it is set out in the Order IET/2735/2015 of electric tolls for 2016.

On 25 November, the Royal Decree 469/2016 was published. It modified the Royal Decree 216/2014 and established the methodology of calculation of the Voluntary Price for the Small Consumer of electric energy (this royal decree established a Reference Trader's remuneration of EUR 4 /kW). It also established its contracting legal regime.

The methodology included the recognition of the costs to carry out the reference retail activity, taking as reference the costs of the three most efficient reference trader and excluding the face-to-face channel, plus a fee for the exercise of the activity (1.05% on energy price). The reference traders must keep a cost accounting, according to criteria and rules to be determined by Ministerial Order.

On 24 December, a Ministerial Order was published with the concrete values, both for the past (from 1 April 2014) and the future (until 2018), establishing a fixed and variable term for the allocation of the Reference Trader's margin.

The reference traders will regularize the past through a customer rebilling in the 9 months after the publication of the Ministerial Order (consumptions made from 1 April 2014 to the publication of the order). In the billings made by each reference traders prior to that date, the value of EUR 4 per kW and year established in Royal Decree 216/2014, (annulled by the Supreme Court rulings), will continue to be applied on a transitional basis.

7. Price formation and tariff structure

Law 24/2013 regulates the aspects relating to the PVPCs, which are defined as the maximum prices that the suppliers that assume the reference supply obligations will be able to charge.

They will be calculated as the sum of the following items:

- the production cost of electricity, based on market mechanisms, taking account of the average price set in the production market during the billing period;
- the corresponding access tolls and fees; and
- the corresponding supply costs.

8. Social tariff

The Royal Decree-law 9/2013 sets out the social tariff for consumers with certain social, consumption and purchase power characteristics supplied at the TUR at their normal residence, and the financing of the social tariff costs. This tariff is calculated as 25% of the PVPC. Until the social and economic indicators are developed for application, the social tariff will apply to individuals in their normal residence supplied under the last resort scheme with contracted capacity of less than 3 kW, to large families or families whose members are all unemployed and to certain pensioners 60 years old or older receiving minimum pensions.

Such costs shall be borne by the parent company of the vertically integrated companies. The allocation of the social tariff costs among such companies will be made according to the number of supplies connected to the distribution network and the number of customers of the retail business of the group.

In the Royal Decree 968/2014, of 21 November 2014, the methodology for fixing the distribution percentage of the amounts to be financed with regard to the social tariff is developed. These percentages will be calculated annually by the CNMC for each business group, as the relation between (i) the sum of the annual averages of the number of feeds connected to the distribution networks of the distributors and of the number of customers of the distributors in which the group participates, and (ii) the sum of all the annual average values of feeds and customers of all the business groups that should be considered for the effects of this sharing.

On 20 October 2015, the Ministry published the Order IET/2182/2015, of 15 October, which set the percentage of the amounts to be financed with regard to the social tariff for 2015. According to this order, Iberdrola should finance 38.26%.

On 10 September, the Order/IET/1451/2016 was published. This order establishes the distribution percentages of the amounts to be financed regarding the Social tariff corresponding to 2016. This order assigns a 37.951119% to Iberdrola España, S.A.U., to be applied as from settlement number 8 of the Social tariff (August). Up until the publication of the order a provisional percentage of 37.97% was applied.

On 30 November, the judgments of the appeals filed by the companies Viesgo, Endesa, Iberdrola and Gas Natural against the Royal Decree 968/2014 were published. This Royal Decree developed the methodology for setting the percentages of Social tariff's finance. In the aforementioned judgments, the Supreme Court recognizes the claim of the companies and annuls the system of financing the Social tariff as discriminatory. The financing companies must be compensated for the amounts contributed in 2015 and 2016 (affected by the annulled articles of RD 2014), with their corresponding interests. As a result, the last settlement of Social tariff made in 2016, (up to the closing date of the year), was the settlement 8 for the period January – August.

Subsequently, on 24 December, the Royal Decree-law 7/2016 was published, which regulates the mechanism for financing the cost of Social tariff and other measures to protect vulnerable electricity consumers. This royal decree-law establishes a new mechanism for financing the Social tariff, charging to the commercialization activity, with immediate entry into force. Until the regulatory development, the trading companies of Iberdrola would finance 35.5% up from 37.97% attributed to the Iberdrola Group in the previous system.

In addition, it creates a second group of "severe vulnerable consumers" who must not have their supply interrupted, as well as co-financing their invoices by the "competent Administrations" and by the same Social tariff funders. This measure must be developed by regulation in 3 months.

9. Load Manager

The Royal Decree-law 6/2010 introduced the load manager as another agent in the electrical system.

The Royal Decree 647/2011, which was approved in May 2011, regulates the functions of load managers, defined as "*companies that, as consumers, are authorised to resell electricity for power recharging services. Load managers are the only subjects with wholesale customer character under the terms provided for the applicable community regulations.*" The Royal Decree 647/2011 sets forth the requirements and obligations of load managers. It also created a new super off-peak tariff applicable to contracts of up to 15 kW, thereby creating a third hour period (from 1 a.m. to 7 a.m.) aimed at encouraging the charging of electric vehicles in this period.

10. Emission allowances

Regarding environment regulations, the issue of CO₂ emissions allowances is critical. This concerns the obligation placed on industry and electricity companies by Directive 2003/87/CE to deliver an emission allowance for each ton of CO₂ emitted by a plant, and the cap is reduced over time so that total emissions fall. In 2020, emissions from sectors covered by the EU ETS will be 21% lower than in 2005.

In 2009, within the European Union's Green Package for energy and climate change, Directive 29/2009/CE was approved, introducing changes and extending the European Union emissions trading system beyond 2012. Phase 3 (2013-20), significantly different from previous phases, is based on rules which are far more harmonised than before. The main changes in the directive were: the default method of allocating allowances is auctioning, not free allocation, although transitional free allocation is envisaged in some cases; extension of the periods of compliance to be followed by consecutive periods in which the amount of rights is determined on an European Union-wide scale; it also provides that allowances can be carried over one period to the next. As a result of the new rules, since 2013, IBERDROLA has no longer had the right to receive any free allocation.

The auctioning of allowances is governed by the EU ETS auctioning Regulation. This covers the timing, administration and other aspects of auctioning to ensure it is conducted in an open, transparent, harmonised and non-discriminatory manner. Two auction platforms are in place: European Energy Exchange (**EEX**) (common platform for the large majority of countries participating in the EU ETS) and Futures Europe (**ICE**) (acts as the United Kingdom's platform). The Member States' shares in the auctioning volume in 2013 to 2020 are distributed as follows: (i) 88% on the basis of their share of verified emissions in 2005 or the average of the 2005-2007 period, (ii) 10% are allocated to the least wealthy EU member states as an additional source of revenue to help them invest in reducing the carbon intensity of their economies and adapt to climate change, and (iii) the remaining 2% is given as a 'Kyoto bonus' to nine EU Member States, which by 2005 had reduced their greenhouse gas emissions by at least 20% of levels in their Kyoto Protocol base year.

A surplus of emission allowances has built up in the ETS since 2009, largely due to the economic crisis (which has reduced emissions more than anticipated) and high imports of international credits. This has led to lower carbon prices and thus a weaker incentive to reduce emissions. The European Commission (EC) is addressing this through short- and long-term measures. As a short-term measure the European Commission postponed in February 2014 the auctioning of 900 million allowances until 2019-2020 ("backloading").

As a long-term solution, changes will be introduced to reform the ETS by establishing an MSR as of 2018, operating from 1 January 2019. The reserve will address the current surplus of allowances and improve the system's resilience to major shocks by adjusting the supply of allowances to be auctioned. It will operate entirely according to pre-defined rules. The 'backloading' was also amended by MSR Decision, passed in October 2015: backloaded allowances will not return to the market in 2019-20, instead they will be introduced in MSR.

11. Toll balance

Electricity Industry Law 54/1997, of 27 November, introduced the liberalisation of electricity generation and retailing activities. The difference between the access toll revenue established by the Government and real costs related to these tolls resulted in a revenue shortfall which led to problems and modifications in the functioning of the system.

To fund this shortfall, which is deferred through the recognition of long-term collection rights recovered by the annuities incorporated in annual fees, a series of measures have been adopted.

The first measure was the Royal Decree-law 6/2009, of 30 April 2009, that set limits to the increase of the shortfall and defined a framework for the gradual sufficiency of the access tolls. It also addressed the mechanism for funding the toll shortfall through a securitisation fund set up for this purpose: Electricity system deficit securitisation fund (**FADE**).

As measures adopted since 2009 proved to be insufficient throughout 2013, the Government carried out a process of regulatory and tax reform for the electricity sector. As a step prior to this reform, the Law 15/2012 established new tax measures and the Royal Decree-law 9/2013, was approved, adopting urgent measures to guarantee the financial stability of the electric system and modified the methodology for the calculation of the remuneration of the transmission and distribution activities, special regime and capacity payments, among other measures.

Finally, Law 24/2013 is governed by the principle of economic and financial sustainability of the electricity system, meaning that any regulatory measure which causes an increase in costs or a reduction in income for the electricity system should incorporate an equivalent reduction of other cost items or an equivalent increase in income that ensures the equilibrium of the system. Thus, the possibility of new deficits accumulating, as have occurred in the past, is ruled out.

This principle is reinforced with the obligation to automatically review the tolls and fees if the temporary imbalances between revenues and costs of the electricity system exceed the following limits from 2014 onwards:

- 2% of the income estimated for the system in a given year.
- The accumulated debt due to imbalances in preceding periods may not exceed 5% of the income estimated for the system in a given year.

The part of the imbalance that, without exceeding such limits, is not compensated by increases in tolls and fees will be financed by the parties to the settlement system in proportion to the remuneration that corresponds to them for their activities.

The amounts thus contributed will be returned in the corresponding settlements during the following five years together with an interest rate equivalent to the market rate.

In contrast to the previous system, these imbalances will not be financed exclusively by large companies and the collection rights corresponding to income deficits may not be assigned to the Securitisation Fund of the electricity system debt after 1 January 2013.

With regard to the excess income that could arise, it will be used to compensate imbalances from previous years and, as long as there are debts pending from previous years, the access tolls and fees may not be revised downward.

The Royal Decree 680/2014, of 1 August, regulates the procedure of budgeting, recognition, settlement and control of the surcharges on the production of electric power in the isolated electricity systems of the non-peninsular territories charged to the Central State Budgets, thus developing the provisions of Law 24/2013, which established that from 1 January 2014, 50% of these surcharges would be financed against the Central State Budgets.

At the end all these measures have enabled the final statements of 2014 and 2015 to be closed with a surplus of EUR 550.3 million and EUR 469.3 million respectively. This surplus will not be used as an income in the regulated settlement of the current financial year.

12. Self-consumption

Self-consumption is regulated for the first time in the Law 24/2013 and defined as the electric energy provided by generation installations associated with a consumer. Self-consumers must pay the same access toll for the consumed energy as other customers (from the network or from your own installation). In addition, a mandatory register for self-consumption installations is created.

Later, the Royal Decree-law 9/2015 of 10 July modified Law 24/2013 to establish the possibility of setting reductions in tolls, fees and costs for certain categories of consumers for which the maximum contracted power consumption and generation installed shall not exceed 10 kW. This measure is exceptionally and it will be implemented as long as the safety and economic and financial sustainability of the system is ensured.

Finally, the Royal Decree 900/2015 of 10 October regulated the administrative, technical and financial conditions of the self-consumption modalities. It differentiated between two types of self-consumption:

- Supply with self-consumption: a consumer in a single electricity supply point or installation, with an internal network of one or more installations to generate electricity for self-consumption, which were not registered as generation facilities. In this case, the consumer is a single subject. The contracted power shall not exceed 100 kW and discharges of energy to the grid do not receive monetary compensation.
- Production with self-consumption: a consumer in an electricity supply point or installation associated with one or several production facilities duly registered in the administrative record of energy production facilities. In this case there are two subjects - the consumer and the producer.

Regarding the economic regime, and until charges associated with system costs are approved, the self-consumer must pay a fixed charge and a variable charge applicable to the self-consumed energy. However, those consumers who fall into the supply with self-consumption modality and have contracted power less than or equal to 10 kW will be exempt from the temporary charge for the self-consumed energy, the insulated electrical systems (Canarian Island, Ceuta, Melilla, Ibiza and Formentera), and cogeneration until 31 December 2019. Self-consumers also pay network tolls for the use of the network, like other consumers.

13. Interruptibility

The interruptibility service for a consumer consists in the reduction of its contracted capacity in response to a reduction order from the system operator. This order will be given taking account of the needs that arise in the operation of the electricity system, according to criteria of security and lowest cost.

The system operator will request the execution of the capacity reduction option, following economic and technical criteria:

- Economic criteria: In situations where the application of the service has a lower cost than that of the adjustment services of the system.
- Technical criteria: As a rapid response mechanism in emergency situations in the operation of the system.

To execute the option, the system operator will send a power reduction order to the service providers who will reduce their active power demanded until the committed residual power values are fulfilled.

The allocation of the interruptibility service will be carried out through an auction procedure managed by the system operator, as established in the Order IET/2013/2013, guaranteeing the effective provision of the service and its execution at the lowest cost for the electricity system.

Finally, the resolution published on 12 August 2016 approves the rules of the competitive procedure of auctions for the allocation of the service of interruptibility. It also approves the model of adhesion to the legal framework (established for participation in the auctions). On 12 October was published the resolution approving the calendar and characteristics for the 2017 electric season of the competitive auction procedure. These auctions took place during the week of 14 to 18 November. The total cost amounted to EUR 524.8 million with a total allocated power of 2,975 MW and an average price of EUR 176,420 / MW.

Relating to the interruptibility, a resolution has been published which sets the average price of energy to be applied in the calculation of the remuneration of the service of interruptibility offered by consumers of non-mainland electric systems to which it is applicable Order ITC/2370/2007, of 26 July, during the fourth quarter of 2016. Its value is fixed at EUR 42.40 / MWh.

14. Energy efficiency

Energy efficiency is an essential aspect of the European 2020 strategy for sustainable growth and one of the most effective forms of strengthening the security of energy supply and reducing emissions of greenhouse gases and other pollutants. In this sense, the European Union has set itself the target of achieving a 20% improvement in energy efficiency by 2020.

Law 18/2014, of 15 October, approving measures for growth, competitiveness and efficiency, contains a set of mechanisms designed to achieve the energy saving targets established in the Energy Efficiency Directive. To this end, it created the National Energy Efficiency Fund, managed by the Institute for the Diversification and Saving of Energy (*Instituto para la Diversificación y Ahorro de la Energía*) and financed by an annual contribution from all suppliers of gas and electricity, wholesalers of oil products and of liquid petroleum gases, according to their sales. The Order IET/289/2015, of 20 February, established the contribution obligations for 2015.

Law 8/2015, of 21 May, modified Law 18/2014 and established that the obliged entities must make an annual contribution from 2016 onwards to the National Energy Efficiency Fund in four instalments: on 31 March, 30 June, 30 September and 31 December of each year. In addition, in order to establish the annual contribution for each obliged entity, positive or negative adjustments can be made, resulting from data provided by the obliged entities, such as sales and other variables, and data set out by the relevant ministerial order of the previous year.

Finally, the Order IET/359/2016 of 17 March established the contribution obligations for 2016.

· Industry regulation and functioning of the gas system in Spain

The natural gas sector in Spain has undergone significant changes in its structure and operation in the last ten years, from a monopoly to a fully open market, driven mainly by the deregulation measures about natural gas internal market in European directives (2009/73/EC Directive is currently in force) aimed at opening up markets and creating a single European gas market.

These liberalised principles have been incorporated and developed in Spanish law through the Hydrocarbon Industry Law 34/1998, which began the deregulation process and, more recently, through the Law 12/2007 and the Royal Decree-law 13/2012 which completed this process.

The Hydrocarbon Industry Law of 1998 laid the foundations for the new gas system, particularly with regard to the separation of activities (regulated and deregulated), the introduction of third-party access to the regulated network, the abolition of the former concessions for piped gas supply and their conversion into regulated administrative permits, and the establishment of a timetable for progressive market deregulation.

In line with these principles, the gas system has been structured around two types of activities: regulated activities (regasification, basic storage, transmission and distribution) and deregulated activities (trading and supply).

The Hydrocarbon Industry Law 34/1998 provided for the legal separation of deregulated and regulated activities and the segregation for accounting purposes of the various regulated activities. In addition, with the publication of Law 12/2007, Spain moved a step closer to achieving functional separation between network activities and deregulated activities and between network activities and technical system management. In 2012, the Royal Decree-law 13/2012 was approved, transposing Directive 2009/73/EC, and establishing further measures of separation in management of the transmission network.

Although the Hydrocarbon Industry Law established the general principles of the new Spanish gas system, the sector's deregulation did not come into practice until 2001, after the publication of the Royal Decree-law 6/2000, on urgent measures to intensify competition in the goods and services markets, and the Royal Decree 949/2001, regulating third party access to gas installations and establishing an integrated economic system for the natural gas sector.

The first of these decrees enacted certain elements of the Hydrocarbon Industry Law with the aim of fostering measures that would facilitate the elimination of entry barriers for new supply companies. In particular, it created the technical system manager (ENAGAS, S.A.), provided for a 25% gas release under the contract for natural gas brought from Algeria through the Maghreb pipeline, and brought forward the timetable for deregulation.

The second, the Royal Decree 949/2001, established firstly the specific terms and conditions for third-party network access and, a remuneration system for regulated activities and a cost-based system of tariffs, tolls and fees structured according to pressure levels and consumption bands.

The remuneration assigned to each company as well as the tariffs, tolls and fees are updated periodically by ministerial orders and resolutions.

The economic system also established a settlement procedure that would allow for redistribution of revenues collected in the form of tariffs, tolls and fees between the various regulated activities in accordance with the remuneration method established. The body responsible for effecting this redistribution is the Ministry of Energy, Tourism and Digital Agenda.

Other issues related to the regulation of the transmission, distribution and supply businesses, the administrative authorisation procedures for natural gas facilities and the regulation of certain aspects of the supply business are dealt with in the Royal Decree 1434/2002.

As for the technical operation of the system, the operating regulations are established in the Order ITC 3126/2005 enacting the gas system technical management rules. Inter alia, these regulations established that each operator is individually responsible for maintaining its liquidity and enacts specific protocols for the conduct of the technical system manager in exceptional operating circumstances.

Despite the sector's progressive deregulation, prevailing regulation upholds the state's obligation to ensure the safety and continuity of supply. To this end, the Royal Decree 1766/2007 stipulates that direct market suppliers and consumers must maintain minimum security stocks equivalent to 20 days' consumption. In addition, it limits the maximum percentage of gas supplies that may be sourced from a single country to 50%.

The state also maintains responsibility for obligatory planning work for certain infrastructures (for example, gas pipelines forming the core transmission network, the secondary transmission network, determining the total liquid natural gas regasification capacity necessary to supply the system and core natural gas storage facilities). For all other infrastructures, the state's planning work is indicative only. In 2012, the Royal Decree-law 13/2012 enacted a series of measures to halt the construction of new infrastructure in a context of falling demand for gas.

As mentioned above, in Spain the deregulation process was completed with Law 12/2007 transposing Directive 2003/55/CE. The two key changes enacted by this law were the elimination of regulated supply and the functional separation between network activities and deregulated activities.

In the Spanish electric system, the market deregulation process was completed on 1 July 2008 with the elimination of regulated supply for customers and the creation of last-resort supply. Currently, low-pressure customers with annual consumption of less than 50,000 kWh who do not choose another supply option shall be supplied by a last-resort supplier at a price calculated automatically. This additional rate is called the last resort tariff.

Law 18/2014, on measures for growth, competitiveness and efficiency, previously the Royal Decree-law 8/2014 established the principle of economic and financial sustainability for the gas system. This principle is reinforced with the obligation to automatically review tolls and fees if the annual imbalance between revenues and costs of the gas system exceeds the following limits:

- 10% of the income receivable for the year; or
- 15% of the sum of the annual imbalance plus annual payments recognised and pending amortisation.

The part of the imbalance that, without exceeding the above limits, is not compensated by the increase in tolls and fees, will be financed by the parties to the settlement system in proportion to their remuneration. The amounts contributed will be returned in the following five years and will earn an interest rate equivalent to the market rate.

The deficit accumulated as at 31 December 2014 will be financed by the owners of the installations during a period of 15 years.

On the other hand, the remuneration of the regulated activities will be based on the costs necessary for an efficient and well-managed company to carry out the relevant activity, following the principle of performing the relevant activity at the lowest cost for the gas system. In addition, the remuneration of regulated activities will be on the basis of six-year regulatory periods. The first regulatory period ends on 31 December 2020.

The remuneration system for distribution is based on the remuneration of the previous year, adjusted for changes in productivity and new customers.

The remuneration system for transmission, storage facilities and regasification is based on the net value of the associated assets. In addition, the associated operating and maintenance costs and premiums for continuity of service are also factored in to calculate the remuneration system.

The Hydrocarbon Industry Law has been modified by Law 8/2015, 21 May 2015.

The main aspects introduced by Law 8/2015 regarding the gas system are:

- The creation of an organised wholesale gas market.
- The designation of the operator of the regulated gas market.
- Some measures relating to minimum security stock levels are adopted.
- CORES (*Corporación de Reservas Estratégicas de Productos Petrolíferos*) is enabled to constitute, maintain or manage natural gas and liquefied natural gas strategic stocks.
- With respect to the Efficiency Fund (*Fondo Nacional de Eficiencia Energética*) the law permits the refund of contributions when necessary (in case of mistake, for example).

- A new fiscal regime is established, benefiting the landowners and regions (*Comunidades Autónomas*) where the activities of exploration, investigation and production with conventional and non-conventional (including fracking) techniques are developed.
- Inspections may be carried out by any natural gas installation company (not only distribution companies).

Finally, the Royal Decree 984/2015 of 30 October 2015 regulated the organised wholesale gas market and the third party access to the facilities of the natural gas system. This market will initially include the negotiation of short-term standardised products by an electronic platform managed by the Market Operator (MIBGAS - OMEL). In addition, this market will centralise the hiring capacity through an electronic platform managed by the Technical System Operator (ENAGAS), with standardised products and auction procedures.

· Alternative energies for transport

The Royal Decree 639/2016, of 9 December, establishes a framework of measures for the implementation of an infrastructure for alternative fuels. This is the transposition of the Directive, which requires each State to set specific objectives and measures to foster infrastructures that allow the deployment of alternative mobility to oil. It contemplates the use of electricity for transportation by road and the supply in ports and airports. It also contemplates the use of natural gas (CNG or LNG) in transport by road or ports.

4.4 Industry regulation in the UK

The principal laws that govern Scottish Power Ltd.'s (hereinafter, **SCOTTISH POWER**) activities are the Electricity Act 1989 (**Electricity Act**) and the Gas Act 1986 (**Gas Act**), as substantially amended and supplemented by numerous subsequent enactments, including the Gas Act 1995, the Utilities Act 2000, the Energy Act 2004, the Energy Act 2008, the Energy Act 2010, the Energy Act 2011, the Energy Act 2013, the Energy Act 2016 and various EU Directives (subject to any changes arising from the UK's forthcoming exit from the EU). These specific energy laws are implemented by UK and EU legislation relating to competition and consumer protection.

1. The Regulatory Authorities

The principal regulatory authority for utilities is the Gas and Electricity Markets Authority (**GEMA**), comprising a chairman and other members appointed by the Secretary of State for Business, Energy and Industrial Strategy (**BEIS**). GEMA is supported by the Office of Gas and Electricity Markets (**OFGEM**). The main instrument of regulation used by GEMA is the licensing regime which in most cases requires the various aspects of the energy industry to be carried out under a licence to which standard conditions apply. In addition, there are a number of statutory obligations, known as relevant requirements, which are enforced by GEMA as if they were licence conditions.

GEMA's principal objective is to promote the interests of present and future consumers and promote effective competition. Under the Energy Act 2010, the interests of such consumers must be taken as a whole, including their interests in the reduction of greenhouse gases and in the security of the supply of gas and electricity to them.

In furthering this objective GEMA must ensure that all reasonable demands for electricity and gas are met, ensure that licence holders are able to finance the activities they are obliged to undertake, and contribute to the achievement of sustainable development. Further provisions concerning the duties of GEMA have been made by the Energy Act 2013, but the provisions in question are yet to be implemented.

GEMA's functions include the granting of licences (and their revocation in certain limited circumstances), the making of changes to licence conditions (including the operation of price controls for the monopoly network functions), the review of industry code modifications, operating schemes for promoting renewable electricity and energy efficiency, and the enforcement of the industry's obligations.

GEMA has the power to impose monetary penalties for past and ongoing breaches of licence conditions and relevant requirements and it can order that redress is provided to consumers. Fines and redress orders for a particular breach can in aggregate be up to 10% of the licensee's applicable turnover.

The principal Regulatory Authority for competition matters is the Competition and Markets Authority (**CMA**). They can undertake general market investigations and, working concurrently with GEMA, can investigate potential breaches of competition law in the utility field. Consumer protection matters are enforced by the CMA, OFGEM and Local Authority Trading Standards departments.

2. Licences

Companies within the SCOTTISH POWER Group hold licences for various functions including:

- the supply of electricity;
- the generation of electricity;
- the distribution of electricity in the South Scotland area, in the Merseyside and North of Wales area;
- the supply of gas;
- the shipping of gas (that is, arranging for the insertion, the transmission, and the removal of it from the public network); and
- the transportation of gas to certain specific sites (such as proposed new gas fired power stations).

The third package of European Union Directives on Electricity (2009/72/EC) established additional restrictions to the ownership of transmission companies. On 19 June 2012, Scottish Power Transmission Limited (SPTL) was certified by OFGEM, in accordance with the Directive's Article 9, with the European Commission approval, on the basis that SPTL's arrangements guarantee more efficient independence than the ITO provisions under the Directive's Chapter V. As a result, the provisions relating ownership separation do not apply to SPTL.

The conditions of licences regulate such matters as:

- for network licences: the quality of service and the charges that can be made.
- for supply to domestic consumers: consumer protection provisions including rules on standards of conduct, provision of information, debt and disconnection, cost reflective pricing, in relation to payment methods, information supply to customers and on treating customers fairly.
- for most types of licence: rules requiring adherence to industry codes that set down the detailed technical rules for operating the industry, and providing for OFGEM to determine whether proposed changes to the codes should go ahead.

The Gas Act 1995 and Utilities Act 2000 introduced standard licence conditions to ensure that all holders of a particular licence type are subject to the same conditions. Under the Electricity and Gas Regulations 2011 (Internal Markets), modifications of individual or standard licencing terms no longer require the holders' consent. However, affected licence holders and other parties can appeal to the CMA on both procedure and substance, except where legislation allows the Secretary of State to modify licence conditions for certain specified purposes (typically the delivery of industry wide reforms). In most cases, these powers are time limited. Changes to licence conditions can also currently be made without the right of appeal in pursuance of a European Union obligation, using powers in the European Communities Act 1972. A market investigation was initiated on 26 June 2014 by GEMA. The investigation was into the operation of retail gas and electricity markets for domestic and small business consumers, and the wholesale markets that support such supply. In June 2016, the CMA published its Final Report which set out the findings from its investigation and its decision on remedies. The report concluded that competition in the wholesale gas and electricity markets works well and that the presence of vertically integrated firms does not have a detrimental impact on competition. No strong case was found for returning to the old "pool" system for the Wholesale Electric Market.

However, a number of adverse effects on competition were identified in the retail market, some due to ill-conceived regulation, but mainly focussed on the 'weak customer response' from the ~70% of customers who are on standard variable tariffs (SVT) and who lose out through lack of engagement in the market. Most of the CMA's remedies are focussed on increasing competition in the SVT segment, including creating a database of disengaged customers (those who have been in the SVT for more than 3 years) which could be used by rival suppliers for marketing, and a programme of trials to develop more effective customer prompts. However, in the case of customers with prepayment meters the CMA decided to impose a transitional safeguard tariff cap, to be set above the "efficient" level of pricing, with the aim of mitigating the damage to competition that might otherwise arise. Other remedies include location-dependent charging for transmission losses, changes to industry settlement processes and code governance, and recommendations to the Government on a number of subjects including GEMA's duties.

The CMA made a number of orders in December 2016 to implement relevant remedies, ahead of its statutory deadline of 23 December to complete implementation. It will remain involved to monitor the implementation and effectiveness of remedies.

3. EU Regulation on Energy Market Integrity and Transparency (REMIT)

GEMA also enforces REMIT in the United Kingdom. It has the power to levy unlimited fines for breaches and since 13 April 2015 can initiate criminal prosecutions for breach of the market manipulation element of REMIT against both companies and the individual employees involved. In the case of individuals, the penalty can include imprisonment for up to two years.

4. Price controls

Prices for the sale of electricity and gas by utilities to final consumers are not currently controlled in the United Kingdom but as a result of a remedy imposed by the CMA, prices for supply to customers with prepayment meters will be subject to a transitional safeguard cap between 1 April 2017 and 31 December 2020. Although there is no controlled tariff for consumers with specific characteristics, all the major suppliers must offer special discounts for certain disadvantaged customers under the Warm Homes Discount programme. The total cost of discounts of the Warm Home Discount programme for SCOTTISH POWER in 2015-2016 was about GBP 6.40 per customer (counting gas and electricity separately) and, like any other costs, suppliers are free to pass on the cost to their tariffs. OFGEM has implemented licence modifications requiring any price variation by payment method to be cost reflective.

Similarly, there are currently no controls other than those established in the Competition Act 1998 and the Transmission Constraint Licence Condition (TCLC), on prices charged to commercial customers or on other prices in the wholesale electricity and gas markets.

TCLC prohibits electricity generators from making excessive profits resulting from actions in balance markets. OFGEM has published guidelines on the interpretation and application of the TCLC. Enforcement decisions under the framework of the TCLC are subject to review by the Competition Appeal Tribunal, rather than the review by the courts applicable to other GEMA enforcement decisions. The condition expires five years after its enactment, having been implemented on 29 October 2012, and is renewable for another two years. OFGEM consulted in April 2016 on renewing TCLC, but no decision has been announced at this stage.

OFGEM has implemented electricity market liquidity obligations for large integrated retail and generation businesses, including SCOTTISH POWER. These include obligations to facilitate trading with smaller companies and also an obligation to create market in a number of wholesale products during two specified “windows” in each business day. Although the prices of bids and offers are not regulated, the licence condition limits the spread between them. There are rules designed to give some protection to obligated licensees in fast or volatile markets. To date, we have incurred some limited costs in complying with this obligation.

Following its Retail Market Review (RMR), OFGEM has imposed in 2013 a number of rules restricting the products that could be sold in the domestic energy market including restrictions on the number and composition of tariffs. Following a recommendation from CMA these restrictions were removed in 2016. Other RMR remedies including information requirements, requirements for notifying customers of lower tariffs and standards of conduct for customer treatment remain in place.

The networks are considered to be a natural monopoly. Therefore, their revenues have been controlled and this is now achieved through the new RIIO framework (Revenues = Incentives + Innovation + Outputs). This involves setting a revenue profile for an eight year period (with a limited revision every four years) based on the regulator's assessment of the costs of an efficient network operator and the likely capital programme (based on a business plan submitted by the Company) in order to calculate the revenue needed to meet a target return on investments. The formula uses a Market Indicator for setting the debt cost, and phases in (for electricity) an asset depreciation period of 45 years, replacing the 20 year period used previously. Various incentives have been added to the formula which also takes account of inflation in order to calculate the permissible revenues for the network.

Under the RIIO framework, there is a greater emphasis on outputs and innovation, as well as on the role that network companies can play in developing a sustainable energy sector.

In the transmission business, SPTL's new RIIO T1 framework became effective in April 2013. In distribution, the new RIIO-ED1 for the Scottish Power network in the South of Scotland and in the Manweb area came into force on 1 April 2015. Following an appeal made to the CMA by British Gas Trading Ltd, a small adjustment was made, which affected the prices set for 2016/17 and later years. The net effect on Scottish Power's distribution licenses is a revenue reduction of GBP 19 million over the 8 years RIIO ED1 period.

OFGEM has brought forward proposals for competitively tendering the construction of large, new and separable transmission projects. This may lead to a few transmission developments being taken forward by others.

5. Other issues

Other key elements of the regulatory regime in the United Kingdom include:

The Renewables Obligation (RO)

For some time, the United Kingdom Government has intended to source at least 30% of electricity from renewable sources by 2020 as part of its commitment to meeting its obligations under the EU Renewables Directive. To this end, the RO Orders (which apply separately to different parts of the United Kingdom within a unified scheme) place obligations on suppliers of electricity to source an increasing proportion of their electricity from renewable sources (based on the expected level of renewable energy production in each year plus a 10 percent spread in order to prevent certificate prices from falling sharply). Suppliers meet their obligations by presenting sufficient Renewables Obligation Certificates (ROCs) or by paying an equivalent amount into a fund.

The proceeds of the fund are paid back to those suppliers that have presented ROCs in proportion to the number of ROCs presented. Since April 2009, the RO has been banded so that differing technologies receive different levels of support depending on the expected costs. The revision of this framework concluded in 2012 and, as a result, projects starting after 1 April 2013 (or later for some technologies) received revised levels of support.

The RO will close for new projects no later than 31 March 2017 and Government has implemented the Contract for Difference (CFDs) mechanism that was part of Electricity Market Reform (EMR). For solar photovoltaic generation plants above 5MW, the RO closed in April 2015. The RO closed in March 2016 for solar photovoltaic plants at 5 MW or below and in May 2016 for onshore wind, in both cases subject to grace periods. The wind farms in Scottish Power's onshore renewables pipeline that received planning permission in time to qualify for the relevant grace period, will be eligible to accredit under the RO so long as they commence generation 31 March 2017. The RO remains in place for facilities entering the scheme before the relevant closure date; payments will continue until 31 March 2027 for projects that started generation before 1 April 2009 and for 20 years after entry into the RO for later dated projects. The Energy Act 2013 foresees changing from the RO to a premium payment on substantially similar terms.

Electricity Market Reform (EMR)

The principal elements of the United Kingdom Government's EMR programme are:

- a new incentive scheme, based on CFDs to support low carbon generation; and
- a Capacity Market to support security of supply (market-wide auction mechanism).

The CFD allocations to date have taken place within the constraints of a budget for low carbon support measures known as the Levy Control Framework (LCF). An initial tranche of contracts were approved during 2014 by the United Kingdom Government as part of a transitional "Final Investment Decision Enabling Process". The first Allocation Round took place on 4 February 2015 in two "pots"; one for established technologies (mainly onshore wind and solar) and a second one for less established technologies (mainly offshore wind). Scottish Power's 714 MW East Anglia ONE offshore Wind Farm achieved a contract in the auction at a price of GBP 119 per MWh. The Government has now announced another CFD Allocation Round for less established technologies which is due to commence in April 2017. A budget allocation of GBP 290 million (2011/12 prices) has been made for this competitive auction within an overall budget of GBP 730 million for up to three Allocation Rounds before May 2020 subject to satisfactory evidence of cost reductions over time. The Government is also currently considering the nature of any future cost control mechanism such as the LCF after the current LCF end date of 2020/21. A further announcement may take place on 8 March 2017 at the time of the Spring Budget.

Annual Capacity Market auctions took place in December 2014, 2015 and 2016, for capacity delivery in winter 2018, 2019 and 2020, respectively. The most recent of these auctions cleared at a price of GBP 22.50 per kW/year. A new Capacity Market Early Auction was held in early 2017 for delivery in Winter 2017/18; this cleared at a lower price of GBP 6.95 per kW/year.

EU-ETS and United Kingdom Carbon Price Support

As in all EU Member States, generators in the United Kingdom participate in the EU-ETS. Since 2013, the Government is required to auction all allocations to the power sector. The Climate Change Act 2008 sets out a trajectory towards reducing CO₂ emissions from 1990 levels by at least 80% by 2050, with interim reduction targets. The Carbon Price Support mechanism is a United Kingdom tax imposed on fossil fuels used for electricity generation at differential rates which simulate a charge on the CO₂ emissions. It was intended to smooth the path of carbon prices in the United Kingdom power sector in the event of instability in the EU-ETS, by topping up the EU-ETS price to a pre-set trajectory. In practice, the EU-ETS price is much lower than expected and in order to mitigate the impact on electricity prices, the United Kingdom Government has capped the Carbon Price Support tax at GBP 18 per tonne CO₂ until at least 2020. At Budget 2016 it was decided to roll forward this tax rate (uprated for inflation) to 2020/21 and this decision was confirmed at the Autumn Statement.

Climate Change Levy (CCL) exemption

As announced in summer budget 2015 the exemption for renewable electricity from the Climate Change Levy (a tax on non-domestic electricity users) ended on 1 August 2015. This has removed a small additional revenue stream for renewable generators though its value was expected to decline in any event around 2020.

Energy Companies Obligation (ECO)

Energy suppliers who supply over 250,000 domestic customers are required to achieve energy efficiency improvements among their customers. As with any other cost, the costs of making those improvements can be incorporated by suppliers into tariffs, subject to the need to remain competitive in the market. ECO ran from 1 January 2013 to 31 March 2015. A separate phase runs from 1 April 2015 to 31 March 2017. The Government has said that from April 2017, ECO will be replaced by a cheaper scheme costing GBP 640 million a year (based initially on a transition scheme). Details were confirmed on 30 January 2017.

Coal closure

In November 2015, the former Secretary of State Amber Rudd announced plans to consult on requirements for all coal power stations without CCS to close by 2025 (subject to any security of supply issues). In late 2016 the Government published a consultation on possible regulatory options to facilitate this. The impact of any such measures on Scottish Power is limited due to the closure of Longannet.

Pollution Control

The Integrated Pollution Prevention and Control (IPPC), the Large Combustion Plant Directive (LCPD) and the Industrial Emissions Directive (IED) cover the regulatory regime for controlling the pollution from certain industrial activities, including thermal combustion generation, and impose limits on various categories of emissions. In particular, the LCPD limits the emission of sulphur dioxide (SO₂), oxides of nitrogen (NO_x) and particles from power plants, whereby operators of such plants have the option of meeting those requirements or accepting a limited hour derogation prior to their closure by the end of 2015. The IED puts in place a similar regime for 2016 and beyond, with more stringent standards. The IED is transposed into United Kingdom's law through the Pollution Prevention and Control (Scotland) Regulations 2012 and amendments to the Environmental Permitting (England and Wales) Regulations 2010. These controls are enforced by the Environment Agency or, in Scotland, the Scottish Environmental Protection Agency.

Industry regulation in USA

Electricity and natural gas distribution

Some of the most important specific regulatory processes that affect AVANGRID Networks, Inc. (hereinafter, AVANGRID NETWORKS) include the New York rate settlement for NYSEG and RG&E, the Connecticut United Illuminating distribution rate case decision, the Maine and Connecticut transmission Federal Energy Regulatory Commission (FERC) Return on Equity (ROE) case and the Reforming Energy Vision (REV) process of New York.

The revenues of AVANGRID NETWORKS are essentially regulated, being based on tariffs established in accordance with administrative procedures set by the various regulatory bodies. The tariffs applied to regulated activities in the United States are approved by the regulatory commissions of the different States and are based on the cost of providing service. The revenues of each regulated utility are set to be sufficient to cover all its operating costs, including energy costs, finance costs and the costs of equity (the last one reflects the Company's capital ratio and the reasonable return on equity).

Energy costs that are set on the New York and New England wholesale markets are passed on to consumers. The difference between energy costs that are budgeted for and those that are actually incurred by the utilities is offset by applying compensation procedures that result in either immediate or deferred tariff adjustments. These procedures apply to other costs, which are in most cases exceptional (effects of extreme weather conditions, environmental factors, regulatory and accounting changes, treatment of vulnerable customers, etc.) that are offset in the tariff process. Any delivery profit from New York and Connecticut that allows a service company exceeds its profitability objectives (usually due to a better than expected cost efficiency), is shared among the service company and its clients, resulting in a decrease in the future tariff.

Each of the eight supply companies in AVANGRID NETWORKS, must comply with regulatory procedures that differ in form but in all cases conform to the basic framework outlined above. As a general rule, tariff reviews cover various years (three in New York and Connecticut) and provide reasonable returns on equity, protection and automatic adjustments for exceptional costs incurred and efficiency incentives.

1. New York

New York State Electric & Gas Corporation (NYSEG) and Rochester Gas and Electric Corporation (RG&E) Rate Plans:

• 2015 NY Rate Filings

On 20 May 2015, NYSEG and RG&E filed electric and gas rate cases with the NYPSC. The companies are requesting rate increases for NYSEG Electric, NYSEG Gas and RG&E Gas, while for RG&E Electric are requesting rate decreases.

NYSEG Electric requested USD 126 million (7% overall) in additional annual delivery revenue to recover prior storm costs, move to a full cycle vegetation management trim programme in line with best industry practice, and earn an adequate return on its investment. RG&E Electric proposed a USD 10 million rate decrease (1% overall) reflecting the return to customers of funds collected during its 2010 rate plan associated with management efficiencies and costs lower than set levels. NYSEG Gas and RG&E Gas are requesting additional revenues of USD 38 million (8% overall) and USD 20 million (5% overall), respectively.

The companies requested a 10.06% return on equity and a 50% equity ratio. The rate filings are for one year but the companies have indicated their interest in pursuing a multi-year settlement.

The NYPSC staff and other parties filed testimony in September 2015 opposing the rate increase requests. The NYPSC Staff proposed a delivery increase of USD 11.8 million for NYSEG Electric, a delivery rate decrease for RG&E Electric of USD 23.4 million, a delivery decrease of USD 2.8 million for NYSEG Gas and a delivery decrease of USD 2.9 million for RG&E Gas. The NYPSC proposed an 8.7% ROE and a 48% equity ratio. NYPSC also proposed to offset the NYSEG Electric storm deferral balance of USD 262 million with excess depreciation reserve amounts which NYPSC staff claims is USD 665 million at NYSEG Electric and USD 129 million at RG&E Electric. The NYPSC stated it was open to discussing a multi-year rate plan for the companies.

On 19 February 2016, the NYSEG, RG&E and other signatory parties filed a Joint Proposal, or the Proposal, with the NYPSC for a three-year rate plan commencing on 1 May 2016. The Proposal balances the varied interests of the signatory parties including but not limited to maintaining the companies' credit quality and mitigating the rate impacts to customers. The Proposal reflects many customer attributes including: acceleration of the companies' natural gas leak prone main replacement programs and enhanced electric vegetation management to provide continued safe and reliable service. The delivery rate increase can be summarized as follows:

Utility	1 May 2016		1 May 2017		1 May 2018	
	Rate Increase Millions USD	Delivery Rate Increase %	Rate Increase Millions USD	Delivery Rate Increase %	Rate Increase Millions USD	Delivery Rate Increase %
NYSEG Electric	29.6	4.10	29.9	4.10	30.3	4.10
NYSEG Gas	13.1	7.30	13.9	7.30	14.8	7.30
RG&E Electric	3.0	0.70	21.6	5.00	25.9	5.70
RG&E Gas	8.8	5.20	7.7	4.40	9.5	5.20

The allowed rate of return on common equity for NYSEG Electric and NYSEG Gas is 9.00%. The equity ratio for both Electric and Gas is 48%. The Proposal includes an Earnings Sharing Mechanism (ESM) applicable. The customer share of earnings would increase at higher earnings levels, with customers receiving 50%, 75% and 90% of earnings over 9.5%, 10% and 10.5% of ROE, respectively, in the first year. Earnings thresholds would increase in subsequent years.

The Proposal reflects the recovery of deferred NYSEG Electric storm costs of approximately USD 262 million, of which USD 123 million will be amortized over 10 years and the remaining USD 139 million will be amortized over five years. The Proposal also continues reserve accounting for qualifying Major Storms (USD 21.4 million annually). Incremental maintenance costs incurred to restore service in qualifying divisions will be chargeable to the Major Storm Reserve provided that they meet certain thresholds.

The Proposal maintains current electric reliability performance measures (and associated potential negative revenue adjustments for failing to meet established performance levels) which include the system average interruption frequency index and the customer average interruption duration index. The Proposal also modifies certain gas safety performance measures at the company, including those relating to the replacement of main leak prone, leak backlog management, emergency response, and damage prevention. The Proposal establishes threshold performance levels for designated aspects of customer service quality and continues and expands bill reduction and arrears forgiveness Low Income Programs at increased funding levels. The Proposal provides for the implementation of NYSEG's Energy Smart Community ("ESC") Project in the Ithaca region which will serve as a test-bed for implementation and deployment of Reforming the Energy Vision (REV) initiatives. The ESC Project will be supported by NYSEG's planned rollout of Distribution Automation and Advanced Metering Infrastructure (AMI) to customers on circuits in the Ithaca region. REV-related incremental costs and fees will be included in the Rate Adjustment Mechanism (RAM) to the extent cost recovery is not provided for elsewhere. Under the Proposal, we will implement a RAM, which will be applicable to all customers, to return or collect RAM eligible deferrals and costs, including: (1) property taxes; (2) Major Storm deferral balances; (3) gas leak prone pipe replacement; (4) REV costs and fees which are not covered by other recovery mechanisms; and (5) Electric Pole Attachment revenues.

The Proposal provides for partial or full reconciliation of certain expenses including, but not limited to: pensions, other postretirement benefits; property taxes; variable rate debt and new fixed rate debt; gas research and development; environmental remediation costs; Major Storms; nuclear electric insurance limited credits; economic development; and Low Income Programs. The Proposal also includes a downward-only Net Plant reconciliation. In addition, the Proposal includes downward-only reconciliations for the costs of: electric distribution and gas vegetation management; pipeline integrity; and incremental maintenance. The Proposal provides that we continue the electric RDMs on a total revenue per class basis and the gas RDMs on a revenue per customer basis.

A hearing on the Proposal was held on 7 April 2016 and a NYPSC order adopting the Proposal was issued on 15 June 2016, with retroactive application beginning on 1 May 2016. The Commission also provided for additional modifications including a timeline for developing the Earnings Adjustment Mechanism described in the Commission's REV Track 2 Order.

· **Reforming the Energy Vision:**

In April 2014, the NYPSC commenced a proceeding titled Reforming the Energy Vision (REV), which is an initiative to reform New York State's energy industry and regulatory practices. REV has followed several simultaneous paths: Track 1 deals with market design and platform technology and Track 2 deals with the regulatory reform. REV's objectives include the promotion of more efficient use of energy, increasing the utilization of renewable energy resources such as wind and solar power (in support of New York State's renewable energy goals) and a wider deployment of "distributed" energy resources, such as micro-grids, in-situ power supplies, and storage.

REV is also intended to promote greater use of advanced energy management products to enhance demand elasticity and efficiencies. Track 1 of this initiative involves a collaborative process to examine the role of distribution utilities in enabling market based deployment of distributed energy resources to promote load management and greater system efficiency, including peak load reductions. We are participating in the initiative with other New York utilities and are providing our unique perspective. The NYPSC has issued a Track 1 Order in 2015, which acknowledges the utilities' role as a Distribution System Platform (DSP) provider, and requires the utilities to file an initial Distribution System Implementation Plan (DSIP) by 30 June 2016. The DSIP was filed on 30 June 2016 and included information regarding the proposed deployment of Automated Metering Infrastructure (AMI). Various proceedings have also been initiated by the NYPSC which are REV related, and each proceeding has its own schedule. These proceedings include the Clean Energy Fund, Demand Response Tariffs, Net Energy Metering/Value of Distributed Energy Resources and Community Choice Aggregation.

Track 2 of the REV initiative is also underway, and through a NYPSC Staff Whitepaper review process, is examining potential changes in current regulatory, tariff, market design and incentive structures which could better align utility interests with achieving New York state and NYPSC's policy objectives. New York utilities will also be addressing related regulatory issues in their individual rate cases. A Track 2 Order was issued in May 2016. The Track 2 Order includes requirements for all electric utilities to file: a system efficiency proposal, an interconnect survey process and proposed Earnings Adjustment Mechanism (EAM), a progress report on aggregated data reporting, an aggregated data privacy policy statement, revisions to their standby service tariffs, a review of their standby rate allocations and proposed revisions, one or more Smart Home Rate demonstration proposals, and revisions to voluntary time of use rates, as well as to propose EAMs for Energy Efficiency and Customer Engagement. Additionally, the order requires electric utilities to participate in a scorecard metric collaborative and a stakeholder process to develop Clean Energy Standard EAM(s). On 1 December 2016, NYSEG and RG&E filed their proposed EAM. On 20 December 2016, NYSEG and RG&E filed a petition for the full deployment of Automated Metering Infrastructure (AMI) with the Commission. The AMI petition requests authorization to implement full-scale AMI at NYSEG Electric, NYSEG Gas, RG&E Electric and RG&E Gas. Approximately 1.8 million electric AMI meters and gas modules will be deployed. The companies also requested to implement a surcharge to recover the investment until such values can be included in base delivery rates in their next rate cases. The Companies expect the Commission to address their petition in 2017.

Reliability Support Service Agreement in the Ginna Nuclear Power Plant

Ginna Nuclear Power Plant, LLC (GNPP), which is a subsidiary of Constellation Energy Nuclear Group, LLC (CENG), owns and operates the R.E. Ginna Nuclear Power Plant, a 581 MW single-unit pressurized water reactor located in Ontario, New York. In May 2014, the New York Independent System Operator (NYISO) produced a reliability study, confirming that the Ginna Facility needs to remain in operation to avoid bulk transmission and non-bulk local distribution system reliability violations in 2015 to 2018.

On 11 July 2014, GNPP filed a petition requesting that the NYPSC initiates a proceeding to examine a proposal for the continued operation of the Ginna Facility. Ginna asserted that in the two preceding calendar years, 2012 and 2013, it had sustained cumulative losses at the Facility of nearly USD 100 million (including the allocation of CENG corporate overhead) and that CENG had not been compensated for any operational risk or an appropriate return on its investment over this period. Based on the results of the 2014 Reliability Study, GNPP requested that: 1) the NYPSC determines that the continued operation of the Ginna Facility is required to preserve system reliability; and 2) the NYPSC issues an order directing RG&E to negotiate and file a Reliability Support Services Agreement (RSSA) for the continued operation of the Ginna Facility.

In November 2014, the NYPSC ruled that GNPP had demonstrated that the Ginna nuclear plant was necessary to maintain the system's reliability and that its actions regarding the relevant retirement notice requirements were satisfactory. The NYPSC also accepted the findings of the 2014 reliability study and stated that it established "the reliability need for continued operation of the Ginna Facility that is the essential prerequisite to negotiating an RSSA." As such, the NYPSC ordered RG&E and GNPP to negotiate an RSSA.

On 13 February 2015, RG&E submitted to the NYPSC RSSA between RG&E and GNPP. RG&E requested that the NYPSC accepted the RSSA and approve cost recovery by RG&E from its customers of all amounts payable to GNPP under the RSSA utilizing the cost recovery surcharge mechanism.

On 21 October 2015, RG&E, GNPP, New York Public Service Commission, Utility Intervention Unit and Multiple Intervenors filed a Joint Proposal with the NYPSC for approval of the RSSA, as modified. The Joint Proposal provides a term of the RSSA from 1 April 2015 through 31 March 2017. RG&E shall make monthly payments to Ginna in the amount of USD 15.4 million. RG&E will be entitled to 70% of revenues from Ginna's sales into the NYISO energy and capacity markets, while Ginna will be entitled to 30% of such revenues. The signatory parties recommend that the NYPSC authorize RG&E to implement a rate surcharge effective 1 January 2016 to recover amounts paid to Ginna pursuant to the RSSA. RG&E's payment obligation to Ginna shall not begin until the rate surcharge is in effect and FERC has issued an order authorizing the FERC Settlement agreement in the Settlement Docket. RG&E will use deferred rate credit amounts (regulatory liabilities) to offset the full amount of the Deferred Collection Amount (including carrying costs), plus credit amounts to offset all RSSA costs that exceed USD 2.3 million per month, not to exceed a total use of credits in the amount of USD 110 million, applicable through 30 June 2017. To the extent that the available credits are insufficient to satisfy the final payment from RG&E to Ginna then the RSSA surcharge may continue past 31 March 2017 to recover up to USD 2.3 million per month until the final payment has been recovered by RG&E from ratepayers. In the month following the expiration of the term on 31 March 2017, Ginna shall prepare and issue an invoice to RG&E for, and RG&E shall pay to Ginna, a one-time payment in the amount of USD 11.5 million. This amount is being accrued pro-rata over the term of the agreement and will be recovered from ratepayers. On 23 February 2016, the NYPSC unanimously adopted the Joint Proposal in the Ginna RSSA proceeding as in the public interest.

· New York Transco

Networks holds an approximate ownership of 20% in the New York Transco. The New York Transco was established by the New York transmission utilities to develop, own, and operate the electric transmission in New York. In December 2014, New York Transco filed for regulatory approval of its tariffs, terms, and conditions with FERC. The filing requests a base ROE of 10.6%, plus 150 basis points as incentives, recognition of construction work in progress, a tariff formula mechanism, and a proposed cost allocation. Various parties, including the NYPSC, have protested the filing with FERC, including the base ROE, the ROE incentives, and the cost allocation. The New York Transco will not make final decisions on transmission project development until a FERC decision.

On 2 April 2015, the FERC issued an order granting, inter alia, the New York Transco's owners' request for a 50 basis points adder for NY Transco's membership in the NYISO RTO, subject to the adder being capped within the zone of reasonableness after a determination of where within that zone its base level ROE should be set. The FERC also set the formula rate and base ROE issue for hearing and settlement judge procedures. In addition, the FERC rejected the New York Transco's owners' cost allocation method for the Transmission Owner Transmission Solutions, or TOTS, Projects because it would allocate costs to Power Supply Long Island and New York Power Authority that they did not voluntarily agree to pay.

On 5 November 2015, the New York Transco's owners, filed the Settlement with the FERC to resolve all outstanding issues associated with the TOTS Projects, including issues related to the TOTS Projects that were set for hearing and issues pending on rehearing. The issues regarding certain other projects remain pending. The Settlement addressed the financial terms that are components of New York TransCo's revenue requirement for the proposed Transmission Owner Transmission Solution (TOTS) Projects, including the base ROE of 9.50%, and a 50-basis point ROE adder, the capital structure of 53%, and the cost allocation under the New York Independent System Operator, Inc. (NYISO) Open Access Transmission Tariff (OATT) for the TOTS Projects. On 17 March 2016, the FERC approved the Settlement.

· Net Energy Metering

On 16 October 2015, the NY Commission issued an Order Establishment Interim Ceilings on the Interconnection of Net Metered Generation (the Floating Cap Order). There the Commission directed that net metering limitations should "float" until completion of a proceeding to develop an interim method of evaluating the benefits of distributed energy resources. The New York Joint Utilities petitioned for rehearing of the Floating Cap Order, expressing concern that an unlimited number of resources could materialize absent a cap, leading to unanticipated and unbounded bill increases for customers. The Commission has not yet acted upon that rehearing request.

Following the issuance of the Floating Cap Order and the launch of the CDG program, the Joint Utilities experienced a surge in new applications for net metered resources, ultimately leading to more than 4,000 MW of interconnection applications. The Commission instituted the Value of DER proceeding in response to the decision to float the net metering cap and the promise to adopt a "new regulatory approach" for DER valuation,

On 28 October 2016 in Case 15-E-0751, In the Matter of the Value of Distributed Energy Resources ("Value of DER Proceeding"), NYPSC Staff issued its Report and Recommendations. The Staff Report contained a number of recommendations. The Joint Utilities' filed comments on 5 December 2016 along with 32 other parties. The Commission is expected to rule of the proceeding in 1Q2017.

2. Connecticut

UI rate case

On 1 July 2016, UI filed an application with the Connecticut Public Utilities Regulatory Authority, or PURA, requesting approval of a three-year rate plan commencing 1 January 2017, and extending through 31 December 2019. UI's application requests an increase of USD 65.6 million in 2017, an additional USD 21.1 million in 2018, and an additional USD 13.4 million in 2019, totaling USD 100.1 million over the three years. During the litigation of the case, the three-year cumulative request was modified to USD 98.3 million. The original application includes a rate levelization proposal to moderate the customer impact of the necessary revenue increases. The proposal defers a portion of the first and second year increases and spreads recovery of the overall increase by approximately equivalent amounts over the three years of the rate plan with carrying charges included. The proposal results in levelized revenue requirement increases of USD 40.7 million in 2017, USD 47.4 million in 2018 and USD 39.1 million in 2019, followed by an offset of USD 25.6 million at the end of the three year rate plan to equate the levelized recovery to the non-levelized revenue requirement increase.

UI's rate request is attributable primarily to the amount of capital expenditures devoted to its electric distribution system for the purpose of reliability and system resiliency, both in relation to routine operations and during major storm events. UI's application also proposes continuation of its revenue decoupling mechanism and proposes a new Earnings Sharing Mechanism (ESM). Under the proposed ESM, 50% of UI's earnings in excess of the allowed ROE, plus a deadband above the allowed ROE, would be flowed through to the benefit of customers. The proposed ESM includes a 20-basis point deadband in 2017 above the authorized ROE, within which there would be no sharing. This deadband would be 30 basis points in 2018 and 40 basis points in 2019. UI proposes to continue applying any Dollars due to customers to reduce the storm regulatory asset, if one exists. If none exists, then the customer share would be provided through a bill credit.

On 15 December 2016, the PURA issued its Final Decision authorizing a cumulative three year rate of USD 57 million for the years 2017, 2018 and 2019. The 2017 rate increase is USD 43.0 M, an additional USD 11.5 million in 2018, and an additional USD 2.9 million in 2019. The PURA provided a 9.10% return on equity and 50% equity ratio. The three year rate plan retains the existing earnings sharing level whereby earnings above the allowed ROE are shared equally between customers and shareholders. The Company's revenue decoupling mechanism continues. The PURA did reduce the residential basic service charge to USD 9.65 per month.

3. Maine

CMP's and UI's transmission tariffs are determined by a tariff regulated by the FERC and administered by ISO New England (ISO-NE). Transmission rates are set annually pursuant to a FERC authorized formula that allows for recovery of direct and allocated transmission operating and maintenance expenses, as well as the return on assets invested. Prior to 16 October 2014, the FERC provided a base ROE of 11.14% and additional ROE incentives applicable to assets based upon vintage, voltage and other factors.

On 30 September 2011, the Massachusetts General Attorney, Massachusetts Department of Public Utilities, Connecticut Public Utilities Regulatory Authority, New Hampshire Public Utilities Commission, Rhode Island Division of Public Utilities and Carriers, Vermont Department of Public Service, numerous New England consumer advocate agencies and transmission tariff customers collectively filed a complaint (Complaint I) with the FERC pursuant to sections 206 and 306 of the Federal Power Act. The filing parties seek an order from the FERC reducing the 11.14% base return on equity (ROE) used in calculating formula rates for transmission service under the ISO-New England Open Access Transmission Tariff (OATT) to 9.2%. CMP and UI are New England Transmission Owners (NETOs) with assets and service rates that are governed by the OATT and will thereby be affected by any FERC order resulting from the filed complaint.

On 19 June 2014, the FERC issued its decision in Complaint I, establishing a methodology and setting an issue for a paper hearing. On 16 October 2014, FERC issued its final decision in the Complaint I setting the base ROE at 10.57% and a maximum total ROE of 11.74% (base plus incentive ROEs) for the October 2011 – December 2012 period as well as prospectively from 16 October 2014, and ordered the NETOs to file a refund report. On 17 November 2014, the NETOs filed a refund report.

On 3 March 2015, the FERC issued an order on requests for rehearing of its 16 October 2014 decision. The March order upheld the FERC's 19 June 2014 decision and further clarified that the 11.74% ROE cap will be applied on a project specific basis and not on a transmission owner's total average return. In June 2015 the NETOs filed an appeal in the U.S. Court of Appeals for the District of Columbia of the FERC's final order. The appeal is currently pending.

On 26 December 2012, a second, ROE complaint (Complaint II) for a subsequent rate period was filed requesting the ROE be reduced to 8.7%. On 19 June 2014, FERC accepted Complaint II, established a 15-month refund effective date of 27 December 2012, and set the matter for hearing using the methodology established in the Complaint I.

On 31 July 2014, a third ROE complaint (Complaint III) was filed for a subsequent rate period requesting the ROE be reduced to 8.84%. On 24 November 2014, FERC accepted the Complaint III, established a 15-month refund effective date of 31 July 2014, and set this matter, consolidated with Complaint II, for hearing in June 2015. Hearings were held in June 2015 on Complaints II and III before a FERC Administrative Law Judge, relating to the refund periods and going forward period. On 29 July 2015, post-hearing briefs were filed by parties and on 26 August 2015 reply briefs were filed by parties. On 13 July 2015, the NETOs filed a petition for review of FERC's orders establishing hearing and consolidation procedures for Complaints II and III with the U.S. Court of Appeals. The Initial Decision determined that, 1) for the 15-month refund period in Complaint II, the base ROE should be 9.59% and that the ROE Cap (base ROE plus incentive ROEs) should be 10.42% and 2) for the 15-month refund period in Complaint III and prospectively, the base ROE should be 10.90% and that the ROE Cap should be 12.19%. The Initial Decision is the Administrative Law Judge's recommendation to the FERC Commissioners. The FERC is expected to make its final decision in early 2017.

CMP and UI reserved for refunds for Complaints I, II and III consistent with the FERC's 3 March 2015 final decision in Complaint I. The CMP and UI total reserve associated with Complaints I, II and III is USD 21.4 million and USD 4.2 million, respectively, as of 30 September 2016. If adopted as final, the impact of the initial decision would be an additional aggregate reserve for Complaints II and III of USD 17.1 million pretax and USD 10.2 million, net of tax, which is based upon currently available information for these proceedings.

On 29 April 2016, a fourth ROE complaint (Complaint IV) was filed for a rate period subsequent to prior complaints requesting the base ROE be 8.61% and ROE Cap be 11.24%. On 20 June 2016, FERC accepted the Complaint IV, established a 15-month refund effective date of 29 April 2016, and set the matter for hearing and settlement judge procedures.

On 6 December 2016 a three judge panel of the D.C. Circuit Court of Appeals heard oral arguments to FERC's final order in this complaint. A decision is expected by Q2 2017.

Net Energy Metering

On 14 September 2016, the MPUC issued a Notice of Rulemaking regarding Amendments to the Net Energy Metering Rule. The Commission initiated a rulemaking to consider several proposed amendments to its net energy billing rule (Chapter 313). First, the proposed amended rule would increase the maximum size for an eligible generating facility from 660 kilowatts to one megawatt. Second, the proposed amended rule would gradually reduce the T&D portion of a customer's bill which is eligible to be netted against the generating facility's output, while netting of the supply portion of the bill will remain largely unchanged. Third, the proposed amended rule would grandfather existing NEB customers for a fifteen year period. Fourth, the proposed amended rule would add specific provisions that allow and provide consumer protections for community net energy billing and net energy billing leases. As noted by the Commission in its Notice of Rulemaking, these proposed amendments would do little to impact existing NEB customers.

CMP filed initial and reply comments in response to the Commission's Notice of Rulemaking. Other parties, including industry experts also provided comments. The MPUC made a decision on its Notice of Rulemaking on 31 January 2017. The MPUC has not yet issued the final rule but did issue a notice stating that the resulting rule a) grandfathers existing customers for fifteen years, b) for new entrants it locks in the phase down level, at the year in which they enter, for fifteen years, and c) maintains incentive margins consistent with the declining costs of solar technology. Below is additional detail of the ruling.

- Grandfathering of existing NEB Customers. All existing customers and new customer installations that occur prior to 1 January 2018 will be grandfathered for fifteen years. This means those customers will receive the current incentives and terms as they exist today.
- Grandfathering of New Entrants to NEB. As new customers sign up over the next 10 years, netting of the transmission and distribution (T&D) portion of the bill will be gradually decreased to reflect reductions in the costs of small renewable generation technology. For example, in the first year NEB customers will receive the full value of the supply portion, and 90% of the T&D portion for each year of the fifteen years.
- Maintaining Incentive Levels. The incentives to NEB customers under the new Rule should not change the length of time it takes for a customer to recoup their investment. The estimated payback for new installations will be similar to what it has been historically. As noted above, for a customer installation signed in year one, the full incentive for supply and 90% of the incentive for T&D is received for fifteen years. As the cost of technology declines, the incentive for T&D also declines for new entrants. For a new customer installation in year two, for example, the cost of the solar panels will have declined but the incentive will also decline to 80% for T&D and the full incentive for supply.
- The rule only applies to residential solar installation on roofs. Many projects are being built across the state today based on existing market mechanisms. The Commission decided not to address larger scaled projects and community projects as part of the NEB rules to ensure we stayed within our regulatory function, and in light of legislative initiatives in these areas.
- Includes Renewable Energy Credit (REC) Based Revenue Stream. The new Rule allows to a NEB customer to choose to monetize the value of their solar generation and receive a credit for that value. NEB installations will be automatically classified as a Maine Class I Renewable Resource.

MNG Rate Case

On 5 March 2015, MNG filed a rate case in order to further recover future investments and provide safe and adequate service. MNG requested a 10.0% ROE and 50.0% equity ratio. The MPUC Staff recommended a separate revenue requirement for MNG's Augusta customers and MNG's non-Augusta customers. The MPUC also recommended a USD 19.95 million disallowance of the Augusta Expansion investment based upon the Staff's conclusion that MNG's management of the Augusta Expansion Project was imprudent.

On 6 November 2015, a stipulation was filed with the MPUC, which was executed by MNG, the Office of Public Advocate and the city of Augusta. The stipulation contained a combined revenue requirement for Augusta and non-Augusta based on a 9.55% ROE and 50% equity ratio. The stipulation also provided for an initial Augusta investment disallowance of USD 6 million and an investment phase-in of USD 10 million. On 22 December 2015, the MPUC rejected the proposed stipulation as not in the public interest. In January 2016, the Administrative Law Judge established a new litigation schedule. The litigation was suspended at the end of January 2016 for settlement discussions. We reserved USD 6 million for this case at the end of 2015.

On 3 May 2016, all active parties to the case filed a stipulation that settled all matters at issue in the case and reflected a 10-year rate plan through 30 April 2026. The MPUC approved the stipulation on 17 May 2016, for new rates effective 1 June 2016. The settlement structure for non-Augusta customers includes a 34.6% delivery revenue increase over five years with an allowed 9.55% ROE and 50% common equity ratio. The settlement structure for Augusta customers includes a 10-year rate plan with existing Augusta customers being charged rates equal to non-Augusta customers plus a surcharge that increases annually for five years. New Augusta customers will have rates set based on an alternate fuel market model. In year seven of the rate plan MNG will submit a cost of service filing for the Augusta area to determine if the rate plan should continue. This cost of service filing will exclude USD 15 million of initial 2012/2013 gross plant investment, however the stipulation allows for accelerated depreciation of these assets. If the Augusta area's cost of service filing illustrates results above a 14.55% ROE then the rate plan may cease, otherwise the rate plan would continue. A disallowance for the initial 2012/2013 gross plant investment is not part of the approved stipulation. The reserve of USD 6 million for this case was reversed in May 2016.

Electricity generation from renewable energy resources

Numerous State Governments and the Federal Government have adopted measures and implemented numerous regulations designed to foster the development of electricity production from renewable resources. State programmes have generally come in the form of: 1) Renewable Portfolio Standards (RPS's) that usually require utilities to generate or purchase a minimum amount of renewable electricity; and 2) tax incentives. To date, the Federal Government has primarily supported renewable energy development through tax credits for production and investment as well as accelerated tax depreciation.

Twenty-nine states and the District of Columbia have adopted mandatory RPS requirements, which vary across the states but will generally range from 15-33% of the generation by 2025. The requirements are typically implemented through a system of tradable renewable energy certificates that verify that a kWh of electricity has been generated from a renewable resource. Several state legislatures have debated whether to repeal or roll back significantly their RPS requirements. In 2014 Ohio enacted legislation to freeze its RPS programme until 2017; in 2015, Kansas replaced its mandatory RPS with a 20% voluntary standard as part of a compromise that retained existing property tax exemptions. In contrast, California in 2015 and Oregon in 2016 enacted legislation to increase the state RPS to 50%.

Most states also offer a variety of tax incentives to promote investment in renewable energy resources. For instance, Washington and Colorado, among other states, exempt the sale and use of renewable energy equipment from taxation, which reduces development costs substantially. Several states reduce property tax requirements on renewable generation facilities through enterprise zones or similar designations, while Minnesota has substituted a property tax in lieu of fix production tax. Other states, such as Texas, boost the construction of electrical infrastructure (Competitive Renewable Energy Zones) to ease the transportation of renewable electricity towards load points.

In 1992, the US Congress enacted legislation that established a Production Tax Credit (PTC) of USD 15 per MWh (adjusted for inflation) for the production of electricity from wind power facilities for the first ten years of a project's operation. This programme has been renewed on several occasions and has been expanded to include the production of electricity from several other renewable resources, including biomass, geothermal, solid urban wastes and hydroelectric power. In 2005, Congress established a 30% investment tax credit (ITC) for solar power projects. The PTC, which is currently valued at USD 23 per MWh, was extended and phased out by the Congress on 18 December 2015. Developers that start construction on a wind project before 2017 will qualify for the full credit, while those starting construction between 2017 and 2019 will qualify for a reduced-value credit. These qualifying facilities may also elect to take a 30% ITC rather than the PTC. Solar ITC was also extended and phased out by Congress on 18 December 2015. Developers that start construction on a solar project before 2020 will qualify for a 30% investment tax credit (ITC). Projects for which construction begins after 2019 are eligible for a lower ITC. The purposes of the PTC and ITC are to make electricity production from renewable resources more competitive relative to fossil fuel and nuclear power facilities.

In addition to the PTC and ITC, renewable energy facilities are eligible for accelerated five-year tax depreciation on their investments. This programme is known as the Modified Accelerated Cost Recovery System. As a result of legislation enacted in 2008, 2009, 2013 and 2014, many facilities placed in service between 2008 and 2014 qualified for bonus depreciation which allowed 50% depreciation deduction in the year a facility was placed in service. In December 2015, Congress enacted legislation to extend and phase out bonus depreciation. Companies can through 2017 deduct 50% of certain capital investments during the year the investment is made. If the investment occurs in 2018, companies can deduct 40% and if it occurs in 2019 only 30% of deduction is allowed.

With respect to interstate transmission networks, the FERC has adopted a series of requirements on transmission operators to improve access and reduce costs for variable generation like wind and solar power. FERC Order 764 is driving changes in scheduling practices and other activities that will increase forecasting accuracy and reduce needed reserves, resulting in lower technology integration costs.

4.5 Industry regulation in Mexico

The Mexican Energy Reform, which began at the end of 2013 with the amendment of Mexican Constitution, set in motion the deep transformation of the electric sector, through the creation of a completely new regulatory framework. As a consequence of this constitutional reform, nine new laws were enacted during 2014 and 2015 and 25 regulations were either created or reformed.

Although the energy reform is aimed mainly at the hydrocarbons sector, it will also offer new business opportunities in the generation, transmission, distribution and management of electricity infrastructure. This transformation opens the energy sector to private investment in activities that were previously reserved to the Government.

The Hydrocarbons Law (LH) regulates activities like petroleum treatment and refining natural gas processing export and import of hydrocarbons and petroleum products; transportation, storage, distribution, compression, liquefaction, decompression, re-gasification, marketing and sale to the public of natural gas, hydrocarbons, petroleum products and petrochemicals, along with the management of integrated systems. All these activities are now open to private investment and subject to the Hydrocarbons Law.

One of the goals of the industry restructuring is to improve the competitiveness of low-carbon power generation. Concurrently with the COP 21 in Paris, the Mexican Congress and Senate passed the Energy Transition Law (*Ley de Transición Energética* - LTE), which creates binding obligations for clean energy generation and emission reductions targets for the future, bringing a strong legal framework to the development of clean energy projects in Mexico.

The previous regulatory framework will continue being applicable to existing businesses and facilities, before the Energy Reform (among them, Iberdrola's businesses), which provides stability and legal certainty in the Mexican regulatory context.

1. The Electric Reform

The Mexican Constitution, amended in December 2013, states that the planning and control of the National Electrical System (SEN), as well as the energy distribution and transmission public service are competency of the Government of Mexico. Power generation, excluding nuclear, is open to private investment, as well as power sales to the end users.

The transmission and Distribution networks (T&D) will remain under State ownership as regulated activities, but the Mexican Government may grant service contracts to private companies, creating opportunities to participate in the construction, operation and maintenance of T&D infrastructure.

The Electricity Industry Law (*Ley de la Industria Eléctrica* - LIE) regulates activities in the electricity sector in Mexico. According to the LIE, the private companies can now generate and sell electricity under an organised Wholesale Electric Market, and also invest in transmission and distribution infrastructure, under specific Public-Private Associations and other legal structures described therein.

From the regulatory side, three agencies will have primary responsibility for the sector. The Energy Secretariat ("SENER") will have the policy function; the Energy Regulatory Commission ("CRE") will have the regulatory function; and the National Energy Control Center ("CENACE"), a new decentralized agency, will manage the power grid and the wholesale electric market.

2. Energy Secretariat

As part of the Energy Reform, the Energy Secretariat (*Secretaría de Energía* - SENER) has been empowered to coordinate the centralised planning and coordination of the energy policy, both for hydrocarbon and electric subsectors. SENER is also in charge of guaranteeing the implementation of the laws derived from the reform including the LTE issued recently for the transition to clean energy and emission reduction.

During the first half of 2015, SENER issued the mandatory requirement of Clean Energy Certificates (CECs) for year 2018, with a target of 5% of the total consumption. In March 2016, it established a target of 5.8% for 2019. Penalties for non-compliance with the requirements of CECs have been issued.

During the second half of 2015, SENER issued the Wholesale Electric Market guidelines and called for the first long term auction for CECs, capacity and energy; eleven companies awarded contracts to develop more than 1.8 GW of new solar and wind capacity.

Through the first half of 2016 SENER called for the second long term auction, and twenty three companies were awarded contracts to develop 2.8 GW of the renewable capacity; the energy-CECs cost was 30% lower than the first auction.

Regarding the coordination and planning of the National Electric System, SENER has issued, in 2015 and 2016, the yearly versions of the National Electric Grid Development Programme (*Programa de Desarrollo del Sector Eléctrico Nacional* - PRODESEN) including projections of power generation, demand and infrastructure requirements from 2016 to 2029.

3. Regulatory Body

As part of the energy reform in Mexico, the country enacted the Regulatory Body Law in August 2014. The regulatory bodies in charge of coordinating activities in the energy field are the National Hydrocarbons Commission (*Comisión Nacional de Hidrocarburos* - CNH) and the Energy Regulatory Commission (*Comisión Reguladora de Energía* - CRE).

CRE and the CNH are the two most relevant regulatory authorities in the energy sector. They have their own legal status, budget, technical and governance autonomy. Both commissions have a similar governance authority of seven commissioners and an executive secretary.

CRE has existed since 1995 as a public body with power and authority to grant permits and issue administrative provisions in the fields of electricity, gas transport and some regulated tariffs for natural gas and liquefied petroleum gas.

As a result of the Energy Reform, CRE's field of authority was expanded significantly, to transportation and commercialisation of hydrocarbon and derivatives, such as gasoline, petrol, diesel fuel oil, etc.

Regarding the electricity sector, the main faculties of CRE are to define terms and conditions of auctions and bidding processes; to supervise the wholesale market operation; to authorise the contract and auction models; to regulate reliability, capacity requirements and operational costs; to determine the regulated tariffs and contract models for services involving transmission, distribution and basic supply of electricity, to authorise models related to technical specifications for connecting power stations and users, intelligent networks, etc. Other roles of CRE include granting permits to market participants and the CECs registry as well as to resolve controversies and to enforce fines related to non-compliance of market participants.

Regarding the hydrocarbon sector, the CRE regulates and promotes the development of transportation, storage, distribution, compression, liquefaction and regasification activities of all hydrocarbons.

The CNH has the fundamental task of regulating and supervising the exploration and extraction of hydrocarbons. It is responsible for the promotion, tendering and undersigning of contracts for this activity.

4. National Agency for Energy Control

Mexico created the National Agency for Energy Control (*Centro Nacional de Control de Energía* - CENACE) as a decentralised public body with authority to perform the operational control of the National Electricity System and the wholesale electric market. CENACE has full autonomy and acts under the authority of SENER and CRE, in order to control the participation of generators and suppliers in the market; acquire and provide electricity and capacity under competitive basis; and summon and manage the auctions of capacity, energy and CECs.

CENACE guarantees open access to the transmission and distribution facilities to all market participants, public and private.

Additionally, CENACE also operates and oversees the preparation of proposals for planning and expansion of the entire national electricity grid through its development programme (PRODESEN), which is then supervised and issued by SENER and thereafter by CRE.

During the first half of 2015, CENACE received from CFE all the relevant assets related to its roles, issued its internal organisational by-laws, delivered the draft of the PRODESEN to SENER and issued the first version of interconnection criteria.

During 2016, CENACE launched the first phase of the Wholesale Electric Market, conducted the second auction for CECs, Clean Energy and Capacity and issued the first result of the Capacity Balance Market process.

5. CFE's Law

The CFE's Law, issued in August 2014, states that CFE becomes a productive state-owned production company wholly owned by the Federal Government. The new CFE has budgetary and governance autonomy, with Board of Directors formed by members of the incumbent secretariats (SENER, Treasury, etc.) and independent board members. This law aims to regulate the organisation, administration, operation, control, evaluation and accountability of CFE and to establish the special regime for productive enterprises subsidiaries and subsidiaries, compensations, acquisitions, leases, services and works, assets, liabilities, state dividend, budget and debt.

The new CFE will operate through separate affiliated companies that will participate in generation, transmission, distribution and supply, so that other parties will have open access to the grid and levelled play roles for the wholesale electricity market. In the second half of 2016 CFE assigned CFE's electric power plants through its six different generation companies. Also, CFE informed that its transmission, distribution and domestic supply affiliated companies are already working independently.

During 2016, CFE performed the legal separation and asset restructuring, and cautiously commenced the operation of the newly created subsidiaries as separated entities in the wholesale electric market. The process was significantly delayed, especially due to the complexity of the asset, labour and management separation.

A very significant success of CFE during 2016 was the renegotiation of the Labour Union Contract, which significantly reduced the burden of the pension liability in CFE's Balance Sheet.

6. Transmission and Distribution

As ruled by the LIE, the Mexican Government will continue performing electric transmission and distribution (T&D) as a strategic regulated public service through state-owned production company CFE, or its subsidiaries. CFE's legal separation allows to create these entities as regulated open access companies. The LIE provides opportunity for T&D activities and related services to be subcontracted with private companies through public-private agreements, so that financing, installation, maintenance, management, operation, expansion, rehabilitation, surveillance and preservation of the required infrastructure can be performed as services provided to the T&D regulated companies.

One of the key elements in this matter is the implementation of a high voltage direct current transmission line that will connect Ixtepec (one of the most important renewable energy generation zone in Mexico) with the central area of the country; the bidding request and the preliminary bidding package was issued in the last quarter of 2016.

7. Generation and Retail

The LIE provides that generation and retail can be performed by any private or public entities subject to the compliance of permitting and market rules. Generation plants 0.5 MW or larger require a permit from the CRE.

These are two types of permits required for electric retail: 1- basic supply with regulated tariff (for those consumers with a lower demand of 1 MW from August 2016) or 2- qualified supply through the wholesale electricity market at liberalized conditions for consumers with a demand of 1 MW or upper.

SENER may revise and reduce the threshold of 1 MW for the possibility of qualifying consumers for the liberalised conditions. However, becoming a qualified consumer is optional, only mandatory for new costumers.

8. Geothermal energy

The Geothermal Energy Law regulates the exploration and use of underground geothermal resources to generate electricity. The private sector can participate through auctions to obtain exploitation rights of geothermal resources. Additionally, the National Water Law was also amended in order to provide special status to the "geothermal water" compatibly with the exploitation of your thermal resources under the Geothermal Energy Law.

9. Wholesale electricity market

The wholesale electric market commenced operation during January 2016 as provided under LIE. It is a nodal marginal price market operated by CENACE, where generators, suppliers and qualified costumers of the electric energy can interact to buy and sale the energy, capacity, ancillary services, CECs and financial transmission rights in Day Ahead, Hour Ahead and Real Time.

The Market Rules are still being developed and issued. The Market Basis were issued during 2015, and based on them, several Manuals have been issued, such as: the Manual for Long Term Auctions, the Manual for Short Term Energy Market, the Manual for Registration of Market Participants, the Manual for Financial Transmission Rights, the Manual for the Market Information System, the Manual for the Capacity Balance Market and the Manual for Distributed Generation.

10. National content

The LIE does not demand a minimum percentage of national content in the infrastructure of the Electric Industry. However, it points out that SENER will establish the minimum percentages and other conditions for national content in terms of the contracts it generates. The Secretary of Treasury will establish the criteria to measure and the targets of domestic content levels for the electricity sector.

11. Surface use and occupancy

The LIE provides that transmission and distribution, being for public service, must be treated as strategic activities in terms of rights of way. This allows greater access to the facilities and rights of way to the national electricity grid. The CRE will issue provisions that will secure access to the power lines and fair compensation to the land owners.

12. Previous regime for permits, plants and electric industry contracts

All the permits and contracts granted and executed under the previous Public Power Service Law (*Ley del Servicio Público de Energía Eléctrica* - LSPEE) will remain under the same terms and conditions, and can be amended as provided there. Once the market starts operating, the holders of these legacy contracts - self supply and Independent Power Producers ("IPP") have the alternative to migrate partially or completely to the new LIE. Existing IPP will remain in effect to the end of their contractual term prior to the migration and Legacy Connection Contracts (*Contratos de Interconexión Legados* - CIL) of the self-supply projects will not be renewed upon their termination.

Permit requests for self-supply, co-generation, small-scale production, imports or exports made before August 2014 were resolved under the LSPEE terms and conditions, provided that the facilities under such permits must start operation before 31 December 2019.

13. Electricity tariffs

The transition of CRE as the new entity responsible of issuing the regulated electricity tariffs (transport, distribution, basic supply and last reserve supply) is still in progress, mainly delayed by the legal separation of CFE and the complexities of the cost allocation associated with it. All the Regulated Tariffs issued during 2015 and 2016 are portions of the additive regulated tariff yet to be totalized. The principle of the new tariffs is to be based on the recovery of all generation costs, connection services, transport and distribution costs, clean energy certificates and other recoverable costs and collection targets.

It is expected that these tariffs will use similar formulas related to the previous regime during a transitory period from 2016 to 2018.

As the main mechanism to promote the reduction of non-technical losses arising from customer's fraud, CRE has imposed collection targets on the T&D companies.

14. Natural Gas Transportation System

As part of the Energy Reform, the former owner of the Natural Gas Transportation System, PEMEX, has been split in the following subsidiaries: Pemex exploration and production, Pemex industrial transformation, Pemex perforation, Pemex logistics, Pemex co-generation and services, Pemex fertilisers and Pemex ethylene, as provided under the PEMEX Law enacted in August 2014.

This law transformed PEMEX into a state-owned production company which performs business activities and aims to profitability goals. Concurrently with this transformation, the natural gas transportation system was transferred from PEMEX to CENAGAS, the National Operator of the Natural Gas Pipeline Grid in order to promote an open market for its transportation, distribution and commercialisation. According to the principle of asymmetrical regulation, PEMEX cannot integrate transportation and commercialisation of gas under the same company anymore.

CENAGAS has issued the 5 year strategic natural gas development programme. CENAGAS formally started to operate during 2016.

As part of the programme to reduce fuel oil consumption, CFE called for several bidding processes to contract natural gas transportation services from pipelines to be owned by private companies. The majority of these pipelines will be operational by 2018, thus increasing the natural gas fired power generation, and reducing CO₂ emissions from the fuel oil based generation. Simultaneously, the Government is promoting multiple gas pipelines intended to expand the existing gas transportation system through CENAGAS.

The natural gas transport and storage systems incorporated into the new integrated tariff scheme must meet the criteria of forming part of an interconnected system, thus providing benefits, improving the safety, continuity, redundancy levels and efficiency of integrated systems.

The Legacy Transportation Permits (permits given before the electric reform) for self-supply and the long term natural gas supply contracts with Pemex required by the electric plants will remain in effect and will not be adversely affected by these changes in the regulatory framework.

During the second half of 2016 CENAGAS was empowered to conduct the future bidding processes for natural gas transportation auctions, (no longer CFE or Pemex). Additionally, all capacity rights of the SISTRANGAS were transferred to CENAGAS to control manage.

SENER issued a Public Policy to create a Natural Gas Open Market by 2018, in order to promote new players and to reduce the role of Pemex in the commercialization.

As part of this public policy, CENAGAS issued an Open Season for Transportation Capacity in the SISTRANGAS, which will grant firm capacity rights to the winning bidders for year 2017 and will help to identify the sections that need to be expanded in the future. The Open Season is for all the capacity available that has not been reserved or contracted under pre-existing long term supply agreements.

4.6 Industry regulation in Brazil

1. Tariffs

Electricity distribution activity carried out by joint ventures, such as Companhia de Eletricidade do Estado da Bahia, S.A. (COELBA), Companhia Eletricidade do Rio Grande do Norte, S.A. (COSERN), Companhia Energética de Pernambuco, S.A (CELPE) and Elektro Eletricidade e Serviços, S.A. (ELEKTRO), which operate in Sao Paulo and Mato Grosso do Sul, is subjected to federal regulation in Brazil.

The Brazilian regulatory framework is based on a system of price cap that is revised every four or five years, depending on each company's concession contract and is updated annually by the regulator. COELBA and COSERN have a five-year term and CELPE and ELEKTRO have a four-year term.

Tariffs are updated annually by the Electric National Energy Agency (*Agência Nacional de Energia Elétrica* - ANEEL), through the annual adjustment process that considers inflation, an ex-ante efficiency factor and variations on non-manageable costs components, such as energy purchase costs and transmission tolls.

Tariffs have two components:

- **Plot A:** corresponding to energy purchases, power transmission services contracts and to other costs that are out of a distributor company administration and passed through to the end tariff.
- **Plot B:** determined as the sum of (i) the return on the non-depreciated regulatory remuneration base (regulatory WACC applied to the replacement cost of non-depreciated distribution installations and other assets), (ii) the return on capital (a depreciation index applied to the gross asset base) and (iii) the operation and maintenance expenses, and the expense for the uncollectible turnover (the regulator defines late payment rates depending on the kind of grant). This last subcomponent is calculated through a benchmarking model which compares all power distributors in the country and determinates efficient cost levels.

In June 2014, ANEEL opened the first debate on the Fourth cycle of tariff review in a public hearing, discussing proposals to change the methodology used to calculate operating costs, cost of capital (WACC), regulatory asset base (RAB), along with uncollectable revenues and distribution losses.

In May 2015, methodologies dealing with Fourth tariff review cycle were approved and applied to ELEKTRO in its tariff review in August 2015. The main points, in summary, are:

- **WACC:** approved regulatory WACC for Fourth cycle is 8.09% real after taxes. This is higher than Third cycle's 7.5%.
- **OPEX:** The OPEX to be used in the first year of the cycle was confirmed and represents a positive margin to efficient companies.
- **Non-technical losses:** In the case of efficient companies, the target will be defined by the historical average instead of the historical minimum.
- **Uncollectable revenues:** benchmarking approach defines the uncollectable, wherein it is used the bad debt database of 49-60 months. Pass through of uncollectable revenues related to sector fees and tariff flags revenues. The result represented an improvement from what was proposed.
- **Third-party assets (special obligations):** inclusion of a fee to operate third-party assets. This is an important improvement compared with previous cycles.
- **X Factor:** The approved X factor for the sector is 1.53% (versus 1.91% from ANEEL's first proposal).
- **Regulatory Asset Base (RAB) and Non-Electrical Assets:** The new methodology for RAB was not applied in ELEKTRO's review but will be applied to NEOENERGIA's distribution companies. According to the new methodology, the values of assets' additional costs and minor components are now given by a reference price database. Also, non-electrical assets' methodology had a data update and it is expected to better reflect companies' costs.

On 25 August, ANEEL approved ELEKTRO's Fourth tariff review, which raised its tariffs in 4.2% on average (0.68% for residential clients and 9.32% for industrial clients). Some highlights of Fourth cycle are: all investments made were recognized in the RAB, higher remuneration rate (from 7.5% to 8.09%, after taxes), positive OPEX margins, third party asset's remuneration and smaller X factor.

The aim of the annual review is to ensure that component A's costs are passed on to consumers and that component B's costs perform in line with inflation and with the pre-determined efficiency factor. An annual tracking account mechanism is used to register component A's unbalances, which should be passed through to tariffs in the following tariff process.

Also regarding distributors' financial exposure due to a rise in costs in early 2015, an extraordinary tariff review occurred in order to preserve financial and economical balance.

On 23 August 2016, ANEEL approved ELEKTRO's annual review, which decreased its tariffs in -13.40% on average (-12.28% for residential clients and -15.02% for industrial clients). The main highlights concerned the reduction of component A's in -4.53%, due to CDE charge decreasing, once the hydrological situation got better in comparison to 2015, and Itaipu power purchase tariff reductions. However, component B had an increase of 9.11%, adjusted by IGP-M inflation index minus X factor.

2. Energy Purchase

For the business of power generation, the review of the sector model introduced in 2004 brought new guidelines for planning responsibilities and expansion generation fleet, significantly reducing risk of further rationing. This expansion is being pursued via public tendering of generation projects in which the successful bidder is the supplier that offers the lowest price in Brazilian Reals per MWh generated, in exchange the successful bidder is awarded a concession or permit of 20 to 35 years (depending on the technology) to operate a power station under a Power Purchase Agreement (PPA) at a price that is an outcome of the tender.

Since 2013, Brazil has undergone some important structural changes in electricity regulation.

In Law 12.783 (the former Provisional Act 579) of 11 January 2013, the Federal Government made official a decrease in electricity tariffs (which led to an extraordinary tariff revision applied on 24 January 2013) and established standards for the renewal of concessions for generation, transmission and distribution expiring between 2015 and 2017. This law allowed power companies to extend their concessions by early renewal of their contracts under specific conditions. As a result of these new rules some generators decided not to renew their concessions. The energy from generators that decided to renew concessions was allocated to Distribution System Operators (DSOs) through quotas, which, however, were not sufficient to meet market needs. Additionally, some PPAs from new energy auctions were suspended or postponed due to delay of construction schedules or revocation by ANEEL.

Thus, mismatches between energy requirements (load) and resources (PPAs) led DSOs to purchase energy in the spot market, raising their costs and significantly affecting their cash flow. In addition, hydrologic conditions have been unfavourable since the final quarter of 2012, with low reservoir levels together with poor performance of rainfalls and inflows, which increased substantially the spot price and thermoelectric generation. The corollary was a significant increase in energy costs, which temporarily impacted earnings of distributors.

Part of this rise in costs was compensated for using funds managed by Government through energy development account and by means of loans underwritten by various financial institutions, centralised in ACR (Account for Regulated Environment) Accounts. These resources were approximately BRL 10,000 million to cover non-recurring expenses incurred in 2013 and BRL 18,800 million to cover those during 2014. The remaining part of non-recurring costs, which wasn't covered by these funds, was passed through to consumers in the annual adjustment of the tariffs.

These financial resources helped to minimise distributors' liquidity problems in 2013 and 2014, but according to International Financial Reporting Standards (IFRS), DSOs were not allowed to recognise regulatory assets and liabilities on their balance sheets. ANEEL therefore opened Public Hearing 61/2014 to discuss whether distributors' concession agreements should be amended allowing the compensation of regulatory assets and liabilities at the end of the concession period, in order to allow its recognition in the distributors' financial statements. This amendment was signed by distributors in November 2014, and these assets and liabilities are presently recognised according to IFRS.

During Public Hearing 64/2014, ANEEL discussed quotas allocation criterion, regarding the energy from generators whose concessions had expired. Federal Decree 7805/2012 established the allocation of new energy quotas in conformity with the size of the market (except the allocation that happened in 2013, which didn't follow this guideline in order to achieve equal tariff reductions between DSOs). As a result, ANEEL approved an allocation criterion that favours exposure to the spot market in 2015 but that follows the proportion of market size in the following years.

In 2015, minimum and maximum limits for spot prices were changed, after discussion within the Public Hearing, these values went from BRL 15.62 and BRL 822.83 per MWh in 2014 to BRL 30.26 and BRL 388.48 per MWh in 2015. This change allowed a significant reduction in the exposure of DSOs' cash flows.

After great tensions related to the lack of rainfall in 2014 and early 2015 (which raised the imminent possibility of rationing), storage reservoirs, especially in Southeast and Midwest, were able to recover and close the month of November at 27.55% of capacity, well above the recorded for the same period of 2014. The year's closing forecast is 33.8% of its capacity.

Despite improved hydrological conditions, economic slowdown observed for three consecutive quarters had significant negative effects on the distribution market. Given that prospects for 2016 are a negative growth of Brazilian GDP, it is expected that the decline in the energy sector's market continues, especially affected by the drop in industrial demand. Thus, the distributors are facing a plausible scenario of overcontracting (above 105%) for the next year. By December 2013, all energy contracts for the year 2016 had already been carried out with completely different projections of the ones checked today, and therefore variations on events outside the managerial scope of distribution combined with unfavourable market conditions have resulted in overcontracting (despite the Company's efforts to mitigate them). The main factors responsible for this scenario are the quotas, migration of potentially free and special customers to free market and other variations resulting from higher market fall than frustration of the energy auctions. Once DSOs have identified difficulties, negotiations have started with MME and ANEEL to counteract the unmanageable effects and neutralize the risks.

In 2016, with political crises and the Impeachment process occurred against former President Dilma Rousseff, the economic situation deteriorated, and the country faced a drop on GDP of -4.0% in the third quarter and an increasing on inflation indexes, such as IPCA and IGP-M. However, by the end of the year, after Michel Temer became president, IGP-M and IPCA had a recover, but GDP is still expected to decrease considering the whole year. These conditions contributed to a drop on energy consumption, worsening distributors overcontracting situation. Elektro surplus position was above 105% that are covered by tariffs. Many actions were taken to mitigate this position in 2016 together with ABRADDE and ANEEL that are listed as following:

- As a result of a Public Hearing 04/2016 that discussed energy surplus due to quotas' contracts, any quota's volume above reposicion volume should be considered as involuntary contracting, which mitigated the over-contracting regarding this issue, reducing Elektro exposure in 6.9%.
- ANEEL announced the result of the Public Hearing 085/2013 that dealt with the reduction of distributors (Power Purchase Agreements – PPAs) due to the migration of special customers to Free Energy Market, and approved the reduction of future PPAs due to the migration of special customers.
- Possibility to sign Bilateral agreements between distributors and generators, with temporary suspension of PPAs.
- Minister of Mines and Energy published the Decree nº 8.828, which suspends the requirement to replace the minimum contracted amount for overcontracted distributors. The measure provides more flexibility to them, since now overcontracted distributors will not be penalized if they do not purchase energy to replace contracts about to expire. For Elektro, there will be direct impacts from 2020 onwards (once we have quotes already allocated in this replacement).
- Elektro and ABRADDE are discussing with ANEEL, as an extension and consequence of Decree 8.828, an adjustment in calculation of "quotas step", considering that overcontracted distributors are no longer penalized for not purchasing the replacement amount.

- In August, the Chamber of Electricity Trading (CCEE) started the execution of New Energy Relocation Mechanism (MCSD Energia Nova) that enables the overcontracted distributors to negotiate contractual reductions with generators. There were already processed three mechanisms for 2016, with supply period of July to December, August to December, and October to December. The results of these three processing allowed Elektro to reduce 2.3% of its energy surplus.
- Retroactive reprocessing of MCSD Energia Nova for the months of July and August 2016, allowing the participation of generators that could not participate previously. The result is expected to be release in February 2017.

In addition, there are other actions that still depend on publication of resolution by ANEEL and MME, and the expectation is that it would be published by the beginning of 2017:

- Consider overcontracting related with the migration of special clients to free market in 2016 as involuntary.
- Adequate the tariff calculation of overcontracting not to consider the amounts of energy contracted by distributors with Belo Monte power plant, once they have delayed the delivery of energy due to problems during the power plant construction.

Beyond the actions mentioned for 2016, there is an action plan to mitigate overcontracting expected to 2017: (1) conversion of capacity contracts into reserve energy contracts; (2) physical guarantee revision of power plants that sell their energy in quota's; (3) possibility to sell interruptible energy with discount; (4) New MCSDs Energia Nova and bilateral agreements; (5) energy trade between distributors and free consumers (allowed by Law 13.360/2016).

After Michel Temer took place as President, many reforms were proposed in order to recover the economy and investor confidence, such as the approbation of public expenses reduction plan. Additionally, in the power sector, were announced the privatization of Eletrobrás distributors, which are expected to be concluded by the end of 2017. However, the CELG's auction was already concluded on 30 November, after the first attempt got frustrated, and the purchase price reduced from 2,800 million to 1,700 million. The winner was the Italian company ENEL, which presented the only proposal, with a goodwill of 0.5 billion.

In October 2016, the transmission auction was also concluded, and 21 from 24 enterprises were contracted. This was possible after ANEEL changed the rules of interest rate of annual allowed revenue (RAP), considering that the first edition of this auction, before Michel Temer's assumption, had only 10 from 24 enterprises contracted.

The GPD expectation for 2016, according to Focus market expectations report on 30 December, is a retraction of -3.49%. For 2017, is expected an increase of 0.5%, and IPCA inflation index is expected to reduce to 4.87%, almost reaching the target of 4.5%.

3. Other Regulatory Changes

On 29 December 2014, by virtue of Resolution 4947/2014, the introduction of the system of tariff flags was approved starting in January 2015. The procedure provides for short-term adjustments to be made to tariffs through the use of triggering indicators in the energy cost component in final tariffs. Tariff flags are determined on a monthly basis and their purpose is to mitigate the exposure of distributors' cash flows to high energy prices by reducing the difference between the price paid for energy by distributors and the price paid by consumers to distributors through tariff. A green flag signals low energy purchasing costs and does not change tariffs paid by consumers. A yellow flag signals that power generation costs are rising due to use of thermal energy in the generation mix and leads to a BRL 25 MWh increase in price. A red flag signals a situation where the costs of providing electrical utilities are becoming even more expensive due to the use of inefficient thermal power stations and results in a BRL 55 MWh increase in tariff. The values of each tariff flag are revised annually or when necessary. In December 2015, since the most expensive thermal plants were shut down, therefore lowering generation costs, ANEEL ruled that red flag would have its additional cost divided in two levels, in which level 2 adds BRL 55 MWh and level 1 adds BRL 45 MWh. From April to December 2016, except for November, it was applied green flag, with no additional value to the tariff.

On 27 August 2015, the Public Hearing to set ABRACE's associates' tariffs (Brazilian Large Industrial Energy Consumers and Free Consumers Association) was opened. CDE ("*Conta de Desenvolvimento Energético*") charge is calculated proportionally to the level of consumption for all the consumers, which means that the largest consumers pay consequently more. ABRACE disagrees with CDE's calculation method and has won an injunction that allows the association not to pay a part of the charge. The result of this Public Hearing will not have impacts in ELEKTRO's results, but is a temporally cash flow mismatch. On 24 September 2015, ANEEL's board meeting discussed the results of the Public Hearing. ANEEL's decision is to publish the new tariff value of ABRACE's associates according to what the injunction determines. The impacts will be retroactive to the injunction date; 3 July 2015. ANEEL is trying to revert the judicial decision. ABRADÉE (Brazilian Electricity Distributors) has filled an injunction in order to protect distributors from any effects. There is still no judicial decision; therefore ABRACE's injunction is still in play. In December 2015, ABRADÉE won the injunction to allow distributors to discount from CDE quota the amounts uncollected by the new tariffs published.

In June 2016, ANACE's associates (National Energy Consumers Association) won another injunction, which took effect since January 2016 that discharge then to pay CDE. On 12 June 2016, ANEEL published Dispatch 1576, regulating the operationalization of the process and allowing distributors to discount of CDE the uncollected revenues since the beginning of ABRACE's injunction effect, in 3 July 2015.

With regard to the sub-transmission assets transfer, in 2015, a Public Hearing was opened in order to collect subsidies from agents to the proposal designed by ANEEL. However, the proposal placed by ANEEL displeased many of the agents involved, and there is still strong resistance to the transfer by the transmission agents. In 2016, the Public Hearing came to a second phase, with a new proposal, less wide than the previous one and easier to be implemented. It is still pending ANEEL's final position about the subject.

On 24 May 2016, ANEEL opened a public hearing to propose an amendment to the concession contract of the distributors who still have not renewed its concession, under the terms of the Law nº 12.783/2013, such as Elektro. ANEEL claims that the newly approved rules for Tariff Adjustment processes are more adequate and, if the concessionaire agrees, the agency can allow the signature of an addendum that incorporates these changes into the concession contract. By the proposal, only the economic clauses regarding distribution tariffs would be discussed. Some proposed changes are:

- The substitution of the IGPM index for the IPCA when updating Parcel B (distribution costs).
- Full neutrality on Parcel A (power purchase and grid costs and regulatory charges), and the migration of the bad debt allowance from Parcel A to Parcel B.
- Extension of the Tariff Revision interval to 5 years.

On 6 September 2016, ANEEL opened another public hearing to discuss improvement of the tariff procedures to be applied to distributors which already renewed their concessions and to companies that choose to adhere to the tariff terms of the new contract. The goal is to define the methodology and formulas of the new tariff calculation rules (PRORET).

In July 2016 ANEEL published a public call for the strategic Research & Development Project entitled: "Improvement of the power sector's business model". The proposal aims to review and discuss the sector's market and business model as a whole. The Project is expected to begin in 2017 and finish in the middle of 2018. Elektro demonstrated interest and is participating together with ABRADÉE Institute. Bain & Company was chosen by the R&D participants to development, and COELBA will be the project coordinator (Elektro was not eligible, once it has already coordinated a Tariff Structure Strategic R&D in 2014). The project of development was already sent to ANEEL evaluation, and is expected to begin in March 2017.

On 6 September 2016, ANEEL approved the regulation for the white hourly tariff for low voltage clients. This allows different tariff prices for customers, and stimulates consumption out of peak hour. The application depends on voluntary adhesion by consumers. The application of white tariff to interested consumers will start in January 2018 and will be gradually applied to customers until 2020.

On 5 October, the Ministry of Mines and Energy (MME) opened a Public Consulting aiming to gather agents' perceptions about the free market environment. MME wants to analyze the impacts concerning market liberalization, such as: population information about the subject, whether binomial tariffs are a requisite to its expansion, possible changes in contracts between generators and distributors and needs of improvement in the current regulation, among others.

On 18 November, the Provisional Measure 735 was converted into Law 13,360 by President Michel Temer. The main changes established are:

- From May 2017, the managing role of the CDE, the RGR (Global Reversion Reserve) and the CCC (Fuel Consumption Account) will be transferred from Eletrobras to CCEE (Chamber of Electricity Trading).
- The apportionment of CDE quotas between distributors will gradually adjust from 2017 to 2030, when the quotas will finally be apportioned proportionally to each distributor's energy market.
- Alters CDE's allocation between clients: Consumers with Social Energy Tariff (low income consumers) won't pay the charge, and Medium and High Voltage clients will pay gradually less each year.
- Increases in Itaipu's Tariff: The additional cost that was paid by the National Treasury to Paraguay for its energy surplus will now be included in the tariffs.
- Grants permission for distributors to negotiate their energy surpluses with free clients: still must be regulated by MME and ANEEL;
- Allow the transfer of control of the company instead of concession termination in certain cases - this should facilitate the privatization of Eletrobras' distributors and the sale of Abengoa's assets;
- New generation projects could sell energy in A-5 and A-7 auctions.
- Existing generators can participate in new energy auction until two years after construction.
- For delay in the beginning of operation in generation and transmission enterprises, there is the possibility of extending the contract in case of excluding of responsibility. The law defines which causes could be classified as excluding of responsibility.

The changes established by Law 13.360 still depend on regulation by ANEEL, and most of the rules will be applied in 2017. There is no impact to Elektro, although this changes could cause an increase of tariffs to consumers.

5. MAIN RISKS AND UNCERTAINTIES

5.1 Risk Management System

The IBERDROLA Group is exposed to various inherent risks in the countries, industries and markets in which it operates and the businesses it carries out, which could prevent it from achieving its objectives and executing its strategies successfully.

The Company's Board of Directors, aware of the importance of this matter, promotes the necessary mechanisms so that the risks relevant to all of the Group's activities and businesses are appropriately identified, measured, managed and controlled, and has established, through the Group's general risk control and management policy, the basic mechanisms and principles necessary for the appropriate management of risk-opportunity with a level of risk which allows:

- attain the strategic objectives formulated by the Group with controlled volatility;
- provide the maximum level of assurance to the shareholders;
- protect the results and reputation of the Group;
- defend the interests of shareholders, customers, other groups interested in the progress of the Company, and of the society in general; and
- ensure corporate stability and financial strength in a sustained manner over time.

For the development of the aforementioned commitment, the Board of Directors and its Executive Committee have the cooperation of the Audit and Risk Supervision Committee, which, as a consultative body, monitors and reports upon the appropriateness of the assessment system and internal control of significant risks, acting in coordination with the audit committees existing in other companies of the Group.

Every action aimed at controlling and mitigating risks will consider the following basic action principles:

- a) Integrate the risk-opportunity vision into the Company's management, through a definition of the strategy and the risk appetite and the incorporation of this variable into strategic and operating decisions.
- b) Segregate functions, at the operating level, between risk-taking areas and areas responsible for the analysis, control, and monitoring of such risks, ensuring an appropriate level of independence.
- c) Guarantee the proper use of risk-hedging instruments and the maintenance of records thereof as required by applicable law.
- d) Inform regulatory agencies and principal external players, in a transparent way, regarding the Group risks and the operation of the systems developed to monitor such risks, maintaining suitable channels that favour communication.
- e) Ensure appropriate compliance with the corporate governance rules established by the Company through its Corporate governance system and the update and continuous improvement of such system within the framework of the best international practices for transparency and good governance, and implement the monitoring and measurement thereof.

- f) Act at all times in compliance with the law and the Company's corporate governance system and, specifically, with the values and standards of conduct established in the *Code of Ethics*, and pursuant to the principle of zero tolerance of illegal acts and fraud set forth in the *Crime Prevention and Anti-Fraud Policy*.

The *Control and risk management general policy* and its basic principles are implemented by means of a comprehensive risk control and management system, supported by a Corporate Risk Committee and based upon a proper definition and allocation of duties and responsibilities at the operating level and upon procedures, system methodologies and tools suitable for the various system stages and activities including:

- a) The ongoing identification of significant risks and threats based on their possible impact on key management objectives and the financial statements (including contingent liabilities and other off-balance risks).
- b) The analysis of such risks, both at each corporate business or function and taking into account their combined effect on the Group as a whole.
- c) The establishment of a structure of policies, guidelines, and limits, as well as of the corresponding mechanisms for its approval and implementation, which effectively contribute to risk management being performed in accordance with the Company's risk appetite.
- d) The measurement and controlling of risks by following procedures and standards which are homogeneous and common to the Group as a whole.
- e) The analysis of risks associated with new investments, as an essential element of decision-making based upon profitability-risk.
- f) The maintenance of a system for internal controlling of compliance with policies, guidelines and limits, by means of appropriate procedures and systems, including the contingency plans needed to mitigate the impact of the materialisation of risks.
- g) The periodic monitoring and control of profit and loss account risks in order to control the volatility of the annual income of the Group.
- h) The ongoing evaluation of the suitability and efficiency of applying the system and the best practices and recommendations in the area of risks for its eventual inclusion in the model.
- i) The audit of the system by the Internal Audit.

In addition, the *Control and risk management general policy* is further developed and supplemented by the *Risk corporate policies* and the *Risk specific policies* established in connection with certain businesses and/or companies of the Group, which are listed below and are also subject to approval by the Company's Board of Directors.

Corporate risk policies structure:

- a) Control and risk management general policy.
- b) Corporate credit risk policy.
 - Corporate credit risk policy.
 - Corporate market risk policy.
 - Operational risk policy in market transactions.
 - Insurance policy.

- Investment policy.
- Financing and financial risk policy.
- Treasury share policy.
- Risk policy for equity interests in listed companies.
- Reputational risk framework policy.
- Purchasing policy.
- IT policy.
- Cybersecurity risk policy.

c) Risk policies for the various businesses of the Group:

- Risk policy for the deregulated business of the IBERDROLA Group.
- Risk policy for the renewables business of the IBERDROLA Group.
- Risk policy for the network business of the IBERDROLA Group.
- Risk policy for the Real Estate business of the IBERDROLA Group.
- Risk policy for the engineering and construction business of the IBERDROLA Group.

The *Control and risk management general policy*, as well as the *Summary of the corporate risk policies* and the *Summary of the Risk specific policies* for the various businesses of the Group are available on the corporate website (www.iberdrola.com).

In order to align the risk impact with the established risk appetite, the Executive Committee of the Board of Directors, acting at the proposal of the business or corporate divisions involved and upon a prior report from the Group's Risk Committee, annually reviews and approves specific guidelines regarding the Group's risk limits.

Pursuant to established guidelines, the competent administrative bodies of each company of the Group, within such company's area of responsibility, reviews and approves the specific risk limits applicable to each of them.

The companies and corporate functions of the Group are responsible for implementing, within their areas of activity, the control systems required for compliance with the *Control and risk management general policy* and with the limits thereunder.

The risk factors to which the Group is generally subject are listed below:

- a) Corporate Governance Risks: the Company assumes the need to safeguard the social interest of the Company and the strategy of sustained maximisation of the economic value of the Company and its long-term success, in accordance with social interest, culture and the Group's corporate vision, taking into account the legitimate public and private interests that converge in the conduct of all business activities, particularly those of the various stakeholders and communities and regions in which the Company and its employees act. A fundamental requirement for the foregoing is compliance with the Company's Corporate governance system, comprising the By-Laws, the Corporate policies, the internal corporate governance rules and the other internal codes and procedures approved by the competent decision-making bodies of the Company and inspired by the good governance recommendations generally recognised in international markets.

- b) Market risks: defined as the exposure of the Group's results and equity to changes in market prices and variables, such as exchange rates, interest rates, commodity prices (electricity, gas, CO₂ emission rights, other fuel, etc.), prices of financial assets and others.
- c) Credit risks: defined as the possibility that a counterparty fails to perform its contractual obligations, thus causing an economic or financial loss to the Group. Counterparties can be final customers, counterparties in financial or energy markets, partners, suppliers, or contractors.
- d) Business risks: defined as the uncertainty regarding the performance of key variables inherent in the business, such as the characteristics of demand, weather conditions, the strategies of different players, and others.
- e) Regulatory and political risks: defined as those arising from regulatory changes made by the various regulators, such as changes in compensation of regulated activities or in the required conditions of supply, environmental regulation, tax regulation including risks relating to political changes that might affect legal security and the legal framework applicable to the businesses of the Group in each jurisdiction, the nationalisation or expropriation of assets, the cancellation of operating licenses and the early termination of contracts with Government.
- f) Operational, technological, environmental, social and legal risks: defined as those related to direct or indirect economic losses resulting from inadequate internal procedures, technical failures, human error, or as a consequence of certain external events, including the economic, social, environmental, and reputational impact thereof, as well as legal and fraud risks. The said risks include those associated with information technology and cybersecurity, as well as the risk of technological obsolescence, among others.
- g) Reputational risks: potential negative impact on the value of the Company resulting from Company's behaviour below the expectations created among various stakeholders: shareholders, customers, media, analysts, Government, employees, and society in general.

Due to its universal and dynamic nature, the system allows for the consideration of new risks that may affect the Group as a consequence of changes in its operating environment or revisions of objectives and strategies, as well as adjustments resulting from ongoing monitoring, verification, review and supervision activities.

The Audit and Risk Supervision Committee of the Board of Directors periodically monitors the evolution of the Company's risks:

- It reviews the Group's risk quarterly reports, which include monitoring compliance with risk limits and indicators and updated key risk maps, submitted by the Group's director of corporate risks.
- It coordinates and reviews risk reports sent periodically, at least semi-annually, by the audit and compliance committees of the main subsidiaries of the Group, being included the subholding companies of the main countries where the Group operates that, along with the risk director appearances are used to prepare a risk report for the Board of Directors at least twice per year.

For further details, see the section *Control systems and risk management of the Corporate Governance Report 2016*.

5.2 Credit risk

The IBERDROLA Group is exposed to credit risk arising from its counterparties (customers, suppliers, financial institutions, partners, etc.) default on their contractual obligations. The exposure may arise with regard to unsettled amounts, the cost of substituting products not supplied and also, in the case of dedicated plants, outstanding amounts.

The credit risk is managed and limited in accordance with the type of transaction and the creditworthiness of the counterparties. A specific corporate credit risk policy is in place which establishes criteria for admission, approval systems, authorisation levels, scoring tools, exposure measurement methodologies, etc.

With regard to credit risk on trade receivables, the historical cost of defaults has remained moderate and stable at close to 1% of total turnover of this activity, despite the current difficult economic environment. Regarding other exposure (counterparties in transactions with financial derivatives, placement of cash surpluses, transactions involving energy and guarantees received from third parties), no significant defaults or losses were incurred in 2016 or 2015.

At 31 December 2016 and 2015, there is no significant credit risk concentration in the IBERDROLA Group.

5.3 Financial risks

5.3.1 Interest rate risk

The IBERDROLA Group is exposed to the risk of fluctuations in interest rates affecting cash flows and market value in respect of items in the balance sheet (debt and derivatives). In order to adequately manage and limit this risk, the IBERDROLA Group manages annually the proportion of fixed and variable debt and establishes the actions to be carried out throughout the year: new sources of financing (at a fixed, floating or indexed rate) and/or the use of interest rate derivatives.

Debt arranged at floating interest rates is basically tied to Euribor, Libor-GBP and Libor-USD and to the most liquid local reference indexes in the case of the borrowings of the Latin American subsidiaries.

The debt structure at 31 December 2016, once considered the hedge provided by the derivatives traded, is included in the Note 5 of the Consolidated financial statements.

5.3.2 Foreign currency translation risk

As the IBERDROLA Group's presentation currency is the euro, fluctuations in the value of the currencies in which borrowings are instrumented and transactions are carried out with respect to the euro, mainly the Sterling Pound, the US Dollar and the Brazilian Real, may have an effect on the finance costs, profit and equity of the Group.

The following items could be affected by foreign currency translation risk:

- Collections and payments for supplies, services or equipment acquisition in currencies other than the local or functional currency.
- Income and expenses of certain foreign subsidiaries indexed in currencies other than the local or functional currency.
- Debt denominated in currencies other than the local or functional currency of the IBERDROLA Group companies.
- Profit or loss on consolidation of foreign subsidiaries.
- Consolidated carrying amount of net investments in foreign subsidiaries.

The IBERDROLA Group reduces this risk by

- Ensuring that all its economic flows are carried out in the currency of each Group company, provided that this is possible and economically viable and efficient, through the use of derivatives if not.

- As far as possible, this covers the risk of transfer of earnings scheduled for the current year, thereby limiting the ultimate impact on Group earnings.
- Mitigating the impact on the consolidated net asset value of a hypothetical depreciation of currencies due to Group's investment in foreign subsidiaries by maintaining foreign currency debt, as well as through financial derivatives.

The debt structure at 31 December 2016, once considered the hedge provided by the derivatives traded, is included in the Note 5 of the Consolidated financial statements.

5.3.3 Liquidity risk

Exposure to adverse situations in the debt or capital markets or in relation to the IBERDROLA Group's own economic-financial situation may hinder or prevent the IBERDROLA Group from obtaining the financing required to properly carry on its business activities.

The IBERDROLA Group's liquidity policy is aimed at ensuring that it can meet its payment obligations without having to obtain financing under unfavourable terms. For this purpose, various management measures are used such as the arrangement of committed credit facilities of sufficient amount, deadline and flexibility, diversification of the coverage of financing needs through access to different markets and geographical areas, and diversification of the maturities of the debt issued.

The sum of cash, liquid assets and committed undrawn credit facilities would sufficiently cover the Group's expected liquidity requirements for a period of over 24 months, excluding the arrangement of any new credit.

The figures relating to changes in the Company's debt are included in Notes 25 and 50 to the Consolidated financial statements.

5.4 Country risk

The activities of the different businesses that the IBERDROLA Group developed are submitted, in greater or lesser extent depending on their characteristics, to various risks inherent to the country where they operate:

- Imposition of monetary and other restrictions on the movement of capital
- Changes in the trade environment
- Economic crisis, political instability and social riots affecting operations
- Nationalisation or expropriation of assets
- Exchange rate fluctuations
- Cancellation of operating licenses
- Anticipated termination of Government contracts
- Changes to administrative policies and regulations in the country

The results of our international subsidiaries, their market value and their contribution to the Group may be affected by such risks.

The IBERDROLA Group's main operations are focused on Spain, United Kingdom, USA, Brazil and Mexico, countries with low or moderate risk, whose credit ratings are as follows:

Country	Moody's	S&P	Fitch
Spain	Baa2	BBB+	BBB+
United Kingdom	Aa1	AA	AA
USA	Aaa	AA+	AAA
Brazil	Ba2	BB	BB
Mexico	A3	BBB+	BBB+

The presence in countries other than the ones mentioned above is not significant at Group level from an economic point of view.

5.5 Activity risks

The activities of the various businesses developed by the IBERDROLA Group are subject to various risks including market, credit, operational, business, regulatory and reputational risks arising from the uncertainty of the main variables that affect them.

5.5.1 Regulatory and political risks

Companies in the IBERDROLA Group are subject to laws and regulations concerning prices and other aspects of their activities in each of the countries in which they operate. The introduction of new laws and regulations or amendments to the already existing ones may have an adverse effect on the Group's operations annual results and economic value of businesses.

The following paragraphs are a few of the new major regulatory measures that were approved in 2016 or are due to be implemented in 2017:

Spain:

- Approval on 17 June 2016 of the Order IET/980/2016 establishing remuneration for electricity distribution companies in 2016, stipulating total remuneration for the Iberdrola Group of EUR 1,655 million (up by 2.7% against 2015) and a regulatory asset base (RAB) for the Group's distribution assets of EUR 8,694 million, thereby removing any uncertainty.

United Kingdom:

- Publication of the final report and conclusions of the Competition Market Authority (CMA) about the gas and electricity retail market analysis in UK with moderate impact for Scottish Power. Its main measures include:
 - o The application of a price cap for prepaid customers.
 - o The creation of a database shared with customer information in order to encourage competition.
 - o The elimination of certain tariff limitations.
- Economic, political and regulatory uncertainty arising from the outcome of the referendum on the exit of the United Kingdom from the European Union, held in June 2016.

United States:

- Approval of rate cases by the regulator of the State of New York RG&E and NYSEG, valid from July 2016 for a period of three years, in satisfactory terms for the Company.

- The approval in the United States of the new tax incentive scheme for the development of renewable energy Production Tax Credits, valid until 2020.

Brazil:

- Approval of Elektro's four-year tariff review, by the Brazilian regulator ANEEL, valid up to August 2019, in satisfactory terms for the Company.

Mexico:

- Possible impact on the Mexican economy of some of the new political and economic measures, announced during the recent election campaign in the US, by the new Trump administration, such as the introduction of trade tariffs.
- Uncertainties about the Energy Market Reform currently being drawn up which, according to the best information available, could affect the profitability of assets dedicated to selling electricity to private partners and the outlook for plants currently under construction.

5.5.2 Network business risk

The regulations of each country in which the IBERDROLA Group's network businesses operate establish regularly revised frameworks, guaranteeing that these businesses will receive reasonable and predictable returns. These frameworks include penalties and bonuses for efficiency, service quality and, eventually, for default management, which have a minor, immaterial impact overall. Significant structural amendments to these regulations could suppose a risk to these businesses.

In general, the profitability of the IBERDROLA Group's network businesses is not exposed to demand risk, except for the Brazilian subsidiaries.

The IBERDROLA Group's network businesses in Spain and in the United Kingdom are not exposed to any market risk associated with energy prices.

The network businesses in Brazil and some of the businesses in the USA sell energy to regulated customers at a price determined by certain previously approved tariffs. In the case of a prudent procurement management and as established by the regulator, the regulatory frameworks in both countries guarantee sums will be collected in subsequent tariff readjustment reviews for possible purchase price deviations from those previously recognised in the tariff.

Given the above, in the case of extraordinary events (extreme drought in Brazil as happened in 2014, catastrophic storms in USA, etc.), occasional temporary gaps between payments and collections may arise with an impact on the cash flows of some of these businesses and eventually on profits recognised under IFRS.

- **Spanish Networks:**

The present regulatory model is based on Electric Industry Law 24/2013 of 26 December, establishing regulatory six-year periods and profitability for distribution activity calculated as the yield on government bonds plus 200 basis points. Profitability was set at 6.5% for the first regulatory period.

The Royal Decree 1048/2013 of 27 December establishing the methodology to calculate remuneration for electricity distribution activities defines a methodology based on standard unit costs of investment and operation. The remuneration of facilities will be calculated on the basis of the real audited cost and the standard cost recognised for each investment, and therefore profitability will depend on the constructive efficiency achieved.

In terms of distribution incentives, the Royal Decree 1048/2013 modifies the definitions of current quality incentives and losses, and establishes a new anti-fraud incentive.

Moreover, in accordance with current regulations, the distribution company does not sell any energy to customers, and it is therefore not exposed to market risk at the present time. This means that fluctuations in demand have no direct impact on the income statement.

– **United Kingdom Networks:**

The group operates in the United Kingdom through its subsidiary Scottish Power Ltd and the following licences:

- SP Distribution PLC (SPD)
- SP Manweb PLC (SPM)
- SP Transmission PLC (SPT)

The current regulatory model for SPD and SPM is based on the RIIO ED1 framework, and on the RIIO T1 framework in the case of SPT. The latest tariff review for electricity distributors (RIIO ED1), including SPD and SPM, is valid from April 2015 to April 2023. The SPT review (RIIO T1) is valid from April 2013 to April 2021.

The weighted average cost of capital or WACC is set for each tariff period. The current real WACC after tax recognised for distribution activities was 3.4% from January to March, and 3.67% from April to December. In the case of transport business it was 4.27% from January to March, and 4.46% from April to December.

The regulator (OFGEM) also establishes incentives/penalties for safety, environmental impact, consumer satisfaction, social obligations, connections and quality, which may have an effect on the income statement.

– **United States Networks:**

The Iberdrola Group operates in the USA through its listed subsidiary Avangrid, which in turn has the following subsidiary network companies:

- New York State Electric & Gas (NYSEG), New York, with a 3-year rate case valid until 2019 (base ROE 9% for distribution).
- Rochester Gas and Electric (RG&E), New York, with a 3-year rate case valid until 2019 (base ROE 9% for distribution).
- Central Maine Power (CMP), Maine, conducting electricity distribution business with an annual extendable rate case (base ROE 9.15% for distribution), and transmission business (base ROE 10.57%).
- United Illuminating (UI), Connecticut, conducting electricity distribution business with a rate case currently undergoing an advanced review, and transmission business (base ROE 10.57%).
- It also has the following natural gas distribution companies: Maine Natural Gas Corporation (MNG), Connecticut Natural Gas (CNG), Southern Connecticut Gas (SCG) and Berkshire Gas (BG).

Companies carrying on regulated business in the USA are exposed to risks associated with the regulations of a number of federal regulatory bodies (FERC, CFTC, DEC) and state commissions, responsible for establishing the regulatory frameworks of the companies regulated (tariffs and other conditions).

The distributors' tariff plans have been designed to reduce the risk to which business is exposed through mechanisms for deferral, reconciliation and provisions for costs. Regulated distributors pass on the costs of gas and electricity to end customers, thereby mitigating any impacts of fluctuations in demand.

– **Brazilian Networks:**

The Iberdrola Group conducts its network business in Brazil through Elektro Redes, S.A. in the state of São Paulo, and the network business of its investee Neoenergia (39% Iberdrola Group), which has the electricity distributors Coelba, Celpe and Cosern in the respective states of Bahia, Pernambuco and Rio Grande do Norte.

Brazilian legislation applicable to regulated electricity distribution business establishes two types of costs: i) "Parcel A", which includes the costs of energy, transport and other obligations and regulatory charges, which can be recovered through tariffs ("pass through") as part of the conditions and limits imposed by ANEEL, except for other obligations and regulatory charges which can always be recovered through tariffs, and ii) "Parcel B", which includes remuneration for investment and the costs of operation and maintenance, which generate either an incentive or a risk for the investor.

ANEEL also acknowledges other smaller incentives to minimise default and impairment of quality and customer satisfaction that can affect the income statement.

Pursuant to current legislation, electricity distribution companies:

- a) transfer the cost of supplying electricity to the end customer through the regulated tariff, provided the energy contracted is between 100% and 105% of the demand required.
- b) risk penalties imposed by the regulator ANEEL, when this is less than 100% due to the exclusive responsibility of the distributor.
- c) risk price fluctuations when it is above 105%.

The dates of the next tariff reviews are as follows: Elektro: August 2019, Celpe: April 2017, Coelba and Cosern; April 2018.

5.5.3 **Renewables business**

The regulations of each country in which the Group operates establish regulatory frameworks aimed at promoting the development of renewable energies based on formulas which may include premiums, green certificates, tax or regulated tariff deductions, which allow investors to obtain sufficient and reasonable return. Any change to the aforementioned regulation may represent a risk for said business.

In addition to the aforementioned regulatory risk, Group's renewable energy businesses may be subject, to a greater or lesser extent, to wind resource risk and market risk.

The Group considers that the wind resource risk is mitigated through the high number of wind power farms available and their geographic diversification, and the trend to compensate less wind energy periods with those with high wind energy on the medium term.

Regarding the electricity price risk the following should be mentioned:

– **Renewables business – Spain**

The Group currently has a renewable installed capacity in Spain of: 5,507 MW wind farms, 303 MW mini hydro, 50 MW solar thermal and 0.09 MW photovoltaic.

Subsequent to the approval of the new regulatory framework (the Royal Decree-law 9/2013, of 12 July, Law 24/2013, of 26 December, the Royal Decree 413/2014, of 6 June, and the Ministerial Order

IET/1045/2014, of 16 June), all renewable energy generated is remunerated at market price plus a premium per MW. This guarantees a reasonable regulated return based on a recognised standard investment. This return is readjusted every three years within predetermined bands to cover any possible deviation in market price. This premium per MW is not applicable for wind farms brought on line during and before 2004. As a result, initially all output would be fully or partially exposed to market risk.

- **Renewables business – United Kingdom**

The Group's current renewables installed capacity in the UK is: 1,619 MW in onshore wind plants and 195 MW in offshore wind plants, operational under current "Renewables Obligation" legislation. This means that income is partially exposed to the risk of the market price for electricity in the UK, as the revenues obtained comprise income from the price of the energy produced and the sale of renewables obligation certificates (ROC certificates).

UK regulations impose minimum ROC obligations per MWh sold on sellers of electricity, 10% more than the system envisages producing, and determine the price at which the rest must buy, which in practice amounts to a floor price at the price of the ROCs.

New renewable technology plants, implemented as of 2016 and 2017 (onshore wind plants, implemented since 12 May 2016, and the rest as of 1 April 2017), are subject to the new "Contract for Difference" remuneration scheme, or CfD, which eliminates market risk for 15 years.

The fixed prices for these projects are established on a project-by-project basis through public tenders. The counterparty guaranteeing this price, "The Low Carbon Contracts Company", finances its potential payments by charging a fee to distributors depending on their market share, and therefore the credit risk with the counterparty is practically zero.

The East Anglia offshore plant, currently under construction, has been awarded a CfD contract.

German offshore wind plant

The renewables division in the UK also manages offshore wind business in other European countries, among which the Wikinger offshore plant (Germany), currently under construction.

Pursuant to German regulations, the new Wikinger plant will have a fixed price for the energy it produces over the first 15 years of operation on a CfD contract, similar to the aforementioned setup in the UK.

The positions exposed to market risk of the renewables businesses in Spain and the UK are managed and included in their position in the Deregulated businesses in these countries, to be hedged in the most efficient manner possible.

In relation to electricity price risk in other countries, mention should be made of the following:

- **Renewables United States**

The Iberdrola Group conducts its renewables business in the US through its listed company Avangrid, which has an installed capacity of 5,588 MW in onshore wind plants, and 50MW in operational photovoltaic plants.

At the present time, approximately 67% of the energy produced is sold on fixed-price long-term contracts with third parties, and some 33% of the energy produced is sold to the market on more short-term arrangements.

With electricity prices around USD 30 per MWh, a 5% change in prices could give rise to an impact of EUR ±8 million on operating results.

– **Renewables Mexico**

In Mexico the business now has an installed capacity of 367 MW in operational onshore wind plants, with two sale schemes: a) fixed-price sale to the CFE on a long-term contract and b) sale to third parties with a discount on the official price published by the CFE.

– **Renewables Brazil**

In Brazil the business now has an installed capacity of 187.3 MW in onshore wind plants, all operating on long-term contracts (PPAs) with a fixed price for the country's distributors. Excesses and shortages in the production contracted with the distributor are settled over periods of four years, and excesses must be offered and shortages purchased at market prices.

– **Renewables business in other European countries**

Installed capacity is currently 615 MW in wind plants and 6.17 MW in photovoltaic facilities operational in Greece, Portugal and other European countries.

Regulations in these countries make a distinction between two energy sale schemes: sales at the tariff (Portugal, Greece, Cyprus and Hungary), or sales at market price plus green certificates (Italy and Romania).

5.5.4 Deregulated electricity and gas generation and retailing businesses Commodity price risk

The activities of the Group's deregulated businesses are subject to a range of market, credit, operating, business and regulatory risks, coming from the uncertainty of the main variables that affect them, such as: fluctuations in commodity prices, changes in hydroelectric and wind energy production (of both the Group's and of third parties), changes in electricity and gas demand, and plant availability.

The main variable that affects IBERDROLA's result in terms of raw materials' market price is the electricity price. However, in many countries, electricity prices are strongly correlated with the price of the fuels used in its production. Therefore, risk studies are carried out on fuel price trends.

In the case of fuel and CO₂ emission allowances, these risks are evident in:

- The electricity generation and retailing business, in which the IBERDROLA Group is exposed to variations in the price of CO₂ emission allowances and in the sale price of electricity, as well as to variations in fuel costs (mainly gas and coal).
- The gas retailing business, in which a large portion of the IBERDROLA Group's operating expenses relate to the purchase of gas for customer supplies. The IBERDROLA Group is therefore exposed to the risk of variations in the price of gas.
- Unhedged energy transactions (discretionary trading).

To a large extent, the mutual closing out of positions by the generation business and retailing business mitigates the market risk to which the Group is exposed. The remaining risk is mitigated by diversifying sale and purchase agreements, and specific clauses therein, as well as by arranging derivatives.

- **Deregulated business in Spain**

Commodities' Price risk

Given current market conditions, the production price of the coal-fired power plants defines, to a large extent, the price of electricity in Spain since coal is the marginal technology necessary to cover electricity demand. Consequently, the price of coal conditions revenues from the other less expensive technologies which are used to cover demand. With coal prices around USD 68 per tonne, a 5% change in the prices could give rise to an impact of EUR ± 15 million on operating results.

The price of CO₂ influences the cost of production in coal-fired power plants. With coal prices around EUR 4.85 per tonne, a 5% change in the prices could give rise to an impact of EUR ± 3 million on operating results.

The majority of gas supplied in Spain is paid indexed to the price of oil by means of complex formulas. IBERDROLA has these types of agreements for the supply of gas, as well as other types of fixed-price supply and with prices not indexed to the market price of oil. These agreements are used for electricity generation, for the consumption of its final customers and for sale to other intermediaries. Due to the fact that the electricity generation margin is covered by the contracting formulas of the system operator, only residual risk remains in sales to final customers and third parties. The risk assumed is reduced and depends on the correlation between the price of oil and the European and international gas prices. In the event of a 5% fluctuation in the oil price, the risk would be EUR ± 1 million.

Hydraulic risk

Despite having a large water storage capacity, IBERDROLA's results depend significantly on the flow contributions. The changes in output with respect to the average value can be up to -4,000 GWh in a dry year and +5,000 GWh in a wet year, the variability would be between EUR ± 135 million. The loss of profit is not covered as it is an IBERDROLA's inherent risk.

Demand risk

Given the current market condition, where price is primarily determined by the generation cost of coal-fired plants, which make up around 15% of the generation mix, it is not considered that demand fluctuations will impact on marginal technology in the market. The impact on the market price of a 1% change in demand is therefore limited, amounting to approximately EUR 0.25 per MWh.

A moderate drop in demand in Spain does not affect the scheduled output of the Group's nuclear, hydroelectric and wind power plants, since there is a mandatory electricity market in Spain guaranteeing the efficient dispatch of output from all technologies.

Nevertheless, there could be an impact if a drop in electricity demand entails an equivalent reduction in the Group's retail sales and consequent narrowing of margin. This is mitigated to some extent by increasing sales of own energy on the wholesale market.

Taking both effects into account, it is estimated that a 1% fluctuation in demand would have an impact of EUR ± 8.5 million overall.

Operational risk

From the perspective of its impact on business results, the main risk arises from nuclear power plant outages (due to stoppages for fuel reloading, in accordance with a pre-established schedule) and hydroelectric power plant outages which are not associated with a large storage reservoir (flow facilities, in which water is not storable). As a result of such outages, production and, therefore, the margin associated with this production are lost. This risk is managed through excellence in the operating and maintenance practices of the plants and a culture focused on total quality and the reduction of operational risks, which allow the impact of this risk to be kept low.

- **Deregulated business – United Kingdom**

Commodity price risk

The IBERDROLA Group does not count on having coal plants in the UK after the closure of current plant Longannet at the end of March 2016.

In the British market, geared towards thermal power generation, the clean spark spread has become the appropriate index to follow the uncertainty of the margins of coal-fired power plants. Despite the fact that commodities (coal, CO₂ and electricity) are listed separately, the uncertainty of the unit margin is studied since it has been detected that it is a better indicator of the uncertainty of the results. With clean spark spread levels around GBP 3 per MWh, a 5% change in the spreads could give rise to an impact of EUR 5 million on operating results.

The IBERDROLA Group does not already have long-term gas contracts at fixed price.

Demand risk

Electricity consumption demand is usually one of the most significant risk factors for any company. However, IBERDROLA currently purchases from third parties a significant portion of the energy it sells (1,800, 2,500 and 4,100 GWh in 2015, 2014 and 2013, respectively, of a total amount of electricity sold of 22,000 GWh/year), since it is more profitable to do so under current market conditions than IBERDROLA producing it and using its own thermal power plants. From a business perspective, fluctuations in electricity demand mean that additional amounts of electricity need to be purchased or that these acquisitions need to be reduced. In any case, the profit or loss IBERDROLA obtains from this intermediation is low and much lower than that obtained from its own output. Thus, demand fluctuations have a small impact on profit or loss of EUR ±10 million for every 1% fluctuation in customer demand.

Operational risk

From the perspective of its impact on business results, the main risk arises from the combined cycle power plants outages. With regard to these outages, all profit or loss obtained from production is committed, although the high operating and maintenance standards of the plants and a culture focused on total quality and the reduction of operational risks, allow the impact on this risk to be kept low. Loss of profit from this type of events (material damages or machinery malfunctions) is covered by an insurance policy after a certain deductible level, which is marked by the risk retention level that IBERDROLA can assume and the insurance conditions that the market offers for risks of these types.

- **Deregulated business – Mexico**

Commodity price risk

Electricity generation at Iberdrola Generación Mexico is gas-intensive. Gas prices therefore comprise an essential component of this risk.

Approximately 83% of the electricity generated in Mexico is sold through long-term sales agreements (to CFE and, to a lesser extent, other major industrial customers), whereby the risk associated with the price of gas for generating this electricity is passed on.

The remaining energy is sold to customers at a price linked to the official tariffs published by CFE. These tariffs depend on the price of various fuels, specially fuel-oil, diesel, natural gas and coal.

As a result, there is a risk associated with the price of these fuels on the international markets, which is properly managed through operations in derivatives markets. These operations reduce the risk, with a lower final risk as a result.

- A 5% change in fuel-oil or diesel prices (which are closely linked) would give rise to a EUR ± 3 million change in results.
- A 5% change in the natural gas price would give rise to a EUR ± 1 million change in results.
- A 5% change in the price of coal would give rise to a EUR ± 1 million change in results.

Demand risk

The structure of the agreements IBERDROLA has entered into in Mexico isolates the business results from electricity demand fluctuations. Revenues come mainly from plant availability and only the sales indexed at the official Mexican tariff are subject to a certain extent by the fluctuation in demand. Nonetheless, most of the plants have committed sales exceeding their production capacity and therefore a shift in demand would not have an impact on their operations or results as the electricity generated would be sold to another customer. Changes in electricity demand in Mexico therefore have no effect on results.

Operational risk

From the perspective of its impact on business results, the main risk arises from combined cycle power plant outages. With regard to these outages, all profit or loss obtained from production is compromised, although the high operating and maintenance standards of the plants and a culture focused on total quality and the reduction of operational risks, allow the impact of this risk to be kept low. Loss of profit from this type of event (material damages or machinery malfunctions) is covered by an insurance policy after a certain deductible level, which is marked by the risk retention level that IBERDROLA can assume, and the insurance conditions that the market offers for risks of these types.

- Deregulated business – United States and Canada

Commodity price risk

IBERDROLA's business in the United States and Canada is geared towards natural gas transport and storage. As a result, the risk assumed mainly arises from fluctuations in the price of natural gas over time. There is no risk arising from the price levels but rather from the difference in the price of natural gas between the period of high prices (winter) and the period of low prices (summer). In the event the difference between both periods is USD 0.21 per MWh, if the aforementioned difference were to fluctuate by 5%, the uncertainty of the results would be EUR ± 1 million.

Operational risk

The business's gas storage facilities are exposed to operational risks associated with outages impeding the injection or extraction of gas, gas storage leaks and shifts in geological structures that hinder recovering injected gas.

IBERDROLA mitigates such risk by conforming to the highest standards of predictive and corrective maintenance, and permanently monitoring the geological parameters of the storage facilities. This will enable it to respond quickly to any potential threats that may be identified.

- Gas supply operations

The IBERDROLA Group maintains an adequate balance in the global mix, both in terms of the number of supplier countries and the type of supply (gas via pipelines or GNL), which is demonstrated in that it has five suppliers from different areas (Norway, Nigeria, Algeria and Qatar, among others).

In the Spanish case, gas supply is guaranteed through long-term agreements. The 23% of this mix of agreements is at a fixed price and the remainder is linked to the prices of various fuels on international markets.

Gas supply in Mexico is secured through long-term agreements with PEMEX and CFE at a price linked to international natural gas prices in the US and, therefore, with price that depends on the same gas prices in that country.

The gas business in the United States and Canada involves natural gas storage, whereby net gas purchases are not necessary over and above the fuel needed for the transfer, injection and extraction thereof. These quantities are small and procured gradually on local gas markets without the existence of long-term supply agreements.

- **Unhedged energy transactions (discretionary trading)**

Discretionary trading of electricity, gas, emissions allowances and other fuels and associated products performed by some of the Group's businesses is residual and the overall risk thereof is mitigated using individual stop-loss limits, whose total aggregate can never exceed 2% of the Consolidated net profit for the period, pursuant to the market risk policy approved by IBERDROLA, S.A.'s Board of Directors.

IBERDROLA has reduced discretionary trading in recent years in line with the widespread move away from market speculation. At 31 December 2015, the notional value of derivatives used in speculative trading (calculated in accordance with the criteria set forth in the European Market Infrastructure Regulation (EMIR)) was below EUR 135 million versus EUR 135 million at 31 December 2015. In any case, these values are much lower than EUR 3,000 million threshold that is set for non-financial companies in the European regulation (EMIR).

5.5.5 Other operational risks

During all of the IBERDROLA Group's activities, direct or indirect losses may arise as a result of inadequate internal procedures, technical failures, human error or external factors.

Any of these risks could cause damage or destruction to the IBERDROLA Group's facilities, as well as injuries to third parties or damage to the environment, along with the ensuing lawsuits, especially in the event of power outages caused by accidents at our distribution networks and possible penalties imposed by the authorities.

Although many of these risks are unpredictable, the IBERDROLA Group mitigates them by carrying out the necessary investments, implementing operation and maintenance procedures and programmes (supported by quality control systems), planning appropriate employee training, and taking out the required insurance covering both material damages and civil liability.

In relation to the insurance cover, IBERDROLA has international insurance programmes to cover equity (insurance for material damages, machinery breakdowns, loss of profits, damages from natural disasters and risks arising from construction work) and third-party liabilities (general civil liability, liability for environmental risks, professional civil liability, etc.).

However, this insurance does not completely eliminate operational risk, since it is not always possible, or it is not in its interest to pass such risk on to insurance companies and, in addition, cover is always subject to certain limitations.

Specifically, the IBERDROLA Group is also exposed to the following operational risks:

- Risk of malfunctions, explosions, fire, toxic spillages or polluted emissions in gas and electricity distribution networks and generating plants. Risks in connection with cybersecurity. Threats or vulnerabilities concerning data, control systems or Group information and communications systems, and any consequences arising from access to, use, disclosure, deterioration, interruption, unauthorised modification or destruction of information or information systems.
- Risks concerning extreme meteorological conditions and other instances of force majeure.
- Risk of sabotage and/or terrorism.

- **Risks in connection with nuclear business**

The IBERDROLA Group's nuclear power plants in Spain are also exposed to risks relating to their operations and risks arising from the storage and handling of radioactive materials.

- Constitutional Spanish law caps the liability of nuclear power plant operators in the event of a nuclear accident at EUR 700 million. This liability for a nuclear accident must be compulsorily insured by the operator of Spanish nuclear power plants. The IBERDROLA Group meets this obligation by taking out Nuclear Civil Liability insurance policies for each plant. However, Law 12/2011, of 27 May, concerning civil liability for nuclear damage or damage caused by radioactive materials, will increase the operator's liability ceiling and the consequent ceiling on mandatory insurance to EUR 1,200 million for nuclear power plants. The law will enter into force when all signatories of the Paris and Brussels Agreements ratify the 2004 Amendment Protocols, as established in these agreements.
- Accordingly, it is important to point out the indirect economic risk to which the aforementioned power plants are exposed as a result of a possible serious incident in Spain or in other country could affect the periodic renewals of their compulsory operating licences and the increase in their safety investments.

- **Environmental risks**

IBERDROLA accepts that the environment places constraints on all human activities and is a factor of companies' competitiveness, and it is committed to promoting innovation in this field and also ecoefficiency, to gradually reducing the environmental impact of its activities, facilities, products and services, and striving to ensure that its activities' development is congruent with future generations' legitimate right to an appropriate environment.

The Group undertakes and promotes this commitment through its policies. IBERDROLA currently has three specific policies in order to manage environmental issues: environmental policy, anti-climate change policy and biodiversity policy, which set forth the principles through which the Company will continue to improve its environmental management.

IBERDROLA was also included, for the twelfth consecutive year, on the global Dow Jones Sustainability Index, a worldwide benchmark for recognition of companies' contributions to sustainable development, as well as on other prestigious international sustainability indexes. It becomes the unique utility in the index since its creation in 1999.

- **Operational risk of operations in markets**

Market trading conducted by the Group's various energy trading desks and treasury dealers is also exposed to operational risk due to possible inappropriate processes, technological faults, human error, fraud or any other external or internal event.

This risk is mitigated by following the operational risk policy when trading on the market based on a robust risk control culture, a proper segregation of duties, the publication of clear processes and policies and secure and flexible information systems. This policy sets specific thresholds and guidelines applicable to all trades performed in accordance with the principle of proportionality.

- **Risks in connection with cybersecurity**

IBERDROLA Group companies may be affected by threats and vulnerabilities in connection with information, control systems or information and communications systems used by the Group, or by any consequences of unauthorised access to or the use, disclosure, degradation, interruption, modification or destruction of information or information systems, including the consequences of acts of terrorism.

These risks are managed in accordance with the basic principles of the cybersecurity policy, which takes the necessary measures to guarantee secure usage of information and communications systems and other cyber-assets, bolstering detection, prevention, defence and response capacities to counter cyberattacks.

5.5.6 Legal risks

The IBERDROLA Group companies are part of a certain in-court and out-of-court disputes within the ordinary course of their activities, the final result of which, in general, is uncertain. An adverse result, or an out-of-court resolution thereof or other proceedings in the future could have a material adverse effect on our business, financial situation, operating results and cash flows. However, the Group's legal advisers believe that the outcome of the aforementioned disputes will not have a significant effect.

Note 43 of the Consolidated financial statements contains a more detailed description of the most significant matters regarding "Contingent liabilities".

5.6 Risks materialised during the year

See *Risk management and control systems* of the 2016 Corporate governance report.

6. SIGNIFICANT SUBSEQUENT EVENTS TO YEAR END

Subsequent events to year end are described in Note 50 of the Consolidated financial statements.

7. RESEARCH AND DEVELOPMENT ACTIVITIES

- Iberdrola believes that innovation is a strategic variable which affects all areas of business and all our activities. We intend to lead innovation within the energy sector, focusing on sustainable development, promotion of renewable energies, utilisation of the opportunities presented by digitalisation in all areas, automation and a focus on technology and new business models. In 2016 more than EUR 211 million were invested in R+D+i, especially projects related to smart grids, clean energy generation, offshore wind facilities and new technologies and business models. More than 200 R+D+i projects, all of which are expected to have an effect on business in the short/medium term, are now ongoing thanks to the involvement of all Group employees.
- Thanks to a constant commitment to innovation, Iberdrola is now a world leader of the energy sector that has kept ahead of the energy transition to address the challenges of climate change and the need for clean energy, and has been acknowledged as Spain's most innovative utility and the third most innovative in Europe in the European Commission's classification.
- Iberdrola Ventures – PERSEO is IBERDROLA's corporate risk capital programme for investing in innovative technologies and business models to guarantee a sustainable energy model. On the international front, in 2016 a Silicon Valley company known as STEM, in which Perseo holds a stake, consolidated its position as leader of the distributed storage market, with more than 200 storage facilities operational. A Salamanca company in which Perseo likewise holds a stake, Arborea Intellbird, is also expanding. Arborea uses drones to inspect all kinds of energy infrastructures, and in 2016 it embarked upon international expansion, having surpassed the milestone of inspections of over 600 wind turbine blades in Spain and Mexico.

Under a clear strategy, which is set out in the 2015-2017 Innovation Plan, innovation is IBERDROLA's primary tool to guarantee the Company's sustainability, efficiency and competitiveness, focusing on three main issues:

- Efficiency, geared towards a continuous streamlining of our operations, managing the useful lives of facilities and equipment, cutting operation and maintenance costs, and reducing our environmental footprint with the aim of adapting to an environment which is more and more demanding and strives to improve constantly from the technological, processes and operations point of view.
- New products and services, in response to customers' needs in an increasingly global and competitive market. These projects deploy existing technology to produce business models offering power supply, facilities and technologies that are increasingly more efficient and environment-friendly such as energy efficiency, electric vehicles, smart grids and distributed energy resources.
- Disruptive business models and technologies that assist us in undertaking the energy challenges ahead, and adapting to the changes that are arising from the electric sector. Through PERSEO, IBERDROLA's corporate venture capital programme, we invest in new disruptive technologies and areas of business focusing on making the energy model sustainable.

Thanks to our human and economic resources allocated to innovation (EUR 211 thousand at 2016), we are now at the forefront of development of new products, services and business models that are transforming the energy sector.

Some of the most innovative ventures by major area are as follows.

7.1 Renewable energies

In 2016, Innovation activities in Renewables have focused primarily on:

- Improving the efficiency of our operating assets,
- Improving the integration of renewable energies,
- Developing new designs or processes for construction in progress or for future or ongoing projects associated with offshore wind power, highlighting the ones applied to Wikinger project (Germany) and East Anglia I (United Kingdom).

Efficiency improvement in Wind Farms is aimed at reducing operating and maintenance costs and improving production.

The field of energy resources continues with the development of an internal model for the design of wind farms based on fluid dynamics and the use of supercomputers.

The best use of the oils used in the gearbox of wind turbines is being analysed in order to extend its useful life and optimize the maintenance operations. The company is also involved in the joint Europe/Brazil HPC4E project (High Performance Computing for Energy) to prepare computational fluid dynamics (CFD) for tomorrow's "exascale" supercomputers.

Extending the lifespan of facilities, reducing costs and guaranteeing reliability are other challenges which are using large amounts of resources and labour on a yearly basis. For example, work continues on the OLEO and MINEROIL projects for the long-term analysis of the behaviour of lubrication oils in different models of machinery. The use of drones for visual thermographic inspections of wind turbine blades in situ at plants ensures early detection to prevent future large-scale damage or more expensive repairs (the Arborea project). Finally, in a bid to boost production without overloading certain components, an analysis was conducted and new control strategies were implemented for wind turbines.

Among the available tools to manage the exploitation of the wind farms, it is working on the continuous optimization of the production prediction to reduce the deviations from the actual production (Meteoflow), and work is also being carried out to monitor the main machinery of turbines and their throughputs for early detection of faults in components or reductions in output, through the use of artificial intelligence and big data.

One of the projects undertaken to integrate renewable energies is ESS2Wind, which sets out to analyse the possible application of battery storage systems for wind plants to provide them with ancillary services. Surveys have also been conducted on hybrid wind/solar/storage integration.

Innovation in offshore wind projects is essential to reduce costs and to limit risks in ongoing and future projects. The piles and jacket foundations for the Wiking offshore wind plant were assembled in 2016. This is the first Iberdrola wind plant to use this kind of foundations. The substation has a ground-breaking design with a 6-legged jacket foundation, and it was also built in two separate blocks (to make it easier to transport to the location), which were assembled afterwards in situ. The MARINEL project analysed an optimised design of the location of the substation's electrical equipment, with features such as alternatives for self-installable substations.

Work was also completed on the Flidar project, the main objective of which is to replace offshore meteorological towers which require costly foundations for their installation with floating stations with an alternative measuring system known as LIDAR (Light Detection and Ranging). Work continued to develop the Leanwind project, the main objective of which is to reduce costs over the plant's lifespan and the supply chain through the principles of "lean" application and the development of innovative solutions and tools. These solutions may be applied to all kinds of offshore facilities, including those with floating foundations, such as those being analysed in the Lifes50+ project.

IBERDROLA continues to work on the European Project Best Paths, which analyses the HVDC (High Voltage Direct Current) multiterminal networks from different suppliers to observe interactions with electrical equipment in wind turbines in a scenario in which offshore wind will be connected to the network. In the same area, work started on the European project "Promotion", which seeks to develop the technology of a number of HVDC systems (converters, protection devices and switching gear).

Finally, initiatives specifically orientated to sustainability such as BRIO project, should be highlighted, which aims to analyse the wind farm after its useful life and the valuation of the high value-added components of the wind turbine blades.

7.2 Clean generation technologies

During 2016, efforts in the area of generation focused on operating efficiency and flexibility, environmental protection, and the improvement of plant safety.

Operating efficiency and flexibility and plant safety: Following completion of the HOREX project a few years ago, work continued on the line of research into the chemical expansion of concrete with the PREXES project, focusing on development of a model to predict expansion in hydraulic concrete structures. With respect to safety at facilities, work started in 2016 on the VIDAGEN project to design and develop a tool to manage the global lifespan of pressurised equipment, with the possibility of adding a structural analysis module subsequently.

In the UK a project was carried out to inspect and repair low-pressure turbine rotor blades at the Rye House combined-cycle facility, using robotised tools, and the design and installation of an uninterruptible battery power supply system at Lanark & Galloway. Research was also conducted into pole fatigue in the Cruachan hydraulic generator.

In the area of nuclear generation, the prominent projects are FILTRONUC and RESONUC. The goal of this first project is to research and develop a new containment filtered venting system for maximising filtering performance on the venting line without compromising the safety and integrity of the facilities. The RESONUC project focuses monitoring and characterizing the resonances in critical systems to establish a solution, thereby ensuring they perform as well as possible as a significant contributor to nuclear plant safety and reliability.

Environmental: Iberdrola remains firmly committed to reducing the environmental impact of its generating plants, backing an ambitious project entitled CO2FORMARE to find a solution to the problem of macrofouling in the cooling systems of electricity generating plants in a sustainable manner and mitigating the environmental impact both emissions into the atmosphere and the aquatic environment.

During 2016, the technical expertise generated in COEBEN-II and implemented at Velilla del Rio Carrion served as a basis to launch the QUEMANOx and REMINOx projects, which use new designs for burners and a combination of technologies already developed to adapt our Lada and Velilla facilities to increasingly stringent environmental requirements, offering an alternative to high-cost commercial solutions.

7.3 Commercial Area - New projects and services

Innovation is essential in commercial activity, in order to offer customers the products and services best suited to their needs. Thus in 2016 IBERDROLA launched the following:

- New initiatives to boost the customer experience:

Innovative campaigns and projects were carried out in 2016, focusing on greater customisation of contents and offers, real-time dispatch of proactive communications, and a better online self-service, for a better and more homogeneous customer experience throughout the entire lifespan, thereby boosting customer engagement. Some of the initiatives were as follows:

- o Optimum tariff: Iberdrola advises its customers on the "*Plan a Tu Medida*" (Plan to Suit You), so that they pay less when they use less power. Here Iberdrola analyses the hourly consumptions of millions of customers to offer them the plan which best suits their consumption, with no need to change their habits. The plans were originally launched in 2015, and were the first plans launched in the sector to adapt the company to customers, instead of customers having to adapt to energy offers.
- o "Tu Asesor Energético" (Your Energy Advisor): this is an online portal which gives comprehensive advice to both individuals and businesses, regardless of whether or not they are customers, on all energy-saving aspects of power bills: optimisation of the economic offer, power output optimisation, advice on energy savings and energy efficiency, callback service to address any queries, and an omnichannel advice service (website, phone and in situ channels).

- New Smart Home products: Consumption Monitors and Smart Lamps:

Iberdrola now has a range of home energy management products using facilities with an Internet connection, providing customers with more information on the power they use, and enabling them to manage their consumption and save energy. A smart thermostat has been available since the beginning of 2015, and sales of the Consumption Monitor began in 2016 - this is an electric meter which can provide a breakdown of the consumptions of the main domestic appliances, and Smart Lamps, or smart LED bulbs which can be controlled by a mobile phone.

Iberdrola is also still involved in Green Mobility R+D+i projects, an area of business to meet the demands of customers and society in general concerning electrical mobility. In 2016 Iberdrola continued to work on innovation projects, among which REMOURBAN and AZKARGA. The CIRVE project also began in 2016, in which Iberdrola assists with the development of rapid-recharge infrastructure corridors for electric cars, to boost electric mobility and connect Spain to France and Portugal.

A pilot project is ongoing in the UK to assess the benefits of using batteries associated with photovoltaic micro-generation. Work is also being carried out to analyse customers' consumption data to give them energy efficiency advice and assistance. Finally, a proactive demand management programme is being offered to larger customers. With respect to new digital products, the new PowerUp platform enables consumers to buy gas or electricity in advance in one-day packages, one-month packages or packages of up to 180 days, at a pre-set price.

7.4 Smart grids

Iberdrola, a leader in digitalisation and automation of assets and infrastructures, is a pioneer developer of smart networks in Spain and Europe, with a constant commitment to safety, the environment and better supply quality. The following are a few of the main initiatives in 2016:

In Europe, Iberdrola leads the UPGRID project, with the goal of reinforcing its capability as an integrator of active demand and distributed generation in low voltage. The IGREENGrid project has been successfully concluded, aimed at finding innovative solutions to integrate renewable generation in the power distribution grid; as has been the DISCERN project, which compares different smart solutions for the grid with a view to achieving the most optimised set of architectures. Work continued on the GRID+STORAGE project to integrate storage solutions in electricity grids.

Spain is working on the LAYCA project to develop a system to locate breakdowns and characterise faults in medium-voltage systems. With respect to the standardisation and maintenance of overhead power lines, Iberdrola leads the MATUSALEN project to develop a tool which determines the aging of voltage cables in underground lines and is a partner on the SILECTRIC project, developing new insulators for overhead lines and high voltage switchgear. Work was completed on the TABON project to develop a verification technology and inspection line. In terms of operational systems, work continued on the development and validation of the new remote management system to provide immediate reliable access to the information required, integrating a number of modules for efficient management of the electricity grid and its meters. The BIDELEK project completed its innovative work on the development and industrialisation of new applications and devices.

A project known as FITNESS was carried out in the UK to demonstrate a new digital substation concept, in addition to the PHOENIX project, which aims to develop a new synchronous hybrid compensator to enable larger amounts of renewable energy to be used in situations when conventional power production is restricted, the POWER2TOWER project to investigate the feasibility of a system to monitor transport networks via wireless communication towers on the supports, and the VWAM project, which analyses virtual models of overhead power lines, developed using LiDAR technology.

Innovative projects are being carried out in Brazil in five main areas: smart systems, network quality and reliability, safety at facilities, loss reduction and sustainability. Two of the projects to develop domestic technology for smart networks were BID MONITOR, a backup system for decision-making concerning sales of electricity, and CIUDADE INTELIGENTE, to implement an urban reference model based on Smart Grids.

Initiatives in the US were deployed in the Energy Smart Community programme (ESC), which sets out to provide an efficient connection for consumers, the local community and the market for distributed energy resources. ESC has projects to improve efficiency, the consumer experience, smart grids and distributed energy resources. Another project, AMI, focuses on the automation of measurement infrastructures, while the ARIES project is an integrated overhead system to assess damage caused by meteorological phenomena, using LIDAR technology. The use of drones to detect damage caused to distribution and transmission lines by snowstorms is also remarkable.

Iberdrola's Technology Centre in Qatar focuses on the development of innovative solutions in three key areas of digitalisation of the electricity system: (1) smart grid measurement and automation, (2) integration of distributed renewable energy and (3) demand management. A number of R+D projects were started up with local universities and research centres, and the company also entered into consultancy projects with other electricity companies in the Middle East, transferring best practices in the design and deployment of smart grids.

7.5 IBERDROLA Ventures – PERSEO

IBERDROLA Ventures – PERSEO is IBERDROLA's Corporate Venture Capital programme, which has a budget of EUR 70 million for investing in innovative technologies and business models that guarantee a sustainable energy model. Since it was established in 2008, over EUR 50 million have been invested in start-ups which are developing technologies and new businesses in the global energy industry. Through this programme, IBERDROLA offers entrepreneurs, especially in the UK, the US and Spain, its investor support, its business knowledge, its base of 32 million customers and more than 45 GW of installed capacity. Additionally, it contributes to develop an innovative and dynamic business network in the energy sector.

The company focuses on several areas of interest including:

- Customer Oriented Solutions: energy efficiency, active demand management, digital solutions, etc.).
- Distributed Energy Resources: generation and storage innovative solutions.
- Renewable Energies: technology related to renewable generation (solar, eolic, offshore, etc.
- New technologies for the O&M of energy infrastructures (robotics, sensors, software, drones, etc.).

The current investment portfolio covers a wide and diverse range of projects under the umbrella IBERDROLA Ventures-PERSEO, together with other funding programmes for technology suppliers and projects with a high social component.

The most notable activities in 2016 included:

- On the international front, consolidation as the leader of the distributed storage market by Silicon Valley Company Stem. This start-up helps commercial and industrial customers save money with a solution for the meter using SW (big data and cloud) and batteries. During 2016, Stem notched up 200 distributed-storage facilities, and has attracted investment of more than USD 110 million since it was created.
- On the domestic front, growth and development of Arborea Intellbird (a company from Salamanca) in which Perseo holds a stake, which sells drone inspection services for all kinds of energy infrastructures. Arborea is now undergoing a major phase of international expansion and growth, in which it is being assisted by Iberdrola, and in 2016 it inspected more than 600 wind turbine blades of the company, carrying out preventive detection of anomalies to reduce the cost of repairs and improving plans for corrective maintenance.

8. ACQUISITION AND DISPOSAL OF TREASURY SHARES

The Group's treasury share policy establishes the following:

Treasury share transactions are considered those transactions carried out by the Company, whether directly or through any of the Group's companies, the object of which are Company shares, as well as financial instruments or agreements of any type, traded or not in the stock market or other organised secondary markets, which grant the right to acquire from, or the underlying security of which are, Company shares.

Treasury share transactions will always have legitimate purposes, such as, among others, to provide investors with liquidity and sufficient depth in the trading of Company shares, to execute treasury share purchase programmes approved by the Board of Directors or General Shareholders' Meeting resolutions, to fulfil legitimate commitments undertaken in advance or any other acceptable purposes in accordance with applicable regulations. Under no circumstances shall the purpose of the treasury share transaction be to interfere with the free establishment of prices. In particular, any conduct referred to in article 83.ter.1 of the Securities Market Law and article 2 of the Royal Decree 1333/2005, of 11 November, implementing the Securities Market Law related to matters of market abuse.

The Group's treasury share transactions will not be carried out, under any circumstances, based on insider information.

Treasury shares will be managed providing full transparency as regards relationships with market supervisors and regulatory organisations.

Note 20 of the Consolidated financial statements presents the movements of IBERDROLA's shares in the Group companies' portfolios in the last years. Likewise, other information on transactions in 2016 and 2015 is presented in the following table:

Treasury shares	Number of shares	Nominal value (thousands of euros)	Cost of treasury shares (thousands of euros)	Average price (euros)	Total shares	% shareholding
12.31.2014	60,985,277	45,739	334,014	5.48	6,388,483,000	0.95
Acquisitions	162,118,086	121,589	938,283	5.79		
Disposals	(148,483,000)	(111,362)	(827,884)	5.58		
Redemption	(6,984,197)	(5,238)	(38,956)	5.58		
12.31.2015	67,636,166	50,728	405,457	5.99	6,336,870,000	1.07
Acquisitions	247,226,143	185,420	1,450,724	5.87		
Disposals	(157,197,000)	(117,898)	(946,566)	6.02		
Redemption	(6,440,532)	(4,830)	(40,679)	6.32		
12.31.2016	151,224,777	113,420	868,936	5.75	6,362,079,000	2.38

Treasury shares of Scottish Power	Number of shares	Nominal value (thousands of euros)	Cost of treasury shares (thousands of euros)	Average price (euros)	Total shares	% shareholding
12.31.2014	1,996,422	1,497	11,705	5.86	6,388,483,000	0.03
Acquisitions	438,580	329	2,759	6.29		
Scrip	66,375	50	–	–		
Redemption	(862,814)	(647)	(4,301)	4.98		
12.31.2015	1,638,563	1,229	10,163	6.20	6,336,870,000	0.03
Acquisitions	404,154	303	2,464	6.10		
Scrip	56,040	42	–	–		
Redemption	(724,352)	(543)	(3,047)	4.21		
12.31.2016	1,374,405	1,031	9,580	6.97	6,362,079,000	0.02

In 2016 and 2015, treasury shares held by the IBERDROLA Group were below the legal limit established.

Finally, the conditions and time periods of the current mandate of the Board of Directors to acquire or transfer treasury shares are detailed below.

At the General Shareholders' Meeting on 28 March 2014, shareholders expressly agreed to delegate powers to the Board of Directors, with powers of substitution, pursuant to the provisions of the Spanish Corporations Law, to carry out derivative acquisition of shares in Iberdrola, S.A. under the following conditions:

- a) Acquisitions may be made directly by IBERDROLA or indirectly through its subsidiaries. The process excludes any subsidiaries carrying out regulated business pursuant to the provisions of the Electricity Sector Law and the Hydrocarbons Law.
- b) Acquisitions may be made by purchase transactions, swaps or any other form permitted by law.
- c) Acquisitions may be made up to the maximum legal threshold (i.e. 10% of share capital).
- d) Such acquisitions may not be made at a price higher than the market price or lower than the nominal value of the share.

Authorisation was granted for a maximum period of five years since approval of the resolution.

- e) A restricted reserve shall be created in equity in the purchasing company equivalent to the value of the parent's shares under assets. This reserve must be maintained as long as the shares are not disposed of or cancelled in accordance with the Spanish Corporations Law.

Shares acquired under these powers can be transferred or cancelled or used for the compensation systems as provided for in the Spanish Corporations Law. They may also be used to develop programmes that encourage participation in the Company's share capital such as the dividend reinvestment plan, loyalty bonuses and other similar instruments.

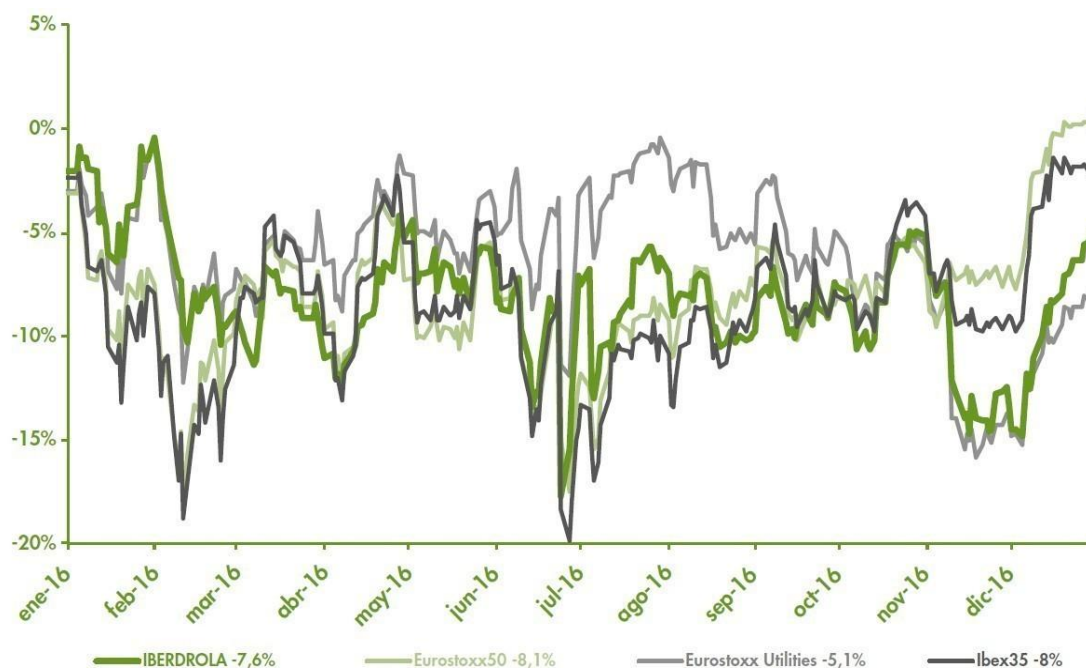
– Stock market data

		2016	2015
Stock market capitalisation (*)	Millions of euros	39,661	41,506
Earnings per share	Euros	0.421	0.381
P.E.R. (share price at year end/profit per share)	Times	14.81	17.19
Price / Carrying amount (capitalisation on carrying amount at year end)	Times	1.08	1.12

(*) 6,362,079,000 shares at 12/31/16 a 6,336,870,000 shares at 12/31/15

– The IBERDROLA share

Stock market performance of IBERDROLA compared to the indexes:



	2016	2015
Number of shares outstanding	6,362,079,000	6,336,870,000
Share price at year end	6.23	6.55
Average share price for the year	6.01	6.12
Average daily volume	25,843,622	31,140,116
Maximum volume (12/16/2016 - 06/26/2015)	117,034,016	90,216,773
Minimum volume (05/16/2016 - 12/24/2015)	4,444,650	4,571,334
Dividends paid (euros)	0.286	0.276
- Gross interim dividend (01/29/2016 - 12/19/2014) (1)	0.127	0.127
- Gross complementary dividend (07/08 y 07/22/2016 - 07/03 y 07/22/2015) (2)	0.154	0.144
Attendance bonus	0.005	0.005
Dividend yield (3)	4.59%	4.21%

(1) Purchase price of rights guaranteed by IBERDROLA.

(2) Complementary dividend in cash (07/08/2016 and 07/03/2015 = EUR 0.03 and purchase price of rights guaranteed by IBERDROLA: 07/22/2016 = EUR 0.124 and 07/22/15 = EUR 0.114).

(3) Interim dividend, complementary dividend and attendance bonus for attending the General Shareholders' Meeting/share price at period end.

9. FURTHER RELEVANT INFORMATION

9.1 Environmental issues and sustainability

9.1.1. Environmental issues

IBERDROLA accepts that the environment places constraints on all human activities and is a factor of companies' competitiveness, and it is committed to promoting innovation in this field and also eco-efficiency, to gradually reducing the environmental impact of its activities, facilities, products and services, and striving to ensure that its activities are congruent with future generations' legitimate right to an appropriate environment.

The Group undertakes and promotes this commitment through its policies, IBERDROLA currently has three specific policies in place to manage environmental issues: its environmental policy, its anti-climate change policy and its biodiversity policy, which set forth the principles through which the Company will continue to improve its environmental management.

Moreover, for the thirteenth consecutive year IBERDROLA featured on the global Dow Jones Sustainability Index, a worldwide benchmark for recognising corporate contributions to sustainable development, and also on other internationally renowned sustainability indexes. It is the only utility to have earned this distinction since the Index was created in 1999.

9.1.2. Sustainability

IBERDROLA's contribution to sustainable development takes form in certain social responsibility practices which address the needs and expectations of their stakeholders, with which the Company maintains a series of lines of communication and dialogue open through which it is able to: communicate objectives, initiatives and achievements obtained in the three areas of sustainable development (economic, environmental and social) and receive evaluations and requests from the interested parties.

Sustainability indicators	2016	2015
Contribution to GDP (Gross Margin) (*)	0.54%	0.55%
Contribution to GDP (Revenue) (*)	1.23%	1.39%
Net profit (millions of euros)	2,705	2,422
CO ₂ Emissions in the period (gr. CO ₂ /kWh): Total	176	225
CO ₂ Emissions in the period (gr. CO ₂ /kWh): Spain	84	103
CO ₂ Emissions in the period (gr. CO ₂ /kWh): SPW	328	530
CO ₂ Emissions in the period (gr. CO ₂ /kWh): Avangrid	58	64
Total production free of emissions (GWh)	78,413	67,868
Production in Spain free of emissions (GWh)	58,400	46,658
Production free of emissions out of total production (%)	57%	52%
Production in Spain free of emissions out of total production (%)	87%	86%
Total installed capacity free of emissions (MW)	29,826	27,744
Total installed capacity in Spain free of emissions (MW)	19,229	18,741
Total installed capacity free of emissions (%)	66%	62%
Total installed capacity in Spain free of emissions (%)	74%	73%
Specific SO ₂ emission Global mix (g/kWh)	0.052	0.108
Specific particles emission Global mix (g/kWh)	0.005	0.007
Specific NO _x emission Global mix (g/kWh)	0.19	0.25

9.2 IBERDROLA Foundation

In 2016, the Group allocated EUR 11,645 thousand to financing the various foundations (EUR 18,985 thousand to Group foundations and EUR 6,584 thousand to associations and entities whose goals are in the interest of the general public).

The main recipient of the funding was Iberdrola Foundation, which received EUR 7,825 thousand. Information on its goals and activities is available at: www.fundacioniberdrola.org. IBERDROLA Foundation is a private, non-profit, cultural foundation, founded by the Company. Its mission is to develop initiatives which effectively contribute to improving the quality of life of the people in the regions and countries where the Group acts, especially in the areas of energy sustainability, art and culture, as well as solidarity and social initiatives. The foundation may act independently to achieve its goals and is fully functional and autonomous. Without prejudice to its collaboration with other entities, Iberdrola Foundation coordinates and executes the Group's corporate social responsibility strategy, so that it is in line with the purpose for which it was created and as assigned there to by the Board of Directors.

Iberdrola Foundation coordinates its welfare work in the United Kingdom through the Scottish Power Foundation, which was granted EUR 1,765 thousand. In the United States, this work is carried out through the Avangrid Foundation with a budget of EUR 2,269 thousand, and in Brazil through the Instituto Iberdrola Brasil, receiving EUR 542 thousand.

In 2016, the Group intends to follow a policy aimed at financing activities of interest to the general public in line with that followed in 2016 as regards amount and allocation.

**ANNUAL CORPORATE GOVERNANCE REPORT
OF LISTED COMPANIES**

Data identifying issuer

Ending date of reference financial year	31/12/2016
Tax Identification Code	A-48010615
Registered name	IBERDROLA, S.A.
Registered address	Plaza Euskadi número 5, Bilbao 48009 Bizkaia España

A. OWNERSHIP STRUCTURE

A.1. Complete the following table about the share capital of the company:

Date of last change	Share capital (€)	Number of shares	Number of voting rights
22/07/2016	4,771,559,250	6,362,079,000	6,362,079,000

State whether there are different classes of shares with different rights attaching thereto:

Yes ☐ No ☒

Class	Number of shares	Nominal value per share	Number of voting rights per share	Different rights

A.2. Breakdown of direct and indirect holders of significant shareholdings in the company as of the end of the financial year, excluding directors:

Individual or company name of the shareholder	Number of direct voting rights	Indirect voting rights		% of total voting rights
		Direct holder of the interest	Number of voting rights	
QATAR INVESTMENT AUTHORITY	-	QATAR HOLDING LUXEMBOURG II, S.À.R.L.	541,378,280	8.51
NORGES BANK	203,362,094	-	-	3.20
BLACKROCK, INC.	-	BLACKROCK GROUP	191,563,600	3.01
KUTXABANK, S.A.	-	KARTERA 1, S.L.	191,034,187	3.00

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

Individual or company name of the shareholder	Date of transaction	Description of transaction
NORGES BANK	24/03/2016	Decrease to below 3% of share capital
NORGES BANK	06/04/2016	Increase to above 3% of share capital

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

Individual or company name of the director	Number of direct voting rights	Indirect voting rights		% of total voting rights
		Direct holder of the interest	Number of voting rights	
MR JOSÉ IGNACIO SÁNCHEZ GALÁN	4,696,445	-	-	0.13
	-	ROYAL PARK 2000, S.L.	3,410,678	
MR IÑIGO VÍCTOR DE ORIOL IBARRA	1,225,083	-	-	0.02
MS INÉS MACHO STADLER	61,801	-	-	0.00
MR BRAULIO MEDEL CÁMARA	27,828	-	-	0.00
MS SAMANTHA BARBER	1,772	-	-	0.00
MS MARÍA HELENA ANTOLÍN RAYBAUD	3,112	-	-	0.00
MR SANTIAGO MARTÍNEZ LAGE	16,264	-	-	0.00
MR JOSÉ LUIS SAN PEDRO GUERENABARRENA	782,432	-	-	0.01
MR ÁNGEL JESÚS ACEBES PANIAGUA	6,112	-	-	0.00
MS GEORGINA KESSEL MARTÍNEZ	2,141	-	-	0.00
MS DENISE MARY HOLT	219	-	-	0.00
MR JOSÉ WALFREDO FERNÁNDEZ	0	-	-	0.00
MR MANUEL MOREU MUNAIZ	22,708	-	-	0.00
	-	MS MARÍA GAMAZO TRUEBA	22,708	
MR XABIER SAGREDO ORMAZA	0	-	-	0.00
Total percentage of voting rights held by the board of directors				0.16

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

Individual or company name of the director	Number of direct rights	Indirect rights		Number of equivalent shares	% of total voting rights
		Direct holder	Number of voting rights		

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

Related individual or company name	Type of relationship	Brief description

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

Related individual or company name	Type of relationship	Brief description
KUTXABANK, S.A.	Corporate	<p>1) Iberdrola and Kutxabank, S.A. both hold interests in Operador del Mercado Ibérico de Energía-Polo Español, S.A. (5.5% and 0.84%, respectively).</p> <p>2) Iberdrola and Kutxabank, S.A. both hold interests in Seed Capital de Bizkaia, SGEIC, S.A. (5% and 10%, respectively).</p> <p>3) Iberdrola and Kutxabank, S.A. both hold interests in Torre Iberdrola, A.I.E. (68.1% and 31.9%, respectively).</p> <p>4) Iberdrola and Kutxabank, S.A. both hold interests in Sociedad Bilbao Gas Hub, S.A. (1.95% and 7.41%, respectively).</p> <p>5) Iberdrola and Kutxabank, S.A. both hold interests in Sociedad de Gestión de Activos Procedentes de la Reestructuración Bancaria, S.A. (0.2% and 2.5%, respectively).</p>

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

Yes ☐ No ☒

Participants in the private shareholders' agreement	% of share capital affected	Brief description of the agreement

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

Yes ☐ No ☒

Participants in concerted action	% of share capital affected	Brief description of the concerted action

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

Not applicable.

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

Yes ☐ No ☒

Individual or company name

Comments

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

As of year-end:

Number of direct shares	Number of indirect shares (*)	Total % of share capital
151,224,777	0	2.37

(*) Through:

Individual or company name of direct holder of the interest	Number of direct shares
Total:	

Explain any significant changes, pursuant to the provisions of Royal Decree 1362/2007, that have occurred during the financial year:

Explain any significant changes
<p>The Company sent to the CNMV three updates to its treasury share position in 2016 as a result of a change in the number of voting rights arising from corporate transactions:</p> <ul style="list-style-type: none"> - notices of direct acquisitions of a total of 41,537,228 shares (0.649%) were provided on 4 February, coinciding with the increase in capital resulting from the "Iberdrola Flexible Dividend" programme. - notices of direct acquisitions of a total of 58,297,884 shares (0.934%) were provided on 9 May, coinciding with the reduction in capital; and - notices of direct acquisitions of a total of 14,141,497 shares (0.222%) were provided on 29 July, coinciding with the increase in capital resulting from the "Iberdrola Flexible Dividend" programme. <p>During financial year 2016 and the elapsed part of 2017, the Company provided three additional notices arising from consecutive direct acquisitions of own shares due to said acquisitions exceeding 1% of voting rights since the preceding notice:</p> <ul style="list-style-type: none"> - notices of direct acquisitions of a total of 56,603,780 shares (0.893%) were provided on 4 January 2016. - notices of direct acquisitions of a total of 63,677,004 shares (1.001%) were provided on 21 November 2016; and - notices of direct acquisitions of a total of 69,572,560 shares (1.094%) were provided on 4 January 2017.

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

<p>The shareholders acting at the General Shareholders' Meeting held on 28 March 2014 resolved to expressly authorise the Board of Directors, with the power of substitution, pursuant to the Companies Act (<i>Ley de Sociedades de Capital</i>), to carry out the derivative acquisition of the shares of Iberdrola on the following terms:</p> <ol style="list-style-type: none"> Purchases may be made by Iberdrola directly, or indirectly through its subsidiaries. Subsidiaries carrying out regulated activities are excluded pursuant to the provisions of the Electricity Industry Act (<i>Ley del Sector Eléctrico</i>) and the Hydrocarbons Act (<i>Ley de Hidrocarburos</i>). Purchases shall be made by means of a purchase and sale agreement, a swap arrangement, or any other transaction permitted by law. Purchases may be made up to the maximum sum permitted by law (i.e. 10% of the share capital). Purchases may not be made at a higher price than that quoted on the Stock Exchange or at a price lower than the share's nominal value. The authorisation was granted for a period not to exceed five years as from the approval of the resolution. The acquiring company shall establish a restricted reserve in shareholders' equity equal to the amount of the shares of the controlling company recorded under assets. Such reserve shall be maintained for so long as the shares are not transferred or retired, in compliance with the provisions of the Companies Act. <p>The shares, if any, purchased as a result of the aforementioned authorisation could be used for either transfer or retirement or could be applied to the remuneration systems provided for in the Companies Act; added to the foregoing alternatives was the possible development of programmes fostering the acquisition of interests in the Company such as, for example, dividend reinvestment plans, loyalty bonds, or similar instruments.</p>
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A.9.bis Estimated free-float:

	%
Estimated free-float:	85.92

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

Yes ☒ No ☐

Description of restrictions
<p>Those having an interest equal to or greater than 3% of the capital or voting rights of two or more companies that have the status of Principal Operator in certain markets or sectors (including the generation and supply of electricity) may not exercise rights in excess of such percentage in more than one entity.</p> <p>Article 29.2 of the By-Laws provides that no shareholder may cast a number of votes greater than those corresponding to shares representing 10% of the share capital.</p> <p>According to article 28, a shareholder may not exercise their right to vote at the General Shareholders' Meeting if it deals with a resolution intended to: (a) relieve the shareholder of an obligation or grant the shareholder a right; (b) provide the shareholder with any kind of financial assistance, including the provision of guarantees in favour thereof; (c) release the shareholder, if a director, from obligations arising from the duty of loyalty as provided by law.</p> <p>Article 50 of the By-Laws provides that the by-law restrictions against the exercise of voting rights by shareholders affected by conflicts established in article 28 above and the limitation on the maximum number of votes that may be cast by a single shareholder contained in sections 2 and 4 of article 29 above shall be deprived of effect upon the occurrence of certain circumstances in the case of a takeover bid.</p> <p>Furthermore, section 527 of the restated text of the Companies Act provides that at listed companies (sociedades anónimas cotizadas), the by-law provisions that directly or indirectly set, as a general rule, the maximum number of votes that may be cast by the same shareholder, by the companies belonging to the same group, or by those acting in concert with the foregoing shall be of no effect when, following a takeover bid, the bidder has reached a percentage that is equal to or greater than 70% of the voting share capital, unless such bidder is not subject to equivalent breakthrough measures or has not adopted them.</p> <p>Pursuant to U.S. law, due to the business carried out by Avangrid, Inc. (a company belonging to the Iberdrola Group) in that country, the acquisition of an interest giving rise to the holding of 10% or more of the share capital of Iberdrola will be subject to the prior approval of certain U.S. regulatory authorities.</p>

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

Yes ☐ No ☒

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

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

Yes ☐ No ☒

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

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B. GENERAL SHAREHOLDERS' MEETING

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

Yes ☒ No ☐

	Quorum % different from that established in section 193 of the Companies Act generally	Quorum % different from that established in section 194 of the Companies Act for the special circumstances described in section 194.
Required quorum upon 1 st call	-	66.67
Required quorum upon 2 nd call	-	60.00

Description of differences
As the only exception to the rules provided for in the Companies Act, article 21.2 of the By-Laws increases the quorum required to hold a valid meeting "in order to adopt resolutions regarding a change in the object of the Company, transformation, total split-off, dissolution of the Company, and the amendment of this section 2", in which case "shareholders representing two-thirds (2/3) of subscribed share capital with voting rights must be in attendance at the first call to the General Shareholders' Meeting, and shareholders representing sixty (60%) per cent of such share capital must be in attendance at the second call".

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

Yes ☒ No ☐

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

	Qualified majority other than that established in section 201.2 of the Companies Act for the cases set forth in section 194.1 of the Companies Act	Other instances in which a qualified majority is required
% established by the entity for the adoption of resolutions	75.00%	75.00%

Describe the differences
Article 52 of the By-Laws provides that all resolutions intended to eliminate or amend the provisions contained in title IV (breakthrough of restrictions in the event of takeover bids), in article 28 (conflicts of interest), and in sections 2 to 4 of article 29 (limitation upon the maximum number of votes that a shareholder may cast), shall require the affirmative vote of three-fourths (3/4) of the share capital present in person or by proxy at a General Shareholders' Meeting.

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

In addition to the provisions of section 285 *et seq.* of the Companies Act, the *By-Laws* of Iberdrola contain articles 21.2 (qualified quorum) and 52 (qualified majority) mentioned in sections B.1 and B.2 above.

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

Attendance data					
Date of general shareholders meeting	% of shareholders present in person	% of shareholders represented by proxy	% absentee voting		Total
			Electronic voting	Other	
27/03/2015	21.45	57.04	0.11	0.05	78.65
08/04/2016	8.00	69.68	0.19	0.04	77.91

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

Yes ☐ No ☒

Number of shares required to attend the general shareholders' meeting	
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- B.6. Section deleted.**

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

www.iberdrola.com > Corporate Governance.

Information regarding past general shareholders' meetings of the Company can be accessed at the same address: www.iberdrola.com > Corporate Governance > General Shareholders' Meeting.

C. STRUCTURE OF THE COMPANY'S MANAGEMENT

C.1. Board of directors

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

Maximum number of directors	14
Minimum number of directors	9

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

Individual or company name of the director	Representative	Type of director	Position on the board	Date of first appointment	Date of last appointment	Election procedure
MR JOSÉ IGNACIO SÁNCHEZ GALÁN	-	EXECUTIVE	CHAIRMAN/CEO	21/05/2001	27/03/2015	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MR IÑIGO VÍCTOR DE ORIOL IBARRA	-	OTHER EXTERNAL	DIRECTOR	26/04/2006	08/04/2016	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MS INÉS MACHO STADLER	-	INDEPENDENT	DIRECTOR	07/06/2006	08/04/2016	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MR BRAULIO MEDEL CÁMARA	-	INDEPENDENT	DIRECTOR	07/06/2006	08/04/2016	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MS SAMANTHA BARBER	-	INDEPENDENT	DIRECTOR	31/07/2008	08/04/2016	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MS MARÍA HELENA ANTOLÍN RAYBAUD	-	INDEPENDENT	DIRECTOR	26/03/2010	27/03/2015	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MR SANTIAGO MARTÍNEZ LAGE	-	INDEPENDENT	DIRECTOR	26/03/2010	27/03/2015	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MR JOSÉ LUIS SAN PEDRO GUERENABARRENA	-	OTHER EXTERNAL	DIRECTOR	24/04/2012	27/03/2015	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MR ÁNGEL JESÚS ACEBES PANIAGUA	-	INDEPENDENT	DIRECTOR	24/04/2012	27/03/2015	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MS GEORGINA KESSEL MARTÍNEZ	-	INDEPENDENT	DIRECTOR	23/04/2013	28/03/2014	GENERAL SHAREHOLDERS' MEETING RESOLUTION

MS DENISE MARY HOLT	-	INDEPENDENT	DIRECTOR	24/06/2014	27/03/2015	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MR JOSÉ WALFREDO FERNÁNDEZ	-	INDEPENDENT	DIRECTOR	17/02/2015	27/03/2015	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MR MANUEL MOREU MUNAIZ	-	INDEPENDENT	DIRECTOR	17/02/2015	27/03/2015	GENERAL SHAREHOLDERS' MEETING RESOLUTION
MR XABIER SAGREDO ORMAZA	-	OTHER EXTERNAL	DIRECTOR	08/04/2016	08/04/2016	GENERAL SHAREHOLDERS' MEETING RESOLUTION

Total number of directors	14
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State the vacancies on the board of directors during the reporting period:

Individual or company name of director	Class of director at time of vacancy	Date of vacancy
MR XABIER DE IRLA ESTÉVEZ	Proprietary director	08/04/2016

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

EXECUTIVE DIRECTORS

Individual or company name of director	Position within the company's structure
MR JOSÉ IGNACIO SÁNCHEZ GALÁN	Chairman & CEO

Total number of executive directors	1
Total % of the board	7.14

EXTERNAL PROPRIETARY DIRECTORS

Individual or company name of director	Individual or company name of the significant shareholder represented by the director or that has proposed the director's appointment

Total number of proprietary directors	0
Total % of the board	

EXTERNAL INDEPENDENT DIRECTORS

Individual or company name of director	Profile
MS INÉS MACHO STADLER	<p>Bilbao, 1959</p> <p>Professional profile and biographical data</p> <p>Other activities: professor of Economics in the Economics and Economic History Department of Universidad Autónoma de Barcelona, professor of the Barcelona Graduate School of Economics, member of the Council of the French Economic Observatory (<i>Observatoire Français des Conjonctures Économiques</i>) (OFCE), and honorary member of the European Economic Association and of the Spanish Economic Association (<i>Asociación Española de Economía</i>).</p> <p>Dates of appointment and re-election as director of Iberdrola, S.A.: 7 June 2006, 29 March 2007, 22 June 2012, and 8 April 2016.</p> <p>Academic training</p> <p>Degree in Economics from Universidad del País Vasco, Master in Economics from l'École des Hautes Études en Sciences Sociales, and Doctor in Economics (Ph.D.) from the same academic institution and from l'École Nationale de la Statistique et de l'Administration Économique (ENSAE) (Paris, France).</p> <p>Noteworthy experience in the energy and industrial engineering sector</p> <p>She has been a member of the International Scientific Advisory Committee of the Basque Centre for Climate Change (bc3) and has served as chair of the Scientific Committee of the 2011 Conference of the Spanish Association for Energy Economics (<i>Asociación Española para la Economía Energética</i>).</p> <p>Noteworthy experience in other industries</p> <p>She has been president of the Spanish Economic Association, coordinator of the National Agency for Quality Evaluation and Accreditation (<i>Agencia Nacional de Evaluación y Prospectiva</i>), and representative at the European Science Foundation, as well as a member-elect of the Council of the European Economic Association and a member of the Executive Committee of the European Association for Research in Industrial Economics. She has been a member of the Advisory Board of the Research Service of Caja de Ahorros y Pensiones de Barcelona, "la Caixa".</p> <p>She has taught at universities in Germany, Belgium, Brazil, Denmark, France, Portugal, and Spain.</p>
MR BRAULIO MEDEL CÁMARA	<p>Marchena, Seville, 1947</p> <p>Professional profile and biographical data</p> <p>Other activities: chair of Fundación Bancaria Unicaja, Hidralia, S.A., and Federación de Cajas de Ahorros de Andalucía, vice-chair of Confederación Española de Cajas de Ahorros (CECA), and a member of the board of directors of the listed company Acerinox, S.A. and of Caja de Seguros Reunidos, Compañía de Seguros y Reaseguros, S.A. and Professor of Public Finance at Universidad de Málaga.</p> <p>Dates of appointment and re-election as director of Iberdrola, S.A.: 7 June 2006, 29 March 2007, 22 June 2012, and 8 April 2016.</p>

	<p>Academic training</p> <p>Degree in Economics and Business Administration from Universidad Complutense de Madrid and Doctorate in Economics and Business Administration from Universidad de Málaga.</p> <p>Noteworthy experience in the energy and industrial engineering sector</p> <p>He has been a member of the board of Compañía Sevillana de Electricidad, S.A., Retevisión and of Abertis Infraestructuras, S.A.</p> <p>Noteworthy experience in other industries</p> <p>He has been executive chair of Unicaja Banco, S.A., chair of Ahorro Corporación, S.A. and of CECA, and a member of the board of Centros Comerciales Carrefour, S.A., and has been a member of the governance bodies of the World Savings and Retail Banking Institute and of the European Savings and Retail Banking Group, of which he was vice-chair.</p> <p>He has also served as Deputy Minister for Economy and Finance of the Autonomous Government of Andalusia and as chair of Consejo Andaluz de Colegios de Economistas. He has also been a member of the board of trustees of the following foundations: Tres Culturas del Mediterráneo, El Legado Andalusi, Doñana 21 and CIEDES (<i>Centro de Investigaciones Estratégicas y Desarrollo Económico y Social</i>).</p>
MS SAMANTHA BARBER	<p>Dunfermline, Fife, Scotland, 1969</p> <p>Professional profile and biographical data</p> <p>Other activities: chair of Scottish Ensemble, vice-chair of Scotland's 2020 Climate Group, member of the Advisory Board for Breakthrough Breast Cancer, of the GlobalScot network, and of the Advisory Board for the Imperial College London MBA, and performs advisory and business coaching work.</p> <p>Dates of appointment and re-election as director of Iberdrola, S.A.: 31 July 2008, 20 March 2009, 22 June 2012, and 8 April 2016.</p> <p>Academic training</p> <p>Bachelor of Arts in Applied Foreign Languages and European Politics from the University of Northumbria, Newcastle (England, United Kingdom) and Post-Graduate degree in EU Law from the University of Nancy (France).</p> <p>Noteworthy experience in the energy and industrial engineering sector</p> <p>She has been a member of the Advisory Council of Scottish Power following the integration of the Scottish company into the Iberdrola Group.</p> <p>Noteworthy experience in other industries</p> <p>She has been a consultant within the European Parliament, where she provided support to the Economic and Monetary Affairs Committee, a board member of Business for Scotland, and the chief executive of Scottish Business in the Community.</p> <p>She has also been a member of the Board of Directors of Right Track Scotland, an organisation dedicated to advancing educational, training, and employment opportunities for youths at risk of social exclusion.</p> <p>She was chosen as one of the "Top 100 Women to Watch" according to the FTSE list and Cranfield University, and was a finalist and earned second place in the annual Director of the Year Awards 2012 of IoD Scotland NED.</p>
MS MARÍA HELENA ANTOLÍN RAYBAUD	<p>Toulon, France, 1966</p> <p>Professional profile and biographical data</p> <p>Other activities: vice-chair of the Board of Directors and member of the Management Committee of Grupo Antolín Irausa, S.A., President of the Spanish Association of Automotive Equipment and Component</p>

	<p>Manufacturers (<i>Asociación Española de Fabricantes de Equipos y Componentes para Automoción</i>) (Sernauto), vice president of Excellence in Management Club (<i>Club de Excelencia en la Gestión</i>), and a board member of France Foreign Trade (<i>Comercio Exterior de Francia</i>), Spain section.</p> <p>Dates of appointment and re-election as director of Iberdrola, S.A.: 26 March 2010 and 27 March 2015.</p> <p>Academic training</p> <p>Degree in International Business and Business Administration from Eckerd College, St. Petersburg, Florida (United States of America), and Master in Business Administration from Anglia University, Cambridge (United Kingdom) and from Escuela Politécnica de Valencia (Spain).</p> <p>Noteworthy experience in the energy and industrial engineering sector</p> <p>She has served as an external independent director of Iberdrola Renovables, S.A. and a member of its Related-Party Transactions Committee.</p> <p>She has been in charge of the corporate Industrial and Strategy Divisions of Grupo Antolín Irausa, S.A., where she has also been a director of Human Resources and the head of Total Quality for the Group.</p>
MR SANTIAGO MARTÍNEZ LAGE	<p>Betanzos, A Coruña, 1946</p> <p>Professional profile and biographical data</p> <p>Other activities: chair of the law firm Martínez Lage, Allendesalazar & Brokelmann, secretary of the board of directors of SKF Española, S.A., vice-chair of the Spanish Association for the Study of European Law (<i>Asociación Española para el Estudio del Derecho Europeo</i>) and the European Law Section of the Royal Academy of Jurisprudence and Legislation (<i>Real Academia de Jurisprudencia y Legislación</i>), a trustee of Fundación España México, and a member of the Arbitrator Appointment Committee of the Spanish Court of Arbitration.</p> <p>Dates of appointment and re-election as director of Iberdrola, S.A.: 26 March 2010 and 27 March 2015.</p> <p>Academic training</p> <p>Degree in Law from Universidad Complutense de Madrid. He continued his studies at the Escuela de Funcionarios Internacionales de Madrid, the Escuela Diplomática, The Hague Academy of International Law, the "Europa Instituut" in Amsterdam (The Netherlands), and the INSEAD in Fontainebleau (France). Career diplomat on leave.</p> <p>Noteworthy experience in the energy and industrial engineering sector</p> <p>He has served as an external independent director of Iberdrola Renovables, S.A. and chair of its Appointments and Remuneration Committee, and secretary of the boards of directors of Fujitsu Services, S.A. and Telettra España, S.A.</p> <p>He has also been a member of the Appointments and Remuneration Committee and of the Audit and Risk Supervision Committee of Iberdrola, S.A.</p> <p>Noteworthy experience in other industries</p> <p>He has been secretary of the Board of Directors of Empresa Nacional Elcano de la Marina Mercante, S.A. and founder and director of the Gaceta Jurídica de la Unión Europea y de la Competencia.</p> <p>He has also been general secretary of the International Federation for European Law (<i>Fédération Internationale pour le Droit Européen</i>) (FIDE) and member of the managing committee of Círculo de Empresarios.</p> <p>As a diplomat, he was posted to Algiers (Algeria), Libreville (Gabon), Sofia (Bulgaria), and Paris (France), and has also served at the Office of the</p>

	Secretary of State for Relations with the European Community.
MR ÁNGEL JESÚS ACEBES PANIAGUA	<p>Ávila, 1958</p> <p>Professional profile and biographical data</p> <p>Other activities: chairman and founding partner of Grupo MA Abogados Estudio Jurídico, S.L., sole director and professional partner of Doble A Estudios y Análisis, S.L.P., member of the Advisory Board of Wolters Kluwer España, and a trustee of Fundación para el Análisis y Estudios Sociales (FAES) and of Fundación Universitaria de Ávila, UCAV. He gives courses, workshops, and lectures on various matters relating to law, politics, and social matters.</p> <p>Dates of appointment and re-election as director of Iberdrola, S.A.: 24 April 2012 and 27 March 2015.</p> <p>Academic training</p> <p>Degree in Law from Universidad de Salamanca.</p> <p>Noteworthy experience in the energy and industrial engineering sector</p> <p>As a lawyer, he has advised companies in the energy and technological/industrial sectors, among others. He also has significant knowledge of the regulatory area due to his work as a member of the Council of Ministers of the Government of Spain, a senator, and a national deputy.</p> <p>Noteworthy experience in other industries</p> <p>He has served on the board of Caja Madrid Cibeles, S.A., which manages the investments of Grupo Caja Madrid in other companies with activities in the financial and insurance sectors (like Mapfre Internacional, S.A.) as well as the retail banking sector outside of Spain. After the public listing of Bankia, S.A., he was a member of the board of Banco Financiero y de Ahorros, S.A. ("BFA"), chairing its Audit and Compliance Committee.</p> <p>In the institutional arena, he has been Minister for Public Administrations, Minister of Justice, and Minister of the Interior of the Spanish Government.</p>
MS GEORGINA KESSEL MARTÍNEZ	<p>Mexico, 1950</p> <p>Professional profile and biographical data</p> <p>Other activities: independent director and chair of the Audit Committee of Grupo Financiero Scotiabank Inverlat, and a partner of Spectron E&I.</p> <p>Dates of appointment and re-election as director of Iberdrola, S.A.: 23 April 2013 and 28 March 2014.</p> <p>Academic training</p> <p>Holder of a degree in Economics from Instituto Autónomo de México and of a Master's and Doctor's degree in Economics from Columbia University (New York).</p> <p>Noteworthy experience in the energy and industrial engineering sector</p> <p>She has been chair of the Energy Regulatory Commission (<i>Comisión Reguladora de Energía</i>) and Energy Secretary of the Government of Mexico.</p> <p>She has also been chair of the Board of Directors of Pemex (Petróleos Mexicanos) and of the Board of Directors of the Federal Electricity Commission (<i>Comisión Federal de Electricidad</i>) (CFE).</p> <p>She has participated in the Energy Council of the World Economic Forum and in the United Nations Organization Secretary General's advisory group (Sustainable Energy for All).</p> <p>Noteworthy experience in other industries</p> <p>She has been an adviser to the chair of the Federal Competition Commission</p>

	<p>(<i>Comisión Federal de Competencia</i>), head of the Quasi-Autonomous Non-Governmental Organisations Investment and Divestment Unit (<i>Unidad de Inversiones y Desincorporación de Entidades Paraestatales</i>) of the Office of the Secretary of Finance and Public Credit of Mexico, general manager of the National Mint of Mexico (<i>Casa de Moneda de México</i>), member of the boards of Nacional Financiera (Nafinsa) and of Banco Nacional de Comercio Exterior (Bancomext), and general manager of Banco Nacional de Obras y Servicios Públicos.</p> <p>In the academic field, she has been a professor in the Economics Department of Instituto Tecnológico Autónomo de México, deputy chair of the course towards a Degree in Economics, and chair of the Alumni Association. She was also holder of the Quintana Chair for Research in International Trade and is the author of many papers and specialised articles.</p>
MS DENISE MARY HOLT	<p>Vienna, Austria, 1949</p> <p>Professional profile and biographical data</p> <p>Other activities: independent director and member of the Risk Committee of HSBC Bank plc., chair and independent director of M&S Financial Services Ltd., independent director and member of the Quality and Safety and Compensation Committees of the Board of Directors of Nuffield Health, member of the governing board of the University of Bristol, and chair of the Appointments Committee of the British Alzheimer's Society.</p> <p>Dates of appointment and re-election as director of Iberdrola, S.A.: 24 June 2014 and 27 March 2015.</p> <p>Academic training</p> <p>Degrees in Spanish Philology, French Philology, and Political Sciences from the University of Bristol and Doctor of Laws from the same university (England, United Kingdom).</p> <p>Noteworthy experience in the energy and industrial engineering sector</p> <p>She has been a director of Scottish Power Renewable Energy Ltd. and of Scottish Power Energy Networks Holdings Ltd.</p> <p>Noteworthy experience in other industries</p> <p>In her diplomatic career, she has been first secretary of the Embassy of the United Kingdom in Brazil, director of Human Resources, of Migration and of the Overseas Territories at the UK Foreign and Commonwealth Office, and ambassador of the United Kingdom to Mexico, Spain, and Andorra. For her contribution to the British diplomatic service, she was elevated to Dame Commander of the Order of St Michael and St George (DCMG).</p> <p>She has also served as chair of the Anglo-Spanish Society and of the Institute of Latin American Studies at the University of London.</p>
MR JOSÉ WALFREDO FERNÁNDEZ	<p>Cienfuegos, Cuba, 1955</p> <p>Professional profile and biographical data</p> <p>Other activities: partner of Gibson, Dunn & Crutcher, member of the board of directors of the Council of the Americas and the Center for American Progress.</p> <p>Dates of appointment and re-election as director of Iberdrola, S.A.: 17 February 2015 and 27 March 2015.</p> <p>Academic training</p> <p>Degree in History from Dartmouth College (New Hampshire, United States of America), and Juris Doctor from Columbia University (New York, United States of America).</p> <p>Noteworthy experience in the energy and industrial engineering sector</p>

	<p>He has been Assistant Secretary of State for Economic, Energy and Business Affairs for the United States of America.</p> <p>He has also been an independent director of Iberdrola USA, Inc.</p> <p>Noteworthy experience in other industries</p> <p>He has served on the boards of Dartmouth College, NPR Station WBGO-FM, the Middle East Institute, and Ballet Hispanico of New York and of non-governmental institutions such as Acción Internacional. He has also been the State Department's representative on the Committee on Foreign Investment in the United States.</p> <p>In addition, he was named one of the "World's Leading Lawyers" by Chambers Global for his M&A work, an "Expert" by the International Financial Law Review, one of the "World's Leading Privatization Lawyers" by Euromoney, and "Embajador de la Marca España" (Ambassador of the Spain Brand).</p>
MR MANUEL MOREU MUNAIZ	<p>Pontevedra, 1953</p> <p>Professional profile and biographical data</p> <p>Other activities: president of Seaplace, S.L., sole director of H.I. de Iberia Ingeniería y Proyectos, S.L. and of Howard Ingeniería y Desarrollo, S.L., director of Tubacex, S.A., member of the Spanish Committee of Lloyd's Register EMEA, and professor at Universidad Politécnica de Madrid – ETSIN, Repsol's Master's program in oil and the Maritime Master's program of Instituto Marítimo Español and Universidad Pontificia Comillas.</p> <p>Dates of appointment and re-election as director of Iberdrola, S.A.: 17 February 2015 and 27 March 2015.</p> <p>Academic training</p> <p>Doctorate in naval engineering from Escuela Técnica Superior de Ingenieros Navales (ETSIN) of the Universidad Politécnica de Madrid, and Master's degree in Oceanic Engineering from the Massachusetts Institute of Technology (MIT).</p> <p>Noteworthy experience in the energy and industrial engineering sector</p> <p>He has been a member of the Board of Directors of Iberdrola Renovables, S.A., and a board member and member of the Audit and Compliance Committee of Gamesa Corporación Tecnológica, S.A.</p> <p>Noteworthy experience in other industries</p> <p>He has been a member of the board of Metalships and Docks, S.A., Neumáticas de Vigo, S.A. and Rodman Polyships, S.A., dean of the Colegio Oficial de Ingenieros Navales y Oceánicos de Madrid y de España, president of the Instituto de Ingeniería de España, and professor of the Repsol Master's program in oil.</p>

Total number of independent directors	10
Total % of the board	71.43

State whether any director classified as independent receives from the company or its group any amount or benefit for items other than director remuneration, or maintains or has maintained during the last financial year a business relationship with the company or with any company of its group, whether in the director's own name or as a significant shareholder, director, or senior officer of an entity that maintains or has maintained such relationship. If applicable, include a reasoned statement of the director regarding the reasons for which it is believed that such director can carry out the duties thereof as an independent director.

Not applicable.

OTHER EXTERNAL DIRECTORS

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

Individual or company name of director	Reasons	Company, officer, or shareholder with which the director has ties
MR IÑIGO VÍCTOR DE ORIOL IBARRA	A company tied to the director billed the Iberdrola Group for services during financial year 2016. The related-party transaction was fully reported in the Annual Corporate Governance Report for financial year 2015.	IBERDROLA
MR JOSÉ LUIS SAN PEDRO GUERENABARRENA	Mr San Pedro Guerenabarrena held the position of chief operating officer (<i>consejero-director general</i>) until 24 June 2014, the date on which he voluntarily ceased executive duties, but continues to serve as a member of the Board of Directors and of the Executive Committee.	IBERDROLA
MR XABIER SAGREDO ORMAZA	He is chair of the Board of Trustees of Bilbao Bizkaia Kutxa Fundación Bancaria, the principal shareholder of Kutxabank, S.A.	KUTXABANK

Total number of other external directors	3
Total % of the board	21.43

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

Individual or company name of director	Date of change	Former class	Current class
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MR MANUEL MOREU MUNAIZ	20/12/2016	Other external	Independent
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C.1.4. Complete the following table with information regarding the number of female directors for the last 4 financial years, as well as the status of such directors:

	Number of female directors				% of total directors of each class			
	Year t	Year t-1	Year t-2	Year t-3	Year t	Year t-1	Year t-2	Year t-3
Executive	-	-	-	-	-	-	-	-
Proprietary	-	-	-	-	-	-	-	-
Independent	5	5	5	4	55.55	55.55	55.55	40
Other external	-	-	-	-	-	-	-	-
Total	5	5	5	4	35.71	35.71	35.71	28.57

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

Explanation of measures
<p>The Company's Corporate Governance System, and particularly the Director Candidate Selection Policy, entrusts the Appointments Committee with the duty to ensure that when new vacancies are filled or new directors are appointed, the selection procedures are free from any implied bias entailing any kind of discrimination and, in particular, that such procedures do not hinder the selection of female directors. The goals thereof include ensuring that female directors continue to account for at least 30% of the Board of Directors by 2020.</p> <p>Iberdrola has consistently increased the number of female directors on its Board of Directors since 2006.</p> <p>Five of the fourteen members of the Board of Directors are currently women.</p> <p>On 7 June 2006, the Board of Directors appointed Ms Inés Macho Stadler as independent director on an interim basis to fill a vacancy; such appointment was ratified by the shareholders at the General Shareholders' Meeting held on 29 March 2007, where the shareholders also approved her re-election for a five-year period. On 22 September 2009, Ms Inés Macho Stadler was appointed as lead independent director (consejera coordinadora), a position governed by the provisions of article 45 of the By-Laws and article 21 of the Regulations of the Board of Directors, which position she has continuously held through the date hereof.</p> <p>At its meeting of 31 July 2008, the Board of Directors resolved to appoint Ms Samantha Barber as an independent director on an interim basis to fill a vacancy; such appointment was ratified by the shareholders at the General Shareholders' Meeting held on 20 March 2009. Ms Barber has also chaired the Corporate Social Responsibility Committee since 24 April 2012, replacing Mr. Braulio Medel Cámara.</p> <p>The shareholders at the General Shareholders' Meeting held on 26 March 2010 approved the proposed appointment of Ms María Helena Antolín Raybaud, with the classification of external independent director.</p> <p>On 23 April 2013, Iberdrola's Board of Directors approved the interim appointment of Ms Georgina Kessel Martínez as an external independent director, which appointment was subsequently ratified by the shareholders at the General Shareholders' Meeting held on 28 March 2014. Furthermore, Ms Kessel Martínez was appointed chair of the Audit and Risk Supervision Committee on 17 February 2015, replacing Mr Julio de Miguel Aynat.</p> <p>On 24 June 2014, the Board of Directors approved the interim appointment of Ms Denise Mary Holt as an external independent director. This appointment was ratified by the shareholders at the General</p>

Shareholders' Meeting held on 27 March 2015.

Finally, the Appointments and Remuneration Committee was split into two separate committees on 27 March 2015. The appointment of Ms María Helena Antolín Raybaud and of Ms Inés Macho Stadler as chairs of the Appointments Committee and the Remuneration Committee, respectively, was approved for these purposes.

As a result of the foregoing, all consultative committees of the Board of Directors are chaired by women.

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

Explanation of measures
<p>The Director Candidate Selection Policy ensures that the proposed appointments of directors are based on a prior analysis of the needs of the Board of Directors. In particular, the candidates must be respectable and qualified persons, widely recognised for their expertise, competence, experience, qualifications, training, availability, and commitment to their duties. They must be irreproachable professionals, whose professional conduct and background is aligned with the principles set forth in the Directors' Code of Ethics and the corporate values contained in the Mission, Vision, and Values of the Iberdrola group.</p> <p>In addition, the selection of candidates shall endeavour to ensure that a diverse and balanced composition of the Board of Directors as a whole is achieved, such that decision-making is enriched and multiple viewpoints are contributed to the discussion of the matters within its power. To this end, the selection process shall promote a search for candidates with knowledge and experience in the main countries and sectors in which the Group does or will do business. The directors must also have sufficient knowledge of the Spanish and English languages to be able to perform their duties.</p> <p>In turn, the Board has entrusted to the Appointments Committee the responsibility of ensuring that when new vacancies are filled or new directors are appointed, the selection procedures are free from any implied bias entailing any kind of discrimination and, in particular, from any bias that might hinder the selection of female directors. This is expressly provided by articles 27.6.c) of the Regulations of the Board of Directors and 3.e) of the Regulations of the Appointments Committee.</p>

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

Explanation of reasons
Not applicable.

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

The Director Candidate Selection Policy conforms to the most stringent domestic and international corporate governance practices regarding appointments, seeking diversity of knowledge, experience, origin, nationality, and gender within the Board of Directors. The policy specifies the Company's commitment to eliminate any implicit bias that hinders the selection of female directors, who currently represent more than 35% of the members of the Board of Directors, having already exceeded the commitment set out in the policy stating that the number of female directors would represent at least thirty per cent of all members of the Board of Directors by 2020. Finally, the policy promotes the inclusion within

the Board of Directors of candidates with experience on boards of directors of subsidiaries of the Group, thus contributing their knowledge of the Company's business through such subsidiaries.

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

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

Individual or company name of the shareholder	Reason

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

Yes ☐ No ☒

Individual or company name of the shareholder	Explanation

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

Name of director	Reason for withdrawal
MR XABIER DE IRLA ESTÉVEZ	Personal reasons.

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

Individual or company name of director	Brief description
MR JOSÉ IGNACIO SÁNCHEZ GALÁN	The chairman & chief executive officer, as an individual decision-making body, has all the powers that may be delegated under the law and the <i>By-Laws</i> .

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

Individual or company name of director	Name of entity within the group	Position	Do he/she have executive duties?
MR JOSÉ IGNACIO SÁNCHEZ GALÁN	SCOTTISH POWER, LTD.	Chairman	NO
MR JOSÉ IGNACIO SÁNCHEZ GALÁN	AVANGRID, INC.	Chairman	NO
MR JOSÉ LUIS SAN PEDRO GUERENABARRENA	IBERDROLA ESPAÑA, S.A.	Chairman	NO

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

Individual or company name of the director	Name of listed company	Position
MR BRAULIO MEDEL CÁMARA	ACERINOX, S.A.	Director
MS GEORGINA KESSEL MARTÍNEZ	GRUPO FINANCIERO SCOTIABANK INVERLAT, S.A. DE C.V.	Director
MS DENISE MARY HOLT	HSBC BANK PLC.	Director
MR MANUEL MOREU MUNAIZ	TUBACEX, S.A.	Director

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

Yes ☒ No ☐

Explanation of rules
Pursuant to the provisions of article 13.b) of the Regulations of the Board of Directors, individuals or legal entities serving as directors in more than five companies, of which no more than three may have shares trading on domestic or foreign stock exchanges, may not be appointed as directors. Positions within holding companies are excluded from the calculation. Furthermore, companies belonging to the same group shall be deemed to be a single company.

C.1.14. Section deleted.

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

Remuneration of the board of directors (thousands of euros)	14,548
Amount of pension rights accumulated by the current directors (thousands of euros)	0
Amount of pension rights accumulated by former directors (thousands of euros)	0

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

Individual or company name	Position(s)
MR FRANCISCO MARTÍNEZ CÓRCOLES	Business CEO of the Group
MR JOSÉ SAINZ ARMADA	Chief Financial and Resources Officer (CFO)
MR LUIS JAVIER ARANAZ ZUZA	Director of Internal Audit
MR PEDRO AZAGRA BLÁZQUEZ	Director of Corporate Development
MR JUAN CARLOS REBOLLO LICEAGA	Director of Administration and Control
MR SANTIAGO MARTÍNEZ GARRIDO	Chief Legal Officer

Total senior management remuneration (in thousands of euros)	11,680
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C.1.17. State the identity of the members of the board, if any, who are also members of the board of directors of significant shareholders and/or in entities of their group:

Individual or company name of director	Company name of the significant shareholder	Position

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

Individual or company name of related director	Individual or company name of related significant shareholder	Description of relationship
MR XABIER SAGREDO ORMAZA	KUTXABANK, S.A.	He is chair of the Board of Trustees of Bilbao Bizkaia Kutxa Fundación Bancaria, the majority shareholder of Kutxabank, S.A.

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

Yes ☒ No ☐

Description of amendments
<p>Set out below are the main amendments to the Regulations of the Board of Directors during financial year 2016:</p> <ul style="list-style-type: none"> - Include and update required references to the new autonomy rule of the Mission, Vision, and Values of the Iberdrola group, which, as an autonomous rule of the Corporate Governance System, contains the corporate philosophy of the Iberdrola Group. - Clarify the role of the Board of Directors in approving the strategic goals of the Iberdrola group, touching on the role to be followed in view of its corporate and governance structure. - Strengthen the independence and legitimacy of the role lead independent director (<i>consejero coordinador</i>), contemplating the need for re-election of the lead independent director by the Board of Directors if the person holding such position is re-elected as a director by the shareholders acting at a General Shareholders' Meeting. - The chair of the Board of Directors is entrusted with the duty of providing new directors with the information needed to perform their duties and to promote access by all directors to training materials and sessions that allow them to continuously update their knowledge. - It is provided that the secretary of the Board of Directors will assist the Compliance Unit in handling investigations that affect a member of the Board of Directors, and specifically in selecting the investigating officer, who shall be a person from outside the Group to guarantee independence. - The powers of the Audit and Risk Supervision Committee are updated to conform them to the new regulations on auditing. - The rules for related-party transactions are clarified and the regulation thereof is relocated: related-party transactions and conflicts of interest with directors and significant shareholders are included once again in the Regulations of the Board of Directors. Those regarding senior officers are governed by the <i>Procedure for Conflicts of Interest and Related-Party Transactions with Senior Officers</i>. - As to the approval of related-party transactions, the clarification is made that when dealing with transaction in which Iberdrola, S.A. does not participate, the scope of authorisation of the Board of Directors, or the Executive Committee if applicable, shall be circumscribed to verifying that the transaction is performed on market terms and conditions and in accordance with the principle of equal treatment, but such authorisation does not change the distribution of powers provided for by the corporate and governance structure of the Iberdrola Group. - The Sole Transitional Provision regarding the renewal of the Board of Directors is deleted.

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

1. APPOINTMENT AND RE-ELECTION OF DIRECTORS

The appointment, re-election, and removal of directors is within the purview of the shareholders at the General Shareholders' Meeting.

Vacancies that occur may be filled by the Board of Directors on an interim basis until the next General Shareholders' Meeting.

The Appointments Committee must advise the Board of Directors regarding the most appropriate configuration thereof and of its committees as regards size and equilibrium among the various classes of directors existing at any time. This is in any event based on the conditions that candidates for director

must meet pursuant to the Director Candidate Selection Policy.

The following may not be appointed as directors or as individuals representing a corporate director:

- a) Domestic or foreign companies competing with the Company in the energy industry or other industries, or the directors or senior officers thereof, or such persons, if any, as are proposed by them in their capacity as shareholders.
- b) Individuals or legal entities serving as directors in more than five companies, of which no more than three may have shares trading on domestic or foreign stock exchanges.
- c) For purposes of the provisions of the preceding paragraph, positions within holding companies are excluded from the calculation. Furthermore, companies belonging to the same group shall be deemed to be a single company.
- d) Persons who, during the two years prior to their appointment, have occupied high-level positions in Spanish government administrations that are incompatible with the simultaneous performance of the duties of a director of a listed company under Spanish national or autonomous community law, or positions of responsibility with entities regulating the energy industry, the securities markets, or other industries in which the Group operates.

Individuals or legal entities that are under any other circumstance of disqualification or prohibition governed by provisions of a general nature, including those that have interests in any way opposed to those of the Company or the Group.

The Board of Directors and the Appointments Committee, within the scope of their powers, shall endeavour to ensure that the candidates proposed are respectable and qualified persons, widely recognised for their expertise, competence, experience, qualifications, training, availability, and commitment to their duties.

It falls upon the Appointments Committee to propose the independent directors, as well as to report upon the proposals relating to the other classes of directors.

If the Board of Directors deviates from the proposals and reports of the Appointments Committee, it shall give reasons for so acting and shall record such reasons in the minutes.

2. EVALUATION OF DIRECTORS

The Board of Directors shall annually evaluate: (i) its operation and the quality of its work; (ii) the performance of their duties by the chairman of the Board of Directors and by the chief executive officer, based on the report submitted thereto by the Appointments Committee; and (iii) the operation of its committees, in view of the report submitted thereto by such committees. For such purpose, the chairman of the Board of Directors shall organise and coordinate the aforementioned evaluation process with the chair of each committee. The following section reports on the evaluation process during financial year 2016.

3. REMOVAL OF DIRECTORS

Directors "shall serve in their position for a term of four (4) years, so long as the shareholders acting at the General Shareholders' Meeting do not resolve to remove them and they do not resign from their position".

The Appointments Committee shall inform the Board of Directors regarding proposed removals due to breach of the duties inherent to the position of director or due to a director becoming affected by supervening circumstances of mandatory resignation or withdrawal. In addition, the Committee may propose the removal of directors in the event of disqualification, structural conflict of interest, or any other reason for resignation or withdrawal, pursuant to law or the Company's Corporate Governance System.

The Board of Directors may propose the removal of an independent director before the passage of the period provided for in the By-Laws only upon sufficient grounds, evaluated by the Board of Directors after a report from the Appointments Committee, or as a consequence of takeover bids, mergers, or other similar corporate transactions resulting in a significant change in the structure of the Company's share capital, as recommended by the Good Governance Code of Listed Companies.

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

Description of amendments
<p>Iberdrola has an on-going commitment to the development of its corporate governance, adopting the best practices in the international markets that apply thereto. In order to continue to permanently improve, Iberdrola evaluates the operation of its governance bodies on an annual basis, and based on the conclusions thereof defines an Action Plan with the principal areas of work for the coming year.</p> <p>More than 90% of the work areas defined in the Action Plan were met during 2016. Specifically, significant advancements were made in the following areas:</p> <ol style="list-style-type: none"> 1. Renewal of the composition of governance bodies: <ul style="list-style-type: none"> - Continuous renewal of the Board of Directors with the inclusion of a director having extensive experience in the financial and audit sector and broad knowledge of the Iberdrola group. - Increase in the percentage of independent directors on the Board of Directors from 64% to 71%. - Adjustment in the composition of the Executive Committee, aligning the representation of the various categories of directors on the Executive Committee with that of the Board of Directors. 2. Supervision of strategy and other critical issues: <ul style="list-style-type: none"> - Approval of the financial strategy and forecasts for 2016-2020. - Formalisation of the Mission, Vision, and Values of the Iberdrola group as a integral norm of the Corporate Governance System. - Revision of the Company's cyber-security strategy. 3. Transparency/communication with and engagement of shareholders: <ul style="list-style-type: none"> - First publication of the Annual Report on Engagement and Contacts with Shareholders. - First publication of the Activities Report of the Board of Directors and of the Consultative Committees thereof. 4. Remuneration: <ul style="list-style-type: none"> - Comparative study of the remuneration of the directors with the support of an outside adviser.

C.1.20 bis Describe the process of self-evaluation and the areas evaluated by the board of directors, as it may be assisted by an external consultant, regarding diversity in its composition and powers, the operation and composition of its committees, the performance of the chairman of the board and chief executive officer, and the performance and contribution of each director.

The Board of Directors evaluates its performance on an annual basis. On 25 October 2016 the Board of Directors approved the commencement of the process of evaluation of the Board of Directors itself, the Executive Committee, its consultative committees, the directors individually, and the chairman & CEO. In the last case, the evaluation was led by the lead independent director. The process concluded at the meeting of the Board of Directors held on 21 February 2017, with the approval of the results of the evaluation and the Action Plan for financial year 2017.

In order to align the Company with best international practices, it was decided to hire PricewaterhouseCoopers Asesores de Negocios, S.L. ("PwC") as an external adviser in the evaluation process.

The evaluation process covered approximately 500 objectively quantifiable and measurable indicators, which are updated each year with the latest trends and regulatory changes. The fields analysed in each of the reports were: (i) compliance with the Companies Act and the internal rules of the Company; (ii) a comparative analysis with domestic and international comparables; (iii) monitoring of the most advanced trends in corporate governance; and (iv) the application of the work areas defined in the action plans for

prior financial years.

The conclusions of the evaluation process reflect absolute compliance with the indicators relating to mandatory legal rules and regulations and an alignment of more than 90% with the latest international trends and with the application of the areas for improvement identified during prior years.

The Action Plan 2017 deriving from the evaluation process focuses on continuing to advance in three areas, principally:

1. Supervision of the implementation of the strategy, governance model, and business model.
2. Continued evolution of the abilities of the Board of Directors, advancing with programmes for initial orientation and training of the directors.
3. Compare trends regarding remuneration.

C.1.20 *ter* List any business relationships of the consultant or any company of its group with the company or any company of its group.

The business relationships of the consultant and the companies of its group with the Company and the group in 2016 came to the aggregate amount of 5.6 million euros, and were mainly focused on the following:

- Support in the regulatory and tax areas.
- Advice on accounting issues.
- Support to the Office of the Secretary of the Board of Directors.
- Advice on cyber-security and implementation of information technology systems.

C.1.21. State the circumstances under which the resignation of directors is mandatory.

Directors must submit their resignation from the position and formally resign from their position upon the occurrence of any of the instances of disqualification from or prohibition against performing the duties of director provided by law or by Iberdrola's Corporate Governance System.

In this connection, article 16.3 of the Regulations of the Board of Directors provides that the directors must submit their resignation to the Board of Directors in the following cases:

- a) When, due to supervening circumstances, they are involved in any circumstance of disqualification or prohibition provided by law or the Corporate Governance System.
- b) When, as a result of any acts or conduct attributable to the director, serious damage is caused to the value or reputation of the Company or there is a risk of criminal liability for the Company or any of the companies of the Group.
- c) When they cease to deserve the respectability or to have the capability, expertise, competence, availability, or commitment to their duties required to be a director of the Company.

In particular, when the activities carried out by the director, or the companies directly or indirectly controlled by the director, or the individuals or legal entities that are shareholders of or related to any of them, or the individual representing a corporate director, may compromise the competence of the director.
- d) When they are seriously reprimanded by the Board of Directors because they have breached any of their duties as directors, by resolution adopted by a two-thirds majority of the directors.
- e) When their continuance in office on the Board of Directors may for any reason, either directly, indirectly, or through persons related thereto, jeopardise the faithful and diligent performance of their duties in furtherance of the corporate interest.
- f) When the reasons why the director was appointed cease to exist and, in particular, in the case of proprietary directors, when the shareholder or shareholders who proposed, requested, or decided the appointment thereof totally or partially sell or transfer their equity interest, with the result that such

equity interest ceases to be significant or sufficient to justify the appointment.

- g) When an independent director unexpectedly falls under supervening circumstances that prevent the director from being considered as such pursuant to the provisions of law.

The resignation provisions set forth under f) and g) above shall not apply when, after a report from the Appointments Committee, the Board of Directors believes that there are reasons that justify the director's continuance in office, without prejudice to the effect that the new supervening circumstances may have on the classification of the director.

C.1.22. Section deleted.

C.1.23. Are qualified majorities, different from the statutory majorities, required to adopt any type of decision?

Yes ☒ No ☐

If so, describe the differences.

Description of differences
The Regulations of the Board of Directors (article 5.1 of the Regulations of the Board of Directors) require a majority of at least two-thirds of the directors present at the meeting in person or by proxy to approve the amendment thereof.
The serious reprimand of a director for having breached any of the duties entrusted thereto as director (article 16.3.d) of the Regulations of the Board of Directors) requires a majority of two-thirds of the directors.

C.1.24. Explain whether there are specific requirements, other than the requirements relating to directors, to be appointed chairman of the board of directors.

Yes ☐ No ☒

Description of requirements

C.1.25. State whether the chair has a tie-breaking vote:

Yes ☒ No ☐

Matters on which a tie-breaking vote may be cast
In the event of a tie, the chairman has a tie-breaking vote on any matter unless he becomes subject to a conflict of interest, in which case he must abstain from participating in the deliberation and voting stages of the respective resolution.

C.1.26. State whether the by-laws or the regulations of the board set forth any age limit for directors:Yes ☐ No ☒

Age limit for the chair	-
Age limit for the CEO	-
Age limit for directors	-

C.1.27. State whether the by-laws or the regulations of the Board establish any limit on the term of office for independent directors that is different than the term provided by regulatory provisions:Yes ☐ No ☒

Maximum number of terms	
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C.1.28. State whether there are formal rules for proxy-voting at meetings of the board of directors, the manner of doing so, and especially the maximum number of proxies that a director may hold, as well as whether any restriction has been established regarding the categories of directors to whom proxies may be granted beyond the restrictions imposed by law. If so, briefly describe such rules.

Pursuant to article 36.2 of the By-Laws, all of the directors may cast their vote and give their proxy in favour of another director, provided, however, that non-executive directors may only do so in favour of another non-executive director. Articles 32.2 and 36.2.b) of the Regulations of the Board of Directors require that directors attend the meetings of the Board of Directors. When directors are unable to attend in person for well-founded reasons, they shall endeavour to give a proxy to another director, to whom they shall give any appropriate instructions, but may not grant a proxy in connection with matters in respect of which they are involved in a conflict of interest.

The proxy granted shall be a special proxy for the Board meeting in question and may be communicated by any means allowing for the receipt thereof.

There is no maximum number of proxies provided per director.

C.1.29. State the number of meetings that the board of directors has held during the financial year. In addition, specify the number of times the board has met, if any, at which the chair was not in attendance. Proxies granted with specific instructions shall be counted as attendance.

Number of meetings of the board	8
Number of meetings of the board at which the chair was not in attendance	0

If the chair is an executive director, state the number of meetings held without the presence in person or by proxy of any executive director and chaired by the lead independent director.

Number of meetings	0
--------------------	---

State the number of meetings held by the different committees of the board of directors during the financial year:

Number of meetings of the Executive Committee	13
Number of meetings of the Audit and Risk Supervision Committee	13
Number of meetings of the Appointments Committee	9
Number of meetings of the Remuneration Committee	7
Number of meetings of the Corporate Social Responsibility Committee	12

C.1.30. State the number of meetings that the board of directors has held during the financial year with the attendance of all of its members. Proxies granted with specific instructions shall be counted as attendance:

Number of meetings with the attendance of the directors	8
% in attendance of total votes during the financial year	100%

C.1.31. State whether the annual individual accounts and the annual consolidated accounts that are submitted to the board for approval are previously certified:

Yes ☒ No ☐

Identify, if applicable, the person/persons that has/have certified the annual individual and consolidated accounts of the company for preparation by the board:

Name	Position
MR JOSÉ IGNACIO SÁNCHEZ GALÁN	Chairman & CEO
MR JUAN CARLOS REBOLLO LICEAGA	Director of Administration and Control

C.1.32. Explain the mechanisms, if any, adopted by the board of directors to avoid any qualifications in the audit report on the annual individual and consolidated accounts prepared by the board of directors and submitted to the shareholders at the general shareholders' meeting.

Articles 3 and 6 of the Regulations of the Audit and Risk Supervision Committee provide that it shall have the following duties, among others:

- Supervise the process of preparing and presenting regulated financial information relating to the Company, both individual and consolidated with its subsidiaries, reviewing compliance with legal requirements, the proper delimitation of the scope of consolidation, and the correct application of accounting standards, and submit recommendations or proposals to the Board of Directors to safeguard the integrity thereof.
- Establish appropriate relationships with the auditor to receive information regarding matters that might entail a threat to the independence thereof, for examination by the Committee, and any other information related to the development of the audit procedure, as well as such other communications as are provided for in the laws on auditing of accounts and in other legal provisions on auditing. The Committee must receive written confirmation from the auditor on an annual basis of their

independence in relation to the Company or entities directly or indirectly related thereto, as well as a detailed breakdown of information on additional services of any kind provided to and the corresponding fees received from such entities by such auditor or persons or entities related thereto, pursuant to the legal provisions governing the auditing of accounts.

- On an annual basis, prior to the audit report, issue a report containing an opinion on whether the independence of the auditor is compromised, which shall be made available to the shareholders upon the terms set forth in the Regulations for the General Shareholders' Meeting. This report shall contain a reasoned assessment of the provision of each and every one of the additional services other than the legal audit referred to in the preceding point, considered individually and as a whole, and in relation to the rules on independence or the legal provisions regarding the auditing of accounts.
- Report in advance to the Board of Directors regarding the financial information that the Company must disclose on a regular basis because of its status as a listed company; the Committee shall make sure that the interim accounts are prepared in accordance with the same accounting standards as the annual accounts and, for such purpose, it shall consider the appropriateness of a limited review by the auditor.
- Review the contents of the audit reports on the accounts and of the reports on the limited review of interim accounts, if any, as well as other mandatory reports to be prepared by the auditor, prior to the issuance thereof, in order to avoid qualified reports.
- Act as a channel of communication between the Board of Directors and the auditors, causing them to hold an annual meeting with the Board of Directors to report thereto on the work performed and the accounting status and risks of the Company.

Article 51 of the Regulations of the Board of Directors provides, among other things, that:

- The Board of Directors shall meet with the auditors at least once per year in order to receive information regarding the work performed and regarding the accounting status and risks of the Company.
- The Board of Directors shall use its best efforts to definitively prepare the accounts such that there is no room for qualifications by the auditors. However, when the Board of Directors believes that its opinion must prevail, it shall provide a public explanation of the content and scope of the discrepancy.

Pursuant to the above-cited articles, the Audit and Risk Supervision Committee reports on the financial information of the Company throughout the financial year and prior to the approval thereof by the Board of Directors and its submission to the National Securities Market Commission (*Comisión Nacional del Mercado de Valores*). The reports of the Committee, which the chair thereof presents to the full Board of Directors, are mainly intended to disclose such aspects, if any, as may give rise to qualifications in the audit report of Iberdrola and its consolidated group, making the appropriate recommendations to avoid any such qualifications.

Accordingly, the Committee submitted to the Board of Directors the following reports regarding the annual and half-yearly financial reports and the interim management statements of the Company for financial year 2016:

- Report dated 25 April 2016 on the interim management statement for the first quarter of 2016.
- Report dated 18 July 2016 on the economic/financial report for the first half of 2016.
- Report dated 24 October 2016 on the interim management statement for the third quarter of 2016.
- Report dated 20 February 2017 regarding the annual accounts of Iberdrola and its consolidated group for financial year 2016.

As disclosed in the information about Iberdrola posted on the website of the National Securities Market Commission (www.cnmv.es), the audit reports on the individual and consolidated annual accounts prepared by the Board of Directors have historically been issued without qualifications.

C.1.33. Is the secretary of the board a director?

Yes ☐ No ☒

If the secretary is not a director, complete the following table.

Individual or company name of the secretary	Representative
MR JULIÁN MARTÍNEZ-SIMANCAS SÁNCHEZ	-

C.1.34. Section deleted.

C.1.35. State the mechanisms, if any, used by the company to preserve the independence of auditors, financial analysts, investment banks, and rating agencies.

1. MECHANISMS TO PRESERVE THE INDEPENDENCE OF THE AUDITOR

The Auditor Contracting and Relations Policy, contained within the Company's Corporate Governance System, provides that:

- The Audit and Risk Supervision Committee shall receive information from the auditor regarding matters that might entail risks to the independence thereof.
- The Committee shall receive from the auditor, on an annual basis, written confirmation of its independence with respect to the Company or entities directly or indirectly related thereto, and information on additional services (other than auditing) provided thereto.
- The auditor shall provide to the Committee annual information regarding the profiles and the track record of the persons making up the audit teams of the Company and of the Iberdrola Group, stating the changes in the composition of such teams compared to the preceding financial year.
- The Committee shall issue, on an annual basis and prior to the issuance of the audit report, a report setting forth an opinion on the independence of the auditor. This report shall in any case pass upon the impact on the independence of the auditor of the provision of services additional to those referred to above and shall attach a reasoned assessment thereof.
- The Committee shall monitor the quality assurance and independence safeguarding internal procedures implemented by the auditor.
- The Committee shall not submit a proposal to the Board of Directors, which in turn shall not submit a proposal to the shareholders at a General Shareholders' Meeting, for appointment of firms as auditor when it has evidence that they are affected by a lack of independence, a prohibition, or pursuant to the law on auditing. In particular, if the fees accrued from the provision of audit services and services other than audit that the Company and any other entity of the Iberdrola Group expect to pay the auditor or audit firm or a member of its network during each of the last three consecutive financial years represent more than fifteen per cent of the total annual income of the auditor or audit firm and of said network.

As regards 2016:

- Iberdrola's auditor appeared on twelve occasions before the Audit and Risk Supervision Committee and on one occasion before the Board of Directors to report on various matters relating to the audit process. During these appearances, the auditor did not report issues that might put its independence at risk.
- On 18 February 2016 the auditor sent written confirmation of its independence with regard to the audit of financial information for financial year 2015.
- On 12 July 2016 the auditor sent written confirmation of its independence with regard to the limited review of financial information through 30 June 2016.
- On 15 February 2017 the auditor sent written confirmation of its independence with regard to the audit of the financial information for financial year 2016.
- The auditor represented in the aforementioned letters that it had implemented the internal procedures

necessary to ensure its independence.

- The hiring of the auditor for services other than auditing is authorised in advance by the Committee. The hiring is supported by the respective letters of the partner responsible for the audit confirming the non-existence of restrictions on independence to perform this work.
- In its written confirmation of 15 February 2017, the auditor reported that there were no hirings of professionals from the auditor at the Company or its group, except in the case of the Company, where three team leaders were hired, and Avangrid, Inc., where one team leader was hired. The Audit and Risk Supervision Committee believes that these hirings do not affect the independence of the auditor, as they involve professionals with short-term professional experience and who held positions of medium/low responsibility at the audit firm.
- On 20 February 2017 the Committee issued its report to the Board of Directors regarding the independence of the Company's auditor. The Committee concluded that the auditor performed its audit work with independence from the Company or entities related thereto.

2. MECHANISMS TO PRESERVE THE INDEPENDENCE OF FINANCIAL ANALYSTS, INVESTMENT BANKS, AND RATING AGENCIES

The principles which form the basis of the relations of the Company with financial analysts, investment banks, and rating agencies are contained in the Policy regarding Communication and Contacts with Shareholders, Institutional Investors, and Proxy Advisors and are transparency, non-discrimination, truthfulness, and trustworthiness of the information supplied. The Finance and Resource Division, through the Investor Relations Division, manages their requests for information and requests submitted by institutional or retail investors (in the case of retail investors, through the Office of the Shareholder). The Finance and Resource Division gives mandates to investment banks. The Development Division gives the appropriate advisory mandates to investment banks within the scope of its activities, in coordination with the Finance and Resource Division.

The independence of financial analysts is protected by the Investor Relations Division, which ensures the objective, fair, and non-discriminatory treatment thereof.

To actualise the principles of transparency and non-discrimination, always in strict compliance with regulations regarding the Securities Market, the Company has a number of communication channels:

- Personalised assistance for analysts, investors, and rating agencies.
- Publication of the information relating to quarterly results and other specific events, such as those relating to the submission of the Business Prospects or to corporate transactions.
- E-mail through the corporate website (accionistas@iberdrola.com) and a toll-free line for shareholders (+34 900 100 019).
- In-person and broadcasted presentations.
- Release of announcements and news.
- Visits to Company facilities.

C.1.36. State whether the Company has changed the external auditor during the financial year. If so, identify the incoming and the outgoing auditor:

Yes ☐ No ☒

Outgoing auditor	Incoming auditor

If there has been any disagreement with the outgoing auditor, provide an explanation thereof:

Yes ☐ No ☒

Description of the disagreement

C.1.37. State whether the audit firm performs other non-audit work for the company and/or its group. If so, state the amount of the fees paid for such work and the percentage they represent of the aggregate fees charged to the company and/or its group:

Yes ☒ No ☐

	Company	Group	Total
Amount of other non-audit work (thousands of euros)	0	60	60
Amount of non-audit work / Aggregate amount billed by the audit firm (%)	0	0.3	0.2

C.1.38. State whether the audit report on the annual accounts for the prior financial year has observations or qualifications. If so, state the reasons given by the chair of the audit committee to explain the content and scope of such observations or qualifications.

Yes ☐ No ☒

Explanation of reasons

C.1.39. State the consecutive number of years for which the current audit firm has been auditing the annual accounts of the company and/or its group. In addition, state the percentage represented by such number of financial years audited by the current audit firm with respect to the total number of financial years in which the annual accounts have been audited:

	Company	Group
Number of continuous financial years	11	11

	Company	Group
Number of years audited by the current audit firm / Number of years in which the company has been audited (%)	45.83	45.83

C.1.40. State whether there is any procedure for directors to hire external advisory services, and if so, describe it:

Yes ☒ No ☐

Describe the procedure
<p>Pursuant to the provisions of article 35 of the Regulations of the Board of Directors, in order to be assisted in the performance of the duties entrusted thereto, any director may request the hiring of legal, accounting, technical, financial, commercial, or other expert advisers, whose services shall be paid for by the Company.</p> <p>The assignment must deal with specific issues of certain significance and complexity arising during the performance of the director's duties.</p> <p>The request for an expert to be hired shall be channelled through the secretary of the Board of Directors, who may subject it to the prior approval of the Board of Directors; such approval may be denied in well-founded instances, including the following circumstances:</p> <ul style="list-style-type: none"> a) That it is not necessary for the proper performance of the duties entrusted to the directors. b) That the cost thereof is not reasonable in light of the significance of the issues and the assets and income of the Company. c) That the technical assistance sought may be adequately provided by the Company's own experts and technical personnel. d) That it may entail a risk to the confidentiality of the information that must be made available to the expert. <p>Furthermore, article 25.2 of the Regulations of the Audit and Risk Supervision Committee, article 18.2 of the Regulations of the Appointments Committee, article 14.2 of the Regulations of the Remuneration Committee, and article 17.3 of the Regulations of the Corporate Social Responsibility Committee provide that such committees may seek advice from outside professionals, who shall submit their reports directly to the chair of the relevant committee. It shall also be ensured that conflicts of interest do not undermine the independence of any external advice received.</p>

C.1.41. State whether there is any procedure for directors to obtain sufficiently in advance the information required to prepare for meetings of management-level decision-making bodies and, if so, describe it:

Yes ☒ No ☐

Describe the procedure
<p>Section 16 of the General Corporate Governance Policy provides that "the Company has a programme to provide directors with information and updates in response to the need for professionalisation, diversification, and qualification of the Board of Directors.</p> <p>In order to improve their knowledge of the Group, presentations are made to the directors regarding the businesses thereof. In addition, a portion of each meeting of the Board of Directors tends to be dedicated to a presentation on economic, legal, or political/social issues of importance to the Group.</p> <p>The directors have access to a specific application, the directors' website, that facilitates performance of their duties and the exercise of their right to receive information. This website includes information deemed appropriate for preparation of the meetings of the Board of Directors and the committees thereof in accordance with the agenda, as well as training materials intended for the directors and presentations made to the Board of Directors.</p> <p>In addition, the directors shall be given access through the directors' website to the minutes of the meetings of the Board of Directors and the committees thereof, as well as such other information that the Board of Directors resolves to include".</p> <p>Pursuant to article 34.4 of the Regulations of the Board of Directors, there shall be an inclusion on the directors' website of such information as is deemed appropriate for preparation of the meetings of the Board of Directors and the committees thereof, in accordance with the agenda included in the calls to meeting, as well as access to materials relating to director training programmes.</p> <p>In addition, article 36.3.a) of the Regulations of the Board of Directors provides that a director is specifically required to "properly prepare the meetings of the Board of Directors and, if applicable, the</p>

meetings of the Executive Committee or of the committees of which the director is a member, for which purposes the director must diligently become apprised of the running of the Company and the matters to be discussed at such meetings”.

C.1.42. State whether the company has established any rules requiring directors to inform the company —and, if applicable, resign from their position— in cases in which the credit and reputation of the company may be damaged, and if so provide a detailed description:

Yes ☒ No ☐

Explain the rules

Section 17 of the General Corporate Governance Policy sets out the obligations and duties of the directors, including, as a statement of the duty of loyalty, the duty to submit their resignation to the Board of Directors in the event of supervening disqualification, lack of competence, prohibition against holding office as a director, and other instances provided for in the Company's Corporate Governance System.

As provided by subsections c) and d) of article 44.2 of the Regulations of the Board of Directors, the director must inform the Company of any judicial, administrative, or other proceedings instituted against the director which, because of their significance or characteristics, may seriously reflect upon the reputation of the Company. In particular, if a director is subject to investigation or an order for further criminal prosecution upon indictment, or if an order for the commencement of an oral trial is issued against the director for the commission of any of the crimes contemplated in section 213 of the Companies Act, such director shall give notice thereof to the Company, through the chairman of the Board of Directors. In such instance, the Board of Directors shall review this circumstance as soon as practicable and, following a report of the Appointments Committee, shall adopt the decisions it deems fit taking into account the interests of the Company.

In addition, the director must inform the Company of any fact or event that may be relevant to the holding of office as a director.

Directors must also submit their resignation to the Board and formally resign from their position in the events set forth in article 16.3 of the Regulations of the Board of Directors, particularly:

- a) When, due to supervening circumstances, they are involved in any circumstance of disqualification or prohibition provided by law or the Corporate Governance System.
- b) When, as a result of any acts or conduct attributable to the director, serious damage is caused to the value or reputation of the Company or there is a risk of criminal liability for the Company or any of the companies of the Group.
- c) When they cease to deserve the respectability or to have the capability, expertise, competence, availability, or commitment to their duties required to be a director of the Company.

In particular, when the activities carried out by the director, or the companies directly or indirectly controlled by the director, or the individuals or legal entities that are shareholders of or related to any of them, or the individual representing a corporate director, may compromise the competence of the director.
- d) When they are seriously reprimanded by the Board of Directors because they have breached any of their duties as directors, by resolution adopted by a two-thirds majority of the directors.
- e) When their continuance in office on the Board of Directors may for any reason, either directly, indirectly, or through persons related thereto, jeopardise the faithful and diligent performance of their duties in furtherance of the corporate interest.
- f) When the reasons why the director was appointed cease to exist and, in particular, in the case of proprietary directors, when the shareholder or shareholders who proposed, requested, or decided the appointment thereof totally or partially sell or transfer their equity interest, with the result that such equity interest ceases to be significant or sufficient to justify the appointment.
- g) When an independent director unexpectedly falls under supervening circumstances that prevent the director from being considered as such pursuant to the provisions of law.

In any of the instances set forth in section 3 of article 16 of the Regulations of the Board of Directors, the Board of Directors shall request the director to resign from such position and, if applicable, shall propose the director's removal from office to the shareholders at the General Shareholders' Meeting.

By way of exception, the resignation provisions set forth in letters f) and g) of article 16.3 of the Regulations of the Board of Directors cited above shall not apply when, after a report from the Appointments Committee, the Board of Directors believes that there are reasons that justify the director's continuance in office, without prejudice to the effect that the new supervening circumstances may have on the classification of the director.

C.1.43. State whether any member of the board of directors has informed the company that such member has become subject to an order for further criminal prosecution upon indictment or that an order for the commencement of an oral trial has been issued against such member for the commission of any of the crimes contemplated in section 213 of the Companies Act:

Yes ☐ No ☒

Name of director	Criminal case	Comments

State whether the board of directors has analysed the case. If so, provide a duly substantiated explanation of the decision adopted regarding whether or not the director should remain in office or, if applicable, describe the actions taken by the board of directors through the date of this report or that it plans to take.

Yes ☐ No ☐

Decision made / action taken	Duly substantiated explanation

C.1.44. Describe the significant agreements entered into by the company that go into effect, are amended, or terminate in the event of a change in control at the company as a result of a takeover bid, and effects thereof.

Not applicable.

C.1.45. Identify on an aggregate basis and provide a detailed description of the agreements between the company and its management level and decision-making positions or employees that provide for indemnities, guarantee or "golden parachute" clauses upon resignation or termination without cause, or if the contractual relationship is terminated as a result of a takeover bid or other type of transaction.

Number of beneficiaries	45
Type of beneficiary	Executive directors, officers, and employees

Description of agreement
<p>1. EXECUTIVE DIRECTORS</p> <p>Pursuant to the provisions of his contract, the chairman & chief executive officer has the right to receive a severance payment in the event of termination of his relationship with the Company, provided that such termination is not the consequence of a breach attributable thereto or exclusively due to his own decision to withdraw. The amount of the severance payment is three times annual salary.</p> <p>Furthermore, in consideration for his two-year non-compete commitment, the chairman & chief executive officer is entitled to severance equal to the remuneration for that period.</p> <p>Since 2011, the Director Remuneration Policy provides that the limit on the amount of such severance under new contracts signed with executive directors shall be two times their annual salary.</p> <p>2. OFFICERS</p> <p>Some contracts with officers of Iberdrola include specific severance clauses. The purpose of such clauses is to obtain an effective and sufficient level of loyalty from senior officers who are necessary for the management of the Company and thus avoid a loss of experience and knowledge that might jeopardise the achievement of strategic objectives. The amount of the severance is determined based on length of service and the reasons for the officer's withdrawal from office, up to a maximum of five times annual salary.</p> <p>Notwithstanding the foregoing, the Senior Officer Remuneration Policy provides since 2011 that the limit on the amount of the severance under new contracts with senior officers shall be two times their annual salary.</p> <p>3. EMPLOYEES</p> <p>The contracts of employees linked to Iberdrola by an ordinary employment relationship do not generally include specific severance clauses and, accordingly, the applicable provisions of labour law shall apply in the event of termination of the employment relationship.</p>

State whether such agreements must be reported to and/or approved by the decision-making bodies of the company or its group:

	Board of directors	General Shareholders' Meeting
Decision-making body approving the provisions	X	

	Yes	No
Is information about these provisions provided to the shareholders at the general shareholders' meeting?	X	

C.2. Committees of the board of directors

C.2.1. Describe all of the committees of the board of directors, the members thereof, and the proportion of executive, proprietary, independent, and other external directors of which they are comprised:

EXECUTIVE COMMITTEE

Name	Position	Class
MR JOSÉ IGNACIO SÁNCHEZ GALÁN	CHAIRMAN	Executive director

MS INÉS MACHO STADLER	MEMBER	Independent director
MR JOSÉ LUIS SAN PEDRO GUERENABARRENA	MEMBER	Other external director
MR ÁNGEL JESÚS ACEBES PANIAGUA	MEMBER	Independent director
MR MANUEL MOREU MUNAIZ	MEMBER	Independent director

% executive directors	20.00
% proprietary directors	0
% independent directors	60.00
% other external	20.00

Explain the duties assigned to this committee, describe the procedures and rules of organisation and operation thereof, and summarise the most significant activities thereof during the year.

The Executive Committee is assigned all the powers of the Board of Directors, except for those powers that may not be delegated pursuant to legal or by-law restrictions. The chairman of the Board of Directors, and the chief executive officer, if any, are members in any case. The secretary of the Board of Directors acts as secretary of the Committee.

The Executive Committee shall meet as many times as deemed necessary by the chair thereof. It shall also meet when so requested by a minimum of two of the directors forming part thereof.

Resolutions of the Committee shall be adopted by absolute majority of its members who are present at the meeting in person or by proxy.

The duties of this Committee consist of making proposals to the Board regarding strategic decisions, investments, and divestitures that are significant for the Company or the Group, assessing their conformity to the budget and the strategic plans and analysing and monitoring business risks.

The duties of the Committee are provided in article 38 of the By-Laws and are further developed in article 25 of the Regulations of the Board of Directors.

State whether the composition of the executive committee reflects the participation of the different directors within the board based on their class.

Yes ☒ No ☐

If no, explain the composition of your executive committee

AUDIT AND RISK SUPERVISION COMMITTEE

Name	Position	Class
MS GEORGINA KESSEL	CHAIR	Independent director

MARTÍNEZ		
MS DENISE MARY HOLT	MEMBER	Independent director
MR JOSÉ WOLFREDO FERNÁNDEZ	MEMBER	Independent director
MR XABIER SAGREDO ORMAZA	MEMBER	Other external director

% executive directors	0
% proprietary directors	0
% independent directors	75.00
% other external	25.00

Explain the duties assigned to this committee, describe the procedures and rules of organisation and operation thereof, and summarise the most significant activities thereof during the year.

The Audit and Risk Supervision Committee is an internal informational and consultative body.

A majority of its members shall be independent, and at least one of them shall be appointed taking into account the knowledge and experience thereof in the areas of accounting, audit, and risk management.

The Board of Directors shall appoint a chair of the Committee from among the independent directors forming part thereof, as well as its secretary, who need not be a director.

The members of the Audit and Risk Supervision Committee shall be appointed for a maximum term of four years and may be re-elected on one or more occasions for terms of the same maximum length. The chair shall hold office for a maximum period of four years, after which period the director who has held office as such may not be re-elected until the passage of at least one year from ceasing to act as such.

A valid quorum shall be established with the attendance at the meeting, in person or by proxy, of a majority of its members, and resolutions shall be adopted by an absolute majority of votes of the members present at the meeting in person or by proxy.

The duties of the Committee are provided in article 39 of the By-Laws and are further developed in article 26 of the Regulations of the Board of Directors, as well as in the Regulations of the Audit and Risk Supervision Committee.

Identify the director who is a member of the audit committee and who has been appointed taking into account the director's knowledge and experience in the areas of accounting, audit, or both, and report the number of years that the chair of this committee has held office.

Name of director with experience	MS GEORGINA KESSEL MARTÍNEZ
Number of years during which chair has held the position	1

APPOINTMENTS COMMITTEE

Name	Position	Class
MS MARÍA HELENA ANTOLÍN RAYBAUD	CHAIR	Independent director
MR IÑIGO VÍCTOR DE ORIOL IBARRA	MEMBER	Other external director
MR ÁNGEL JESÚS ACEBES PANIAGUA	MEMBER	Independent director

% executive directors	0
% proprietary directors	0
% independent directors	66.67
% other external	33.33

Explain the duties assigned to this committee, describe the procedures and rules of organisation and operation thereof, and summarise the most significant activities thereof during the year.

The Appointments Committee is an internal informational and consultative body.

A majority of the members of the Appointments Committee must be classified as independent. The Board also appoints the chair thereof from among the independent directors forming part thereof, as well as its secretary, who need not be a director.

The members of the Appointments Committee shall be appointed for a maximum term of four years and may be re-elected on one or more occasions for terms of the same maximum length.

A valid quorum shall be established with the attendance at the meeting, in person or by proxy, of a majority of its members, and resolutions shall be adopted by an absolute majority of votes of the members present at the meeting in person or by proxy.

The duties of the Committee are set out in article 27 of the Regulations of the Board of Directors, as well as in the Regulations of the Appointments Committee.

REMUNERATION COMMITTEE

Name	Position	Class
MS INÉS MACHO STADLER	CHAIR	Independent director
MR IÑIGO VÍCTOR DE ORIOL IBARRA	MEMBER	Other external director
MR SANTIAGO MARTÍNEZ LAGE	MEMBER	Independent director

% executive directors	0
% proprietary directors	0

% independent directors	66.67
% other external	33.33

Explain the duties assigned to this committee, describe the procedures and rules of organisation and operation thereof, and summarise the most significant activities thereof during the year.

The Remuneration Committee is an internal informational and consultative body.

A majority of the members of the Remuneration Committee must be classified as independent. The Board also appoints the chair thereof from among the independent directors forming part thereof, as well as its secretary, who need not be a director.

The members of the Remuneration Committee shall be appointed for a maximum term of four years and may be re-elected on one or more occasions for terms of the same maximum length.

A valid quorum shall be established with the attendance at the meeting, in person or by proxy, of a majority of its members, and resolutions shall be adopted by an absolute majority of votes of the members present at the meeting in person or by proxy.

The duties of the Committee are set out in article 28 of the Regulations of the Board of Directors, as well as in the Regulations of the Remuneration Committee.

CORPORATE SOCIAL RESPONSIBILITY COMMITTEE

Name	Position	Class
MS SAMANTHA BARBER	CHAIR	Independent director
MR BRAULIO MEDEL CÁMARA	MEMBER	Independent director
MR MANUEL MOREU MUNAIZ	MEMBER	Independent director

% executive directors	0
% proprietary directors	0
% independent directors	100.00
% other external	0

Explain the duties assigned to this committee, describe the procedures and rules of organisation and operation thereof, and summarise the most significant activities thereof during the year.

The Corporate Social Responsibility Committee is an internal informational and consultative body.

A majority of the members of the Corporate Social Responsibility Committee must be classified as independent. The Board of Directors shall appoint a chair of the Committee from among the members forming part thereof, as well as its secretary, who need not be a director.

The members of the Corporate Social Responsibility Committee shall be appointed for a maximum term of four years and may be re-elected on one or more occasions for terms of the same maximum length.

A valid quorum shall be established with the attendance at the meeting, in person or by proxy, of a majority of its members, and resolutions shall be adopted by an absolute majority of votes of the members present at the meeting in person or by proxy.

The duties of the Committee are provided in article 41 of the By-Laws and are further developed in article 29 of the Regulations of the Board of Directors, as well as in the Regulations of the Corporate Social Responsibility Committee.

C.2.2. Complete the following table with information regarding the number of female directors comprising the committees of the board of directors for the last four financial years:

	Number of female directors							
	Financial Year 2016		Financial Year 2015		Financial Year 2014		Financial Year 2013	
	Number	%	Number	%	Number	%	Number	%
Executive Committee	1	20.00	1	20.00	1	20.00	1	20.00
Audit and Risk Supervision Committee	2	66.66	2	66.66	2	50.00	1	33.33
Appointments Committee	1	33.33	1	33.33	1	33.33	1	33.33
Remuneration Committee	1	33.33	1	33.33	1	33.33	1	33.33
Corporate Social Responsibility Committee	1	33.33	1	33.33	2	66.66	2	66.66

C.2.3. Section deleted.

C.2.4. Section deleted.

C.2.5. State, if applicable, the existence of regulations of the board committees, where such regulations may be consulted, and the amendments made during the financial year. Also state if any annual report of the activities performed by each committee has been voluntarily prepared.

1. AUDIT AND RISK SUPERVISION COMMITTEE

The Audit and Risk Supervision Committee has its own Regulations, which may be viewed by interested parties on the Company's website (www.iberdrola.com).

Article 20.2 of the Regulations of the Audit and Risk Supervision Committee provides that within three months following the end of each financial year of the Company, the Audit and Risk Supervision Committee shall submit to the Board of Directors for approval a Report describing its work during the financial year covered thereby, which shall be made available to the shareholders on occasion of the call to the Annual General Shareholders' Meeting.

The Report for financial year 2016 was prepared by the Audit and Risk Supervision Committee at its meeting of 12 January 2017.

2. APPOINTMENTS COMMITTEE

The Appointments Committee has its own Regulations, which may be viewed by interested parties on the Company's corporate website (www.iberdrola.com).

Article 20.2 of the Regulations of the Appointments Committee provides that within three months following the end of the Company's financial year, the Committee shall submit to the Board of Directors for approval a report detailing its work for the financial year covered by the report.

The Report for financial year 2016 was prepared by the Appointments Committee at its meeting of 19 January 2017.

3. REMUNERATION COMMITTEE

The Remuneration Committee has its own Regulations, which may be viewed by interested parties on the Company's corporate website (www.iberdrola.com).

Article 16.2 of the Regulations of the Remuneration Committee provides that within three months following the end of the Company's financial year, the Committee shall submit to the Board of Directors for approval a report detailing its work for the financial year covered by the report.

The Report for financial year 2016 was prepared by the Remuneration Committee at its meeting of 13 January 2017.

4. CORPORATE SOCIAL RESPONSIBILITY COMMITTEE

The Corporate Social Responsibility Committee has its own Regulations, which may be viewed by interested parties on the Company's corporate website (www.iberdrola.com).

Article 19.2 of the Regulations of the Corporate Social Responsibility Committee provides that within three months following the end of each financial year of the Company, the Committee shall submit to the Board of Directors for approval a report on its activities during the financial year covered by the report.

The Report for financial year 2016 was prepared by the Corporate Social Responsibility Committee at its meeting of 16 January 2017.

As a new development this year, an Activities Report of the Board of Directors and of the Committees thereof for financial year 2016 is published for purposes of the call to the General Shareholders' Meeting.

This document replaces the traditional Annual Activities Report of the Consultative Committees of the Board of Directors (Committees Book), such that on this occasion it will also include information of interest regarding the activities carried out by the Board of Directors and by the Executive Committee during 2016.

This innovation is based on the Company's commitment to good corporate governance practices and transparency and to the growing demand by shareholders and proxy advisors for companies to report on the activities of their governance bodies.

C.2.6. Section deleted.

D. RELATED-PARTY TRANSACTIONS AND INTRAGROUP TRANSACTIONS

D.1. Explain any procedures for approving related-party and intragroup transactions.

Procedure for the approval of related-party transactions
<p>Article 43 of the Regulations of the Board of Directors provides that:</p> <ol style="list-style-type: none"> Any transaction by the Company or the companies forming part of its Group with directors, with shareholders that directly or indirectly own a shareholding interest that is equal to or greater than that legally regarded as significant at any time or that have proposed or caused the appointment of any of the directors of the Company, or with the respective related persons ("Related-Party Transactions"), shall be subject to the approval of the Board of Directors, or in urgent cases, of the Executive Committee, following a report from the Appointments Committee. In the event that authorisation has been granted by the Executive Committee due to the urgency of the matter, the Executive Committee shall give notice thereof to the Board of Directors at its next meeting in order for it to be ratified. The authorisation of Related-Party Transactions must be approved by the shareholders at the General Shareholders' Meeting in the instances provided by law, and particularly if it relates to a transaction having a value of more than ten per cent of the corporate assets. As an exception, Related-Party Transactions with any of the listed companies of the Group (as is the case of Avangrid, Inc.) or with the subsidiaries thereof shall not be subject to the provisions of article 43, provided that they have corporate governance rules similar to those of the Company. The execution of a Related-Party Transaction puts the director engaging in said transaction or who is related to the person engaging in the transaction in a conflict of interest, for which reason the provisions of article 39 of the Regulations of the Board of Directors shall apply, to the extent applicable. The Board of Directors, through the Appointments Committee, shall ensure that Related-Party Transactions are carried out under arm's length conditions and with due observance of the principle of equal treatment of shareholders in the same situation. In the case of transactions to be carried out by companies of the Group, the scope of authorisation of the Board of Directors, or that of the Executive Committee, if applicable, referred to in the preceding sections, shall be circumscribed to the verification of compliance with such particulars. In the case of customary and recurring Related-Party Transactions in the ordinary course of business, it shall be sufficient for the Board of Directors to give prior generic approval of the kind of transaction and of the conditions for performance thereof, following a report from the Appointments Committee. If a Related-Party Transaction entails the successive performance of different transactions, of which the second and subsequent transactions are mere acts of execution of the first transaction, the provisions of this article 43 shall only apply to the first transaction carried out. The authorisation shall not be required in connection with transactions that simultaneously satisfy the following three conditions: that they are conducted under contracts whose terms and conditions are standardised and apply on an across-the-board basis to a large number of customers; that they are conducted at prices or rates established generally by the party acting as supplier of the goods or services in question, and that the amount thereof does not exceed one percent of the consolidated annual income of the Group. The Company shall report Related-Party Transactions in the Half-Yearly Financial Report and in the Annual Corporate Governance Report, in the cases and to the extent provided by law. Likewise, the Company shall include in the notes accompanying the annual accounts information regarding the transactions by the Company or by the companies of the Group with the directors and with those persons who act for the account of the latter when such transactions are conducted other than in the ordinary course of the Company's business or other than under normal arm's length conditions. <p>To this end, the directors must give written notice to the secretary of the Board of Directors, on a semi-annual basis, within the first week of January and July of each year, regarding the Related-Party Transactions that they have engaged in. If they are not carried out, the directors shall so report. The secretary of the Board of Directors shall send a notice to the directors on a semi-annual basis requesting the appropriate information that must be sent to the Company.</p> <ol style="list-style-type: none"> The notice must include the following information: the nature of the transaction; the date on which the

transaction originated; the conditions and periods for payment; the name of the person who carried out the transaction and the relationship, if any, with the director; the amount of the transaction; and other aspects, such as pricing policies, guarantees given and received, and any other feature of the transactions that allows for a proper assessment thereof, particularly such information as allows for verification that it has been carried out on arm's length conditions and in compliance with the principle of equal treatment.

12. The secretary of the Board of Directors shall prepare a register of Related-Party Transactions. The information set forth in such register shall be made available to the Compliance Unit when it so requests, and shall also periodically be made available to the Audit and Risk Supervision Committee through the Internal Audit Area Division.

D.2. Describe those transactions that are significant due to the amount or subject-matter thereof between the company or entities of its group and the company's significant shareholders:

Individual or company name of the significant shareholder	Individual or company name of the company or entity within its group	Nature of the relationship	Type of transaction	Amount (thousands of euros)
QATAR INVESTMENT AUTHORITY	IBERDROLA, S.A.	Corporate	Dividends and other distributed benefits	21,571

D.3. Describe those transactions that are significant due to the amount or subject-matter thereof between the company or entities of its group and the company's directors or officers:

Individual or company name of directors or officers	Individual or company name of related party	Relation	Nature of the relationship	Amount (thousands of euros)

D.4. Report the significant transactions made by the company with other entities belonging to the same group, provided they are not eliminated in the preparation of the consolidated accounts and they are not part of the ordinary course of business of the company as to their purpose and conditions.

Name of the entity within the group	Brief description of the transaction	Amount (thousands of euros)
GAMESA GROUP	Purchase of material assets	483,113
GAMESA GROUP	Receipt of services	62,604
GAMESA GROUP	Purchase of goods (finished or in progress)	702

GAMESA GROUP	Sale of goods (finished or in progress)	3,127
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In any case, report any intragroup transaction with entities established in countries or territories considered to be tax havens:

Name of the entity within the group	Brief description of the transaction	Amount (thousands of euros)

D.5. State the amount of transactions with other related parties.

Amount (thousands of euros)	
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D.6. Describe the mechanisms used to detect, determine, and resolve potential conflicts of interest between the company and/or its group, and its directors, officers, or significant shareholders.

1. CONFLICTS OF INTEREST BETWEEN THE COMPANY AND THE DIRECTORS

Pursuant to article 39 of the Regulations of the Board of Directors, a conflict of interest shall be deemed to exist in those situations provided by law, particularly when the interests of the director, either for their own or another's account, directly or indirectly conflict with the interest of the Company or of companies within the Group and their duties to the Company. An interest of a director shall exist when a matter affects the director or a person related thereto or, in the case of a proprietary director, when it also affects the shareholder or shareholders that proposed or caused the appointment thereof or persons directly or indirectly related thereto.

Such article contains a list of persons deemed to be related for such purposes, distinguishing between an individual and a corporate director.

Conflicts of interest shall be governed by the following rules:

- a) Communication: once a director becomes aware of being in a situation of conflict of interest, the director must give written notice of the conflict to the Board of Directors, in the person of the secretary thereof. The secretary shall periodically submit a copy of the notices received to the Appointments Committee, in the person of the secretary thereof.

The notice shall contain a description of the situation giving rise to the conflict of interest, with a statement as to whether it is a direct conflict or an indirect conflict through a related person, in which case the latter person must be identified.

The description of the situation must describe, as applicable, the subject matter and the principal terms of the transaction or the planned decision, including the amount thereof or an approximate financial assessment thereof. If the situation giving rise to the conflict of interest is a Related-Party Transaction (as this term is defined in article 43), the notice shall also identify the department or person of the Company or of any of the companies of the Group with which the respective contacts were made.

Any question as to whether a director might be involved in a conflict of interest must be forwarded to the secretary of the Board of Directors, and the director must refrain from taking any action until it is resolved.

- b) Abstention: if the conflict arises from an operation, transaction, or circumstance that requires any kind

of operation, report, decision, or acceptance, the director must refrain from taking any action until the Board of Directors studies the case and adopts and informs the director of the appropriate decision.

To this end, the director shall leave the meeting during the deliberation and voting on those matters in which the director is affected by a conflict of interest, and shall not be counted in the number of members attending for purposes of the calculation of a quorum and majorities.

At each meeting of the Board of Directors and of the committees thereof, the secretary shall remind the directors, before dealing with the agenda, of the abstention rule established in this article.

- c) Transparency: whenever required by law, the Company shall report any cases of conflict of interest in which the directors have been involved during the financial year in question and of which the Company is aware by reason of notice given thereto by the director affected by such conflict or by any other means.

However, if the conflict of interest situation is, or may reasonably be expected to be, of a structural and permanent nature, it shall be deemed that there is a loss of the competence required to hold office. In this regard, article 16 of the Regulations of the Board of Directors provides that a loss of competence is an event of resignation, removal, and withdrawal of the director.

2. CONFLICTS OF INTEREST BETWEEN THE COMPANY AND THE SENIOR OFFICERS AND OTHER PERSONS SUBJECT TO CONFLICT OF INTEREST RULES

The Procedure for Conflicts of Interest and Related-Party Transactions with Senior Officers subjects these kinds of conflicts to the same rules of communication, abstention, and transparency.

3. CONFLICTS OF INTEREST BETWEEN THE COMPANY AND SIGNIFICANT SHAREHOLDERS

Transactions between companies forming part of the Group with significant shareholders or shareholders that have proposed the appointment of any of the directors and their respective related persons are dealt with in article 43 of the Regulations of the Board of Directors mentioned in section D.1. They must be carried out on arm's-length conditions and be previously approved by the Board of Directors. Approval by the shareholders at a General Shareholders' Meeting shall be required if the value of the transaction exceeds 10% of the corporate assets. All transactions shall be reported in the *Annual Corporate Governance Report* and in the *Annual Financial Report*.

4. CONFLICTS OF INTEREST WITH OTHER EMPLOYEES

The Code of Ethics, which dedicates a specific section to conflicts of interest, applies to all professionals within the Group, regardless of rank.

D.7. Is more than one company of the group listed in Spain?

Yes ☐ No ☒

Identify the subsidiaries listed in Spain:

Listed subsidiaries

State whether they have publicly and accurately defined their respective areas of activity and any possible business relationships among them, as well as those between the listed dependent company and the other companies within the group:

Yes ☐ No ☐

Describe the possible business relationships between the parent company and the listed subsidiary, and between the subsidiary and the other companies within the group

Identify the mechanisms established to resolve possible conflicts of interest between the listed subsidiary and the other companies within the group:

Mechanisms for the resolution of possible conflicts of interest

E. RISK CONTROL AND MANAGEMENT SYSTEMS

E.1. Explain the scope of the company's Risk Management System, including the system for managing tax risks.

The General Risk Control and Management Policy and the Risk Policies that further develop such risks apply to all companies over which the Company has effective control, within the limits established by the laws applicable to the regulated activities carried out by the Group in the various countries in which it operates.

The General Risk Control and Management Policy and the basic principles underpinning it are implemented by means of a Comprehensive Risk Control and Management System, supported by a Risk Committee of the Group and based upon a proper definition and allocation of duties and responsibilities at the operating level and upon supporting procedures, methodologies, and tools, covering the following stages:

- a) The ongoing identification of significant risks and threats based on their possible impact on key management objectives and the accounts (including contingent liabilities and other off-balance sheet risks).
- b) The analysis of such risks, both at each corporate business or function and taking into account their combined effect on the Group as a whole.
- c) The establishment of a structure of policies, guidelines, and limits, as well as of the corresponding mechanisms for the approval and implementation thereof, which effectively contribute to risk management being performed in accordance with the Company's risk appetite.
- d) The measurement and monitoring of risks, by following consistent procedures and standards that are common to the Group as a whole
- e) The analysis of risks associated with new investments, as an essential element of decision-making based upon profitability/risk.
- f) The maintenance of an internal system for monitoring compliance with policies, guidelines, and limits, by means of appropriate procedures and systems, including the contingency plans needed to mitigate the impact of the materialisation of risks.
- g) The periodic monitoring and control of profit-and-loss account risks in order to control the volatility of the annual income of the Group.
- h) The ongoing evaluation of the suitability and efficiency of applying the system and the best practices and recommendations in the area of risks for eventual inclusion thereof in the model.
- i) The audit of the system by the Internal Audit Division.

Developed in accordance with the following basic action principles:

- a) Integrate the risk/opportunity vision into the Company's management, through a definition of the strategy and the risk appetite and the incorporation of this variable into strategic and operating decisions.
- b) Segregate functions, at the operating level, between risk-taking areas and areas responsible for the analysis, control, and monitoring of such risks, ensuring an appropriate level of independence.
- c) Guarantee the proper use of risk-hedging instruments and the maintenance of records thereof as required by applicable law.
- d) Inform regulatory agencies and the principal external players, in a transparent fashion, regarding the risks facing the Group and the operation of the systems developed to monitor such risks, maintaining suitable channels that favour communication.
- e) Ensure appropriate compliance with the corporate governance rules established by the Company through its Corporate Governance System and the update and continuous improvement of such system within the framework of the best international practices as to transparency and good governance, and implement the monitoring and measurement thereof.
- f) Act at all times in compliance with the law and the Company's Corporate Governance System and, specifically, with due observance of the values and standards of conduct reflected in the Code of Ethics and the principles and good practices reflected in the Corporate Tax Policy, under the principle

of zero tolerance towards the commission of unlawful acts and situations of fraud set forth in the Crime Prevention Policy and in the Anti-Corruption and Anti-Fraud Policy.

Excluded from the scope of this policy are listed country subholding companies and the subsidiaries thereof which, pursuant to their own special framework of strengthened autonomy, have their own risk policies approved by their competent bodies. In any event, said risk policies must be in accord with the principles set forth in this *General Risk Control and Management Policy* and in the other *Risk Policies* of the Company.

At those companies in which the Company has an interest but which do not belong to the Group, the Company shall promote principles, guidelines, and risk limits consistent with those established in the *General Risk Control and Management Policy* and in its supplemental *Risk Policies* and shall maintain appropriate channels of information to ensure a proper understanding of risks.

E.2. Identify the decision-making bodies of the company responsible for preparing and implementing the Risk Management System, including the system for managing tax risks.

The Board of Directors of the Company undertakes to develop all of its capabilities in order for the significant risks to all the activities and businesses of the Group to be adequately identified, measured, managed, and controlled, and establishes through the *General Risk Control and Management Policy* the mechanisms and basic principles for appropriate management of the risk/opportunity ratio, at a risk level that makes it possible to:

- a) attain the strategic objectives formulated by the Group with controlled volatility;
- b) provide the maximum level of assurance to the shareholders;
- c) protect the results and reputation of the Group;
- d) defend the interests of customers, shareholders, other groups interested in the progress of the Company, and society in general; and
- e) ensure corporate stability and financial strength in a sustained fashion over time.

1. BOARD OF DIRECTORS

Within its area of authority, and with the support of the Audit and Risk Supervision Committee, it promotes the implementation of the mechanisms required to ensure the adequate identification, measurement, management, and control of all significant risks, defines the strategy and profile of the Company's risks, including tax risks, and approves the Group's *Risk Policies*.

2. EXECUTIVE COMMITTEE

In order to align the risk impact with the established risk appetite, the Board of Directors, acting at the proposal of the business or corporate divisions involved and upon a prior report from the Group's Risk Committee, annually reviews and approves specific guidelines regarding the risk limits from the Corporate Policies of the Group.

Pursuant to established guidelines, competent management decision-making bodies of the country subholding companies and each of the principal companies of the Group, within their area of responsibility, annually review and approve the specific risk policies and limits applicable to each of them and implement the control systems required to ensure compliance with the *General Risk Control and Management Policy* and with the limits thereunder.

3. AUDIT AND RISK SUPERVISION COMMITTEE

As a consultative body of the Board of Directors, it is charged with the following duties:

- Directly supervise the unit vested with the power to actively participate in the preparation of the Company's risk strategy and in significant decisions affecting the management thereof.
- Continuously review the internal control and risk management systems, such that the principal risks are properly identified, managed, and reported.
- Ensure that the Group's risk control and management system identifies at least:

<ul style="list-style-type: none"> Ø The various risk factors to which the Company is exposed, including contingent liabilities and other off-balance sheet risks among financial, economic, or tax risks; Ø The establishment and review of the risk map and levels that the Company deems acceptable. Ø The measures planned in order to mitigate the impact of identified risks in the event that they materialise. Ø The internal control and reporting systems to be used to control and manage the above risks.
<ul style="list-style-type: none"> - (Specifically in the tax area) Receive from the Company's tax director information on the tax guidelines used by the Company during the financial year and, in particular, on the level of compliance with the <i>Corporate Tax Policy</i>, and report to the Board of Directors on the tax policies applied and, in the case of transactions or matters that must be submitted to the Board of Directors for approval, regarding the tax consequences thereof when such consequences represent a significant issue. - Maintain appropriate relationships with the Risk Division and with the audit and compliance committees of the other companies of the Group. - Report in advance on the risks of the Group to be included in the Company's <i>Annual Corporate Governance Report</i> and give notice thereof to the Board of Directors, through the Corporate Social Responsibility Committee, for an assessment of its conclusions.
<p>4. BOARDS OF DIRECTORS OF COUNTRY SUBHOLDING COMPANIES OF THE PRINCIPAL COUNTRIES IN WHICH THE GROUP OPERATES</p> <p>They are assigned the power to approve the <i>Risk Policies</i> for the various businesses of the Group in the country in question as well as to establish the limits and specific risk indicators applicable to such businesses, based on the nature and unique aspects of each country.</p> <p>5. RISK COMMITTEE OF THE GROUP</p> <p>The Risk Committee of the Iberdrola Group is a technical body chaired by the chief financial officer, and which performs executive duties in connection with customary risk management and gives advice to the Group's governance bodies.</p> <p>The Committee meets, at a minimum, one time per month, with the participation of the Group's director of Risk Management, those responsible for risks at the corporate businesses and areas that have a Risk Management function, the Internal Audit Division, and the Administration and Control Division.</p> <p>The Group's Risk Committee is complemented with the Credit Risk and Market Risk Committees of the Group, which report to said Risk Committee and which meet on a fortnightly and monthly basis, respectively, to discuss and decide on credit and market (financial and commodities) risk issues.</p>

E.3. Point out the principal risks, including tax risks, that could affect the achievement of business goals.

<p>The Group is subject to various risks inherent in the different countries, industries, and markets in which it does business and in the activities it carries out, which may prevent it from achieving its objectives and successfully implementing its strategies.</p> <p>The section entitled "Main risk factors associated with the activities of the Iberdrola Group" of the Management Report within the Annual Report for financial year 2016 provides a detailed description of the principal risks associated with the activities carried out by the main businesses of the Group, as well as the risks of the corporation.</p> <p>Owing to its universal and dynamic nature, the comprehensive risk system allows for the consideration of new risks that may affect the Group following changes in its operating environment or revisions of objectives and strategies, as well as adjustments resulting from ongoing monitoring, verification, review, and supervision activities.</p> <p>Pursuant to the definitions established by the <i>General Risk Control and Management Policy</i>, at the Group level, risks are classified as follows:</p> <p>a) Corporate Governance Risks: the Company accepts the need to achieve the fulfilment of the</p>
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corporate interest and the sustained maximisation of the economic value of the Company and its long-term success, in accordance with the Group's corporate interest, culture, and corporate vision, taking into account the legitimate public and private interests that converge in the conduct of all business activities, particularly those of the various Stakeholders and the communities and regions in which the Company and its employees act. A fundamental requirement for the foregoing is compliance with the Company's Corporate Governance System, made up of the By-Laws, the Corporate Policies, the internal corporate governance rules, and the other internal codes and procedures approved by the competent decision-making bodies of the Company and inspired by the good governance recommendations generally recognised in international markets.

- b) **Market Risks:** defined as the exposure of the Group's results and assets to changes in market prices and variables, such as exchange rates, interest rates, commodity prices (electricity, gas, CO2 emission allowances, other fuel, etc.), prices of financial assets, and others.
- c) **Credit Risks:** defined as the possibility that a counterparty fails to perform its contractual obligations, thus causing an economic or financial loss to the Group. Counterparties can be end customers, counterparties in financial or energy markets, partners, suppliers, or contractors.
- d) **Business Risks:** defined as the uncertainty regarding the performance of key variables inherent in the business, such as the characteristics of demand, weather conditions, the strategies of different players, and others.
- e) **Regulatory and Political Risks:** defined as those arising from regulatory changes made by the various regulators, such as changes in compensation of regulated activities or in the required conditions of supply, or in environmental or tax regulations, including risks relating to political changes that might affect legal security and the legal framework applicable to the businesses of the Group in each jurisdiction, nationalisation or expropriation of assets, the cancellation of operating licences, and the early termination of government contracts.
- f) **Operational, Technological, Environmental, Social, and Legal Risks:** defined as those related to direct or indirect economic losses resulting from inadequate internal procedures, technical failures, human error, or as a consequence of certain external events, including the economic, social, environmental, and reputational impact thereof, as well as legal and fraud risks. Said risks include those associated with information technology and cybersecurity, and with technological obsolescence, among others.
- g) **Reputational Risks:** potential negative impact on the value of the Company as a result of conduct by the company below the expectations created among various Stakeholders, as defined in the Stakeholder Relations Policy.

E.4. Identify whether the entity has a risk tolerance level, including one for tax risk.

The Company's Board of Directors annually reviews and approves the acceptable risk tolerance levels for the Group.

The General Risk Control and Management Policy, together with the specific Risk Policies and limits that develop it, qualitatively and quantitatively establish, in sufficiently detailed form, the risk appetite that is annually accepted both at the Group level and at each of its main businesses.

By way of complement, once such limits and guidelines are considered in order to verify the risk assumed globally in the annual profit and loss account, the Administration and Control Division engages in a comprehensive probability analysis of the remaining global risk for the year at the time of approving the annual budget.

In addition, all new multi-year plans are accompanied by their associated risk analysis.

Corporate risk policies and limits reviewed and approved annually:

- Corporate Credit Risk Policy
- Corporate Market Risk Policy
- Operational Risk in Market Transactions Policy
- Insurance Policy

- Investment Policy
- Financing and Financial Risk Policy
- Treasury Share Policy
- Risk Policy for Equity Interests in Listed Companies
- Reputational Risk Framework Policy
- Procurement Policy
- Information Technologies Policy
- Cybersecurity Risk Policy

Risk policies of the various businesses of the Group reviewed and approved annually:

- Risk Policy for the Liberalised Businesses of the Iberdrola Group
- Risk Policy for the Renewable Energy Businesses of the Iberdrola Group
- Risk Policy for the Networks Businesses of the Iberdrola Group
- Risk Policy for the Engineering and Construction Business
- Risk Policy for the Real Estate Business

In general terms, the Corporate Policies, applicable to all of the Group's businesses, establish the framework and the proper practices for the control, management, and mitigation of the various types of risks and establish overall risk limits to be placed among the various businesses, measured in the form of physical, notional, and/or probability figures (VaR, Profit/Risk, CVaR, etc.), through measures such as:

- Limits on maximum global credit risk exposure by type of counterparty
- Limits to market risk proportional to the volume of activity of each business
- Strict global limit on discretionary energy trading
- Limits on operational risk through preventive maintenance programmes and insurance programmes
- Strict limits on activities not associated with the main energy business
- Other

The *Risk Policies* of each of the main businesses of the Group establish the framework and the authorised activities for each of them, together with the qualitative and quantitative risk guidelines, limits, and indicators that should be applicable thereto, adjusted to the specific nature of each of them.

The *Corporate Tax Policy* establishes the limits on tax risk by setting the tax strategy, principles of conduct, and good tax practices assumed by the Company.

The *General Risk Control and Management Policy*, as well as a summary of the *Corporate Risk Policies* and another summary of the Specific Risk Policies for the Various Businesses of the Group, are available on the corporate website (www.iberdrola.com).

E.5. State what risks, including tax risks, have materialised during the financial year.

The risk factors that materialised in the countries and markets in which Iberdrola does business did not have a significant impact on income for the financial year, thanks to the diversification of activities, markets, and geographical areas of the Group, which made it possible for the negative effects of some businesses to be offset by a favourable performance in others.

Note should be taken of the following positive events that have eliminated risks or threats:

- The improvement of the economic situation in Spain during 2016, with GDP growth of 3.2% and a 1.5 point improvement in the unemployment rate, which has translated into a 0.7% (0% adjusted) growth in electricity demand.
- The approval of Order IET 980/2016 establishing the remuneration of electricity distribution

companies in Spain, which set total remuneration for the Group at 1,655 million euros for 2016 (2.7% above 2015) and a regulated assets base (RAB) for the Group's distribution assets at 8,694 million euros, eliminating the corresponding existing uncertainties in this regard.

- The approval on terms favourable to the Group of the remuneration frameworks (rate cases) of: RG&E and NYSEG by the New York regulator, with a base ROE of 9% beginning July 2016 for a 3-year period; and (ii) UI by the Connecticut regulator, with a base ROE of 9.1% beginning in January 2017 for a 3-year period, which eliminate the main uncertainties relating to the principal network businesses of the Group in the USA for the coming years.
- The publication in the United Kingdom, on terms favourable to the sector, of the final report of the Competition Markets Authority (CMA) on the analysis of the retail gas and electricity market in the United Kingdom, without significant impacts for Scottish Power Ltd.
- The significant recovery during 2016 of international prices for coal (96%), gas (60%) and petroleum (59%), with the resulting positive impact on final electricity prices and increased margin for technologies without a variable cost factor.

Risks that have materialised include:

- The unfavourable evolution of some of the projects of Iberdrola Engineering & Construction, causing a 125 million euro decrease (i.e. 100 million euro decrease after taxes) in the EBITDA contributed by the Business to the Group.
- The tax inspection commenced in 2014 by the National Tax Administration Agency (*Agencia Estatal de Administración Tributaria*) regarding the 2008-2011 Corporate Income Tax of the Iberdrola tax Group, 2010-2011 VAT, and other taxes, ended in 2016 with the signing of assessment instruments with agreement, consent, and disagreement of the taxpayer.

The settlements deriving from assessment instruments with agreement and consent have been paid in 2016 and have not have negative effects on the income statement, because they were provisioned.

The settlements deriving from assessment instruments without consent have been appealed to the Central Administrative Economic Tribunal (*Tribunal Económico Administrativo Central*), and a suspension of payment of the assessed debts has been suspended by means of the provision of corresponding bank guarantees. These settlements have also not had negative effects on the income statement for financial year 2016 because the adjustments made upon the inspection, which were settled as debts to the AEAT by final unfavourable judgement, were provisioned because they were evaluated as being probable. No liabilities additional to those already booked at 31 December 2016 are expected to arise.

Finally, it should be noted that activities in 2017 will be subject to the following risk factors:

- The process of negotiation of the United Kingdom's exit from the European Union and the policies that may be adopted by the new United States administration, together with the uncertainty associated with the electoral processes in France and Germany, may cause financial turbulence in the international financial markets, with an expected increase in volatility in exchange rates (with a risk of depreciation of the pound and the Mexican peso) and increases in interest rates in the United States.
- The possible impact on the Mexican economy of some of the possible new political and economic measures announced during the recent electoral campaign in the United States, such as the possible implementation of customs duty, with a potential decrease in electricity demand by the most affected industries.

The uncertainty associated with the final development of the Mexican electricity reform, and particularly the approval of the CFE's new electricity tariff, the main benchmark for free market energy contracts, to which the Group allocates approximately 20% of its production in Mexico.

- The uncertainty associated with the possible confirmation during 2017 of the improvement in macroeconomic data observed at the end of 2016 in Brazil, after a difficult year politically, characterised by the impeachment of Ms. Rousseff, and economically, in terms of GDP, inflation, and unemployment, translating into a decrease in the demand for electricity from our electricity distribution company Elektro.
- Despite the recovery of raw materials prices stated above, they are at low levels compared to the levels of only a few years ago, and uncertainty persists regarding the future performance thereof.
- In the United States, the progressive increase in exposure to market prices in renewables as a result of the expiration of long-term power purchase agreements (PPAs) within the context of low electricity

prices.

E.6. Explain the plans for responding to and supervising the entity's main risks, including tax risks.

The Comprehensive Risk System, together with the Company's control and management policies and systems that develop it, including the Company's Risk Committee and Operating Committee, have allowed for the identification of new risks and threats sufficiently in advance, and to establish appropriate mitigation plans.

The Company's Operating Committee meets on close to a weekly basis.

The Group's Risk Committee meets on a monthly basis, reviews the various risks, and on a quarterly basis approves a Quarterly Risk Report of the Company, which includes the main risk positions, a report on compliance with policies and limits, and an update of the key risk maps.

The Audit and Risk Supervision Committee of the Board of Directors periodically monitors the evolution of the Company's risks at least on a quarterly basis:

- It reviews the Quarterly Risk Reports of the Group, which include monitoring compliance with risk limits and indicators and updated key risk maps, submitted by the Group's director of Corporate Risks.
- It coordinates and reviews Risk Reports sent periodically (at least half-yearly) by the audit and compliance committees of the country subholding companies and head of business companies of the Group.
- It prepares a Risk Report for the Board of Directors at least half-yearly.

F. INTERNAL RISK CONTROL AND MANAGEMENT SYSTEMS IN CONNECTION WITH THE PROCESS OF ISSUING FINANCIAL INFORMATION (ICFRS)

Describe the mechanisms making up the risk control and management systems with respect to the process of issuing the entity's financial information (ICFRS)

F.1. Control environment at the entity

Indicate at least the following, specifying the main features thereof:

F.1.1. What bodies and/or functions are responsible for: (i) the existence and maintenance of an adequate and effective internal control over financial reporting system (ICFRS); (ii) the implementation thereof; and (iii) oversight thereof.

The Board of Directors has the ultimate responsibility for the existence of an adequate and effective internal control over financial reporting system (ICFRS) lies with the Board of Directors of Iberdrola. The Boards of Directors of the country subholding companies and the head of business companies also have this responsibility within their various purviews.

The persons in charge of the country subholding companies and the head of business companies, together with the respective control officers, as well as the directors of the global corporate areas, are responsible for the design and implementation of the ICFRS. Such responsibility is expressly set forth in the certifications signed by such persons on a half-yearly basis in connection with the financial information for their respective areas of responsibility.

Pursuant to article 26.7.d of the Regulations of the Board of Directors, the Audit and Risk Supervision Committee has the power to monitor the effectiveness of the internal control of the Company and its Group. The Committee draws on the support of the Internal Audit Area Division to discharge such responsibility. Any audit and compliance committees at the country subholding and head of business companies have this power within their respective purviews.

F.1.2. Whether any of the following are in place, particularly as regards the financial information preparation process:

- **Departments and/or mechanisms in charge of: (i) the design and revision of the organisational structure; (ii) clearly defining the lines of responsibility and authority, with an appropriate distribution of work and duties; and (iii) ensuring that there are sufficient procedures for the proper dissemination thereof at the entity.**

The Board of Directors of Iberdrola defines the top-level organisational structure. The heads of such top-level organisations, together with the Human Resources Division, are responsible for deployment within their respective areas.

Each top-level division prepares a proposed organisation structure, including a description of the mission, duties, and responsibilities of the various organisations deployed, which must then be validated by the Human Resources Division and the Finance and Resources Division.

Primary responsibility for the preparation of financial information lies with the corporate Administration and Control Division. This division proposes the structure of those responsible for Control at the country subholding companies and head of business companies and is in charge of coordinating and supervising their activities.

Code of conduct, body that approves it, degree of dissemination and instruction, principles and values included (indicating whether the recording of transactions and the preparation of financial information are specifically mentioned), body in charge of reviewing breaches and of proposing corrective actions and penalties.

The Iberdrola Group has a Code of Ethics, approved by the Board of Directors.

According to article 2.1 thereof, "the principles and guidelines for conduct contained in the Code of Ethics apply to all of the Group's professionals, regardless of seniority, geographic or functional location, or the company of the Group for which they provide their services". The Code of Ethics is communicated to and disseminated among the professionals of the Iberdrola Group in accordance with the plan approved for such purpose by the Compliance Unit.

Article 33 of the Code of Ethics expressly provides as follows:

"The Group shall provide true, proper, useful, and consistent information regarding its programmes and actions. The transparency of the information required to be disclosed is a basic principle that must govern the actions of Group professionals.

The economic/financial information of the Group (especially the annual accounts) shall faithfully reflect its economic and financial position and its net worth, in accordance with generally accepted accounting principles and applicable international financial reporting standards. For such purposes, no professional shall conceal or distort the information set forth in the accounting records and reports of the Group, which shall be complete, accurate, and truthful.

A lack of honesty in the communication of information, whether internally within the Group (to employees, subsidiaries, departments, internal bodies, management decision-making bodies, etc.) or outside the Group (to auditors, shareholders and investors, regulatory entities, the media, etc.), is a breach of the Code of Ethics. This includes delivering incorrect information, organising it in an incorrect manner, or seeking to confuse those who receive it".

Control of the application of the Code of Ethics is a duty of the Compliance Unit, a body linked to the Corporate Social Responsibility Committee of the Company's Board of Directors, with duties in the area of regulatory compliance and the Company's Corporate Governance System. This Unit evaluates and prepares an annual report on the level of compliance with the Code of Ethics. The report is transmitted to the Human Resources Division, to the Company's Internal Audit Area Division, and to the Corporate Social Responsibility Committee. In turn, the latter transmits it to the competent governance bodies, to the Company's chairman & chief executive officer, and to the Audit and Risk Supervision Committee.

The Compliance Unit also has the duty to determine whether a Group professional has conducted activities in violation of the law or of the Code of Ethics and, if applicable, to direct the Human Resources Division, or the Division responsible for the human resources function at the relevant Group company, to apply disciplinary measures in accordance with the rules on breach of duties and penalties contained in the collective bargaining agreement to which the professional belongs or in applicable labour law provisions.

Pursuant to article 44.1 thereof, the professionals of the Group expressly accept the rules of conduct established in the Code of Ethics.

In addition, pursuant to article 44.2, professionals who join or become part of the Group in the future shall expressly accept the principles and rules of conduct set forth in the Code of Ethics, which document shall be attached to their respective employment contracts.

Reporting channel that makes it possible to report any irregularities of a financial or accounting nature to the audit committee, as well as any possible breach of the code of conduct and irregular activities at the organisation, specifying, if appropriate, whether it is confidential.

Iberdrola has a procedure in place that must be followed by all employees of the Group who wish to report potentially significant irregularities of a financial and accounting nature and that allows them to

report such irregularities, by e-mail or regular mail, to the chair of the Audit and Risk Supervision Committee.

As established in the procedure itself, the Company's Board of Directors guarantees that the name of the reporting person and the irregularity reported shall be treated in the strictest confidence, both in the reporting process and in any process for the assessment and clarification of the facts conducted by the Audit and Risk Supervision Committee and the organisations of the Company or third parties participating at the request of such Committee.

In accordance with the above-mentioned procedure, the chair of the Audit and Risk Supervision Committee receives and admits the report for further processing. Such admission is made on the basis of the requirements established in the procedure (name of the sender, sufficiently detailed information on the situation reported, need for the report to fall within the scope of the channel, confidentiality guarantee, personal data protection, etc.).

No reports were received during financial year 2016.

Regular training and update programmes for personnel involved in the preparation and review of financial information, as well as in the evaluation of the internal control over financial reporting system, covering at least accounting standards, auditing, internal control, and risk management.

Personnel involved in the preparation and review of financial information, as well as in the evaluation of the internal control over financial reporting system, receives regular training on accounting standards, auditing, internal control, and risk management, according to its specific responsibilities.

In accordance with the organisational structure of the Iberdrola Group, the divisions that have a direct relationship with these types of duties are the Internal Audit Division, the Administration and Control Division, and the Finance and Resources Division.

During financial year 2016, the personnel involved in these duties in Spain received 19,018 hours of training, of which the training in Spain, Mexico, and at Scottish Power Ltd. are noteworthy and are further described below.

The personnel involved in these duties in Spain received 14,094 hours of training, of which 8,434 hours, organised into 163 training activities, were dedicated to technical training directly related to the responsibilities discharged by such personnel, which accounts for 60% of the training they receive, with 511 professionals participating in these courses. There were 3,325 total hours of training at Scottish Power Ltd.

There were 1,463 total hours of training in Mexico, of which 925 hours were for specific technical training, organised into 11 training activities.

The rest of the training hours were carried out by personnel of these organisations at Elektro and Avangrid, Inc. (United States).

Most of these courses are provided by external entities: business schools, universities, or consulting firms specialising in economic/financial issues.

Especially noteworthy is the receipt of various professional certificates by Iberdrola professionals in these functional areas:

- "Certified Internal Auditor (CIA), by two professionals in Spain and two at Avangrid.
- "Certified Internal Auditor" (CISA), by one professional in Spain and two at Avangrid.
- "Certified Fraud Examiner" (CFE), "Certification in Risk Management Assurance" (CRMA) and "Certified Public Accountant" (CPA) by 7 professionals at Avangrid.

The technical training activities in which these professionals engaged include:

- Advanced bank risk analysis
- Advanced business financial analysis
- Payment approvers

- Audit of investments
- NST bank reconciliation
- Treasury reconciliation
- Risk analysis and management practical course
- Excel - financial management applications
- Taxes
- Treasury management
- Value added tax
- Equity and consolidation method of financial statements
- New EU customs code
- Payment requests
- Executive risk management programme
- Reb book legality of Streetworks/permits
- Reform of General Tax Law and New Issues
- Internal Regulations for Conduct in Securities Markets
- ERM System at Insurance Company
- Valuation of financial rate swaps
- Capacity Mechanism
- Graduate First Day Induction
- Issue and/or Receive Safety Documentation
- Red Book Legality of Streetworks/Permits
- Trainee – Electrical Networks Aprec

Generally, these professionals have also taken courses to improve their qualifications in the use of the office automation tools required to perform their duties, mainly Excel.

It should be noted that several international meetings were organised during 2016 among the professionals in these areas, like the X Global Internal Audit Days.

F.2 Risk assessment of financial information

Indicate at least the following:

F.2.1. What are the main features of the risk identification process, including the process of identifying the risks of error or fraud, with respect to:

- Whether the process exists and is documented.

The process for the identification of risks of error in financial information is one of the most important steps in the method for the development of internal control of the financial information of Iberdrola, and the goals, implementation, and results thereof are documented.

The method starts with a review of the consolidated financial information of the Iberdrola Group and of the various country subholding companies in order to select the most significant accounts and notes to the accounts, in accordance with both quantitative (materiality) and qualitative (business risk and visibility to third parties) standards. The selected accounts and notes are grouped into management cycles or large processes in which the selected information is generated. The cycles are analysed and a description of

each is prepared, as a way of identifying possible risks of error in the financial information, in connection with attributes such as completeness, presentation, assessment, cut-off, recording, and validity. The identified risks are submitted to a process of prioritisation, such that the most significant ones are selected by applying professional judgement on a number of indicators (existence of documented processes and controls, existence of systems that automate the processes, whether there have been any incidents in the past, whether the process is known and mature, or whether judgements need to be made to make estimates). The risks of fraud are not explicitly identified, although they are taken into account to the extent that they might generate material errors in financial information.

Once the most significant risks have been selected, the controls needed to mitigate or manage them are selected and designed; such controls are monitored, documented, and systematically reviewed by the Internal Audit Area.

The risks selected are reviewed at least on an annual basis, within the framework of the assessment of the effectiveness of internal control carried out by the persons or divisions responsible therefor. The purpose of such review is to adjust the risks to the changing circumstances in which the Company operates, particularly in the event of changes in the organisation, information technology systems, regulations, products, or the situation of the markets.

- **Whether the process covers all the objectives of financial information (existence and occurrence; completeness; assessment; presentation, breakdown and comparability, and rights and obligations), whether it is updated, and how often.**

As mentioned above, the cycles or large processes in which financial information is generated are reviewed at least on an annual basis in order to identify possible risks of error, in connection with attributes such as validity (existence and authorisation), completeness, assessment, presentation, cut-off, and recording.

- **The existence of a process for the identification of the scope of consolidation, taking into account, among other matters, the possible existence of complex corporate structures, holding entities, or special purpose entities.**

The scope of consolidation is identified on a monthly basis, and the result thereof is the updated corporate map, which expressly identifies the changes that occurred in each period.

This review covers all companies in which Iberdrola or any of its subsidiaries has an interest, no matter how small.

In accordance with the provisions of section 529 of the Companies Act, the Regulations of the Board of Directors provide that the Board of Directors has the power to, among other things, approve the creation or acquisition of equity interests in special purpose entities ("SPEs") or entities registered in countries or territories that are considered to be tax havens ("THEs"), as well as any other transactions or operations of a similar nature that, due to their complexity, might diminish the transparency of the Group.

In accordance with the same law, the Regulations of the Audit and Risk Supervision Committee of Iberdrola provide that the Audit Committee must report to the Board of Directors prior to such decisions being adopted on the creation or acquisition of said entities.

Accordingly, whenever the Company intends to create a special purpose entity or an entity registered in a tax haven, or to acquire an interest in one, the transaction requires a favourable report of the Audit and Risk Supervision Committee and subsequent approval of the Board of Directors.

There are specific procedures for such purpose, tailored to the current corporate governance model, according to which such initiative is to be taken by the Division of the Group or country subholding company, head of business company, or company in which an interest is held through them, that intends to create or acquire a special purpose company or a company registered in a tax haven. In the case of companies that have a board of directors and an audit committee, their corporate governance bodies must first review the proposed transaction.

- **Whether the process takes into account the effects of other types of risks (operational, technological, financial, legal, tax, reputational, environmental, etc.) to the extent that they affect the financial statements.**

The process for the identification of risks of error in financial information takes into account the effects of other types of risks (operational, technological, legal, tax, reputational, environmental, etc.) to the extent that they affect the accounts; such risks are assessed and managed by different corporate units such as the Risk Division or Legal Services, among others. However, no express identification of such other types of risks is carried out to identify financial information risks.

- **What governance body of the entity supervises the process.**

The governance body that supervises the process is the Audit and Risk Supervision Committee, which draws on the support of the Internal Audit Area Division to discharge this responsibility.

F.3. Control activities

Indicate whether at least the following are in place and describe their main features:

- F.3.1. Procedures for review and authorisation of financial information, and description of the internal control over financial reporting system to be published in the securities market, indicating the persons or divisions responsible therefor, as well as documentation describing the flows of activities and controls (including those relating to risk of fraud) of the various types of transactions that could materially affect the financial statements, including the closing process and the specific review of significant judgements, estimates, assessments, and projections.**

The process or structure of certification of financial information, conducted formally on a half-yearly basis, on the dates of the year-end and interim closing processes, reflects the manner in which financial information is generated in the Group.

In such structure, the persons in charge of the country subholding companies and those responsible for the head of business companies, together with the respective directors of control, and the heads of the global corporate areas, certify both the reliability of the financial information in the areas under their responsibility (which is the information they provide for purposes of consolidation at the Group level) and the effectiveness of the internal control system established to reasonably ensure such reliability. Finally, the chairman & chief executive officer, as the highest executive authority, and the director of Administration and Control, as the person responsible for the preparation of financial information, certify the reliability of the consolidated accounts to the Board of Directors.

The Audit and Risk Supervision Committee, with the support of the Internal Audit Area Division, supervises the entire certification process, and submits the conclusions of such review to the Board of Directors at the meetings at which the accounts are formally approved.

As regards the description of the internal control over financial reporting system (ICFRS) to be published in the securities markets, the review and authorisation procedure is the same as that used for all contents of an economic and financial nature of the Annual Corporate Governance Report.

The documentation of the internal control over financial reporting system includes high-level descriptions of the cycles of generation of selected significant financial information, as well as detailed descriptions of the prioritised risks of error and of the controls designed to mitigate or manage them. The description of

the controls includes the evidence to be obtained in the implementation thereof, which is necessary for its review.

Each of the closing processes performed at the business units is regarded as a cycle, and the same is true of all the closing activities performed at the corporate level, of the global consolidation process, and of the process for preparation of the notes to the accounts. As a result, all such activities are subject to the methodological process described in the section relating to risks.

The specific review of critical accounting judgements and significant estimates, assessments, and projections is subject to specific controls within the model, since this type of matter entails the identification of risks of error in the different cycles in which they are made. In many cases, the evidence of such specific controls is the media supporting such reviews.

Independently of the certification process followed in the countries, businesses, and corporate areas, the Audit and Risk Supervision Committee, again with the support of the Internal Audit Division, performs an overall review of financial information on a quarterly basis, ensuring that the half-yearly financial reports and the quarterly management statements are prepared using the same accounting standards as the annual financial reports, verifying the proper delimitation of the scope of consolidation as well as the proper application of generally accepted accounting principles and international financial reporting standards.

F.3.2. Policies and procedures of internal control over reporting systems (including, among others, security of access, control of changes, operation thereof, operational continuity, and segregation of duties) that provide support for the significant processes of the entity in connection with the preparation and publication of financial information.

The controls used to mitigate or manage the risks of error in financial information include controls relating to the most significant computer applications, such as controls of user access permissions or of the integrity of the transfer of information between applications, the transaction, and change management.

In addition, the Iberdrola Group has guidelines or regulations as well as procedures for internal control over reporting systems in connection with software acquisition and development, the acquisition of system infrastructure, software installation and testing, change management, service level management, management of the services provided by third parties, system security and access thereto, management of incidents, operation management, continuity of operations, and segregation of duties.

Such guidelines and procedures (which, in some cases, differ according to geographical area or type of solution and are in the process of progressive standardisation) are applied across all information systems supporting significant financial information generation processes, and on the infrastructure required for the operation thereof.

The Iberdrola Group also has an Information Technology Policy that contemplates the management of risks associated with the use, ownership, operation, participation, influence, and adoption of specific information technology, and the processes for the management and control thereof.

This provides a general controls model integrated with the risk management model that allows for a global evaluation of the risks relating to information technology.

This model includes a periodic evaluation of the effectiveness of the controls on information technologies implemented in the area of the financial systems, adopting the appropriate measures if any incident is detected.

The Systems director of Iberdrola certifies the effectiveness of the internal controls established on information systems on an annual basis.

F.3.3. Internal control policies and procedures designed to supervise the management of activities outsourced to third parties, as well as those aspects of assessment, calculation, or valuation entrusted to independent experts, which may materially affect the accounts.

Generally speaking, the Iberdrola Group has no significant duties outsourced to third parties that have a direct impact on financial information. The assessments, calculations, or valuations entrusted to third parties that may materially affect the accounts are regarded as significant financial information generating activities that lead, if appropriate, to the identification of high-priority risks of error, which, in turn, entails the design of associated internal controls. Such controls cover the review and internal approval of the basic assumptions to be used, as well as the review of the assessments, calculations, or valuations made by outside parties, by verifying them against calculations made internally.

F.4. Information and communication

Indicate whether at least the following are in place and describe their main features:

F.4.1. A specific function charged with defining and updating accounting policies (accounting policy area or department) and with resolving questions or conflicts arising from the interpretation thereof, maintaining fluid communications with those responsible for operations at the organisation, as well as an updated accounting policy manual that has been communicated to the units through which the entity operates.

The Accounting Regulations Division, reporting directly to the director of Administration and Control, is responsible for defining and updating accounting policies, as well as for resolving questions or conflicts stemming from the interpretation thereof. It maintains fluid communications with those responsible for the operation of the organisation and, especially, with those responsible for accounting functions. It publishes a quarterly newsletter, widely disseminated within the Group, on new accounting developments in connection with IFRS, which includes regulation updates (laws and regulations that come into force, drafts issued, laws and regulations enacted, laws approved and pending approval by the European Union, and expected future laws and regulations) as well as accounting questions asked internally, together with the conclusions in respect thereof.

The Accounting Regulations Division is also responsible for continuously updating the Group's accounting practices manual and for the appropriate dissemination thereof.

The accounting manual is updated continuously. For this purpose, the Accounting Regulations Division analyses whether new developments or changes in accounting matters have an effect on the Group's accounting policies, as well as the effective date of each of such laws or regulations. When a new law or regulation, or interpretation thereof, is identified as having an effect on the Group's accounting policies, it is included in the manual and is also communicated to those responsible for preparing the Group's financial information by means of the quarterly newsletters mentioned above, and there is an update of the application in which the manual is maintained.

The updated version of the manual is available in an application on the Group's internal network. This application is also accessible by VPN over the internet and can be linked to e-mail. Any change or the inclusion of a document within the manual generates a notice by e-mail to all users.

F.4.2. Mechanisms to capture and prepare financial information with standardised formats, to be applied and used by all units of the entity or the group, supporting the principal accounts and the notes thereto, as well as the information provided on the internal control over financial reporting system.

The mechanism to capture and prepare the information supporting the principal accounts of the Iberdrola Group is based primarily on the use of a unified management consolidation tool (known as BPC) accessible from all geographical areas, currently deployed across the entire Group.

A large portion of the information supporting the breakdowns in and notes to the financial information is included in the consolidation tool, and the rest is captured on standardised spreadsheets known as reporting packages, which are prepared for the half-year and year-end closing processes.

F.5. Supervision of the operation of the system

Indicate and describe the main features of at least the following:

F.5.1. The activities of supervision of the internal control over financial reporting system (ICFRS) performed by the audit committee, as well as whether the entity has an internal audit function whose duties include providing support to the committee in its work of supervising the internal control system, including the internal control over financial reporting system. Information is also to be provided concerning the scope of the assessment of the internal control over financial reporting system performed during the financial year and on the procedure whereby the person or division charged with performing the assessment reports the results thereof, whether the entity has an action plan in place describing possible corrective measures, and whether the impact thereof on financial information has been considered.

The activities of supervision of the internal control over financial reporting system carried out by the Audit and Risk Supervision Committee include basically: (i) monitoring compliance with the certification process by the various persons or divisions responsible for financial information, (ii) reviewing the design and operation of the internal control system, with the support of the Internal Audit Area Division, to assess the effectiveness thereof, and (iii) periodic meetings with external auditors, internal auditors, and senior management to review, analyse, and discuss financial information, the group companies covered, and the accounting standards applied, as well as, where appropriate, the significant internal control weaknesses detected.

It should be noted that on an annual basis, those responsible for the preparation of the financial information of each country subholding company, each head of business company, and each corporate area carry out a review of the design and operation of the internal control system within their area of responsibility in order to assess the effectiveness thereof, in a process coordinated by the Internal Control Division.

To that end, an analysis is made of whether, as a result of the changing circumstances in which the Group operates (changes in organisation, systems, processes, products, regulation, etc.), changes in identified risks need to be included and prioritised. A review is also made of whether the design of the controls to mitigate or manage the risks that may have changed is appropriate, as well as whether the controls have functioned properly, in accordance with their design.

The conclusions of this annual review, both as regards the deficiencies detected (which are classified as serious, medium, or slight, according precisely to their possible impact on financial information) and with respect to the action plans to correct them, are submitted at an annual seminar session chaired by the director of Administration and Control, at which the Internal Audit Area Division is also in attendance. At such meeting, conclusions are reached concerning the effectiveness of the internal control system at each of the different areas for which they are responsible and, overall, at the Group as a whole.

The most significant conclusions of the review performed are subsequently submitted to the Audit and Risk Supervision Committee within the framework of the periodic meetings with the director of Administration and Control.

Independently of the foregoing, the Internal Audit Area (which reports to the chairman & chief executive officer and is functionally controlled by the Audit and Risk Supervision Committee, and which, as provided in the Basic Internal Audit Regulations of Iberdrola, S.A. and the Companies of its Group, has the primary roles of working with the Audit and Risk Supervision Committee to further develop the powers thereof and to proactively ensure the proper operation of the information technology, internal control, and risk

management systems of the Company), conducts an independent review of the design and operation of the internal control system in support of said Committee, identifies deficiencies, and draws up recommendations for improvement.

As a result thereof, the Internal Audit Area Division continuously monitors the various action plans agreed with the different organisations to correct the deficiencies detected and to implement the suggestions for improvement agreed with the organisations.

The period that the Internal Audit Area Division plans for an in-depth review of the entire internal control system is three years.

Specifically, during financial year 2016, more than 50 cycles corresponding to the companies Avangrid, Inc., Scottish Power, Ltd., Iberdrola España, S.A., Iberdrola México, S.A. de C.V., Elektro Redes, S.A, and Iberdrola Inmobiliaria, S.A. were reviewed, as was the Human Resources corporate management.

In addition, the Internal Audit Area Division performs a review of the operation of the internal controls regarded as most critical on a half-yearly basis, on the dates of the half-year and year-end closing.

The combination of the three-year reviews and the half-yearly reviews of the most critical controls enables the Internal Audit Area Division to perform an assessment of the internal control system, as regards the design and operation thereof, and to issue an opinion on the effectiveness of the internal controls established to ensure the reliability of financial information, which it submits to the Audit and Risk Supervision Committee within the framework of their periodic meetings.

F.5.2. Whether it has a discussion procedure whereby the auditor (as provided in the Technical Auditing Standards), the internal audit function, and other experts can inform senior management and the audit committee or the directors of the entity of the significant internal control weaknesses detected during the review of the annual accounts or such other reviews as may have been entrusted to them. Information shall also be provided on whether it has an action plan to seek to correct or mitigate the weaknesses found.

Generally speaking, the procedure for discussion of significant internal control weaknesses detected is based on periodic meetings of the various agents.

Thus, the Audit and Risk Supervision Committee holds meetings, both at the half-year and at the year-end closing, with the external auditors, the internal auditors, and the division responsible for preparing financial information, in order to discuss any significant aspect of the preparation process and of the resulting financial information.

Specifically, pursuant to the provisions of its Regulations (scope of authority), the Audit and Risk Supervision Committee of Iberdrola has, among other duties, the duty of reviewing, together with the auditors, the significant weaknesses of the internal control system detected in the course of the audit. To such end, the auditor appears before such Committee on an annual basis to submit recommendations in connection with the internal control weaknesses identified during the review of the accounts. Any weaknesses described by the auditor are monitored on an ongoing basis by the Committee, with the support of the Internal Audit Area Division. The auditors did not highlight any significant internal control weaknesses during financial year 2016.

Furthermore, the division responsible for preparing the consolidated accounts also holds meetings with the external auditors and with the internal auditors, both at the half-year and at the year-end closing, to discuss significant issues relating to financial information.

F.6. Other significant information.

Iberdrola has an internal model or system for control over financial reporting, the purpose of which is to reasonably ensure the reliability of the financial information. It is important to note that the development of this model, which commenced in 2006, was not the product of a legal requirement, but rather derived

from the firm belief of both the Board of Directors and the senior management of the Company that in a context of growth and internationalisation as the one that could already be envisaged for the Group, an explicit and auditable internal control system would contribute to maintaining and improving its control environment and the quality of financial information; it would also boost investors' trust because of its effects on the transparency, reputation, and good governance of Iberdrola and of the subsidiaries making up the Iberdrola Group.

The Internal Control over Financial Reporting Model or System (ICFRS) of the Iberdrola Group rests on two main pillars: certification and internal control proper.

Certification is a half-yearly process in which those responsible for financial information in the different areas of the Company certify that: (i) the financial information they deliver to Iberdrola for purposes of consolidation does not contain any material errors or omissions and provides a fair view of the results and the financial condition within their area of responsibility, and (ii) they are responsible for establishing the ICFRS within their area of responsibility and have found, upon evaluation, that the system is effective. The text of these certifications is inspired by the form of certification established in section 302 of the U.S. Sarbanes-Oxley Act.

The culmination of the half-yearly process is a joint certification that the chairman & chief executive officer and the director of Administration and Control submit to the Board of Directors.

The other pillar supporting this model, i.e. internal control proper, is patterned on the reference framework described in the report entitled "Internal Control Integrated Framework" of the Committee of Sponsoring Organisations of the Treadway Commission (COSO), and is primarily aimed at providing a reasonable level of security in achieving the aim of reliability of the financial information.

The methodology used by Iberdrola for the development and continuous update of internal control consists of the following stages or steps: (i) analysis and selection of significant financial information, (ii) grouping such information into cycles or large processes in which it is generated, (iii) identification, assessment, and prioritisation of risks of error in financial information within selected cycles, (iv) design and operation of controls in order to mitigate or manage selected risks, and (v) monitoring and update of the previous steps in order to continuously adapt the model to the circumstances of corporate activities.

One of the salient features of the design of this model is that it seeks to guarantee the quality of financial information during all months of the year, such that it is not limited only to the periods of year-end or half-year closings.

This feature is strengthened through the use of a specific software application developed in-house by the Group that allows for monitoring of the status of controls at all times.

Another important feature of the model is that it extends the culture of internal control to all of the organisations, both corporate and business, that significantly contribute to generating financial information, by assigning personal responsibility for the implementation and documentation of controls.

All relevant documents in connection with Iberdrola's ICFRS, both regarding the certification process and internal control proper, are contained in the aforementioned computer application.

Those responsible for implementing the controls enter into the computer application evidence of such controls having been performed, and then evaluate the results obtained, which they rate as satisfactory or non-satisfactory. This allows for the internal control situation to be monitored in real time, and also makes it possible to act promptly on any deficiencies detected.

In addition, those responsible for control at the country subholding and business subholding companies, as well as those responsible for the corporate areas, carry out an annual review of the design and operation of the SCIIF, as a systematic process for updating such model in order to adapt it to the changing circumstances of corporate activities.

The annual review is coordinated by the Internal Control Division, which is also responsible for managing the computer application and coordinating the development of the ICFRS in the various business units and corporate areas of the Group.

Moreover, the Internal Audit Area Division, which is responsible for supervising internal control as part of its duty of support of the Audit and Risk Supervision Committee, performs an independent review of the design and operation of the ICFRS, identifying deficiencies and formulating recommendations for improvement. Such review is carried out in accordance with an established policy of rotation among the different cycles within the model over a period of three years.

The Internal Audit Area Division also performs a half-yearly independent review of the effectiveness of the internal controls established to guarantee the reliability of financial information. It also reviews the process

for certification of financial information on a half-yearly basis. The conclusions of such reviews are submitted to the Audit and Risk Supervision Committee, which, if appropriate, adopts such conclusions and submits them in turn to the Board of Directors.

The current scope of the ICFRS is such that, based on materiality standards, it covers the entire Iberdrola Group. At present, more than 1,000 persons within the Group use the software application, both to document evidence of the performance of more than 2,300 controls (which mitigate or manage more than 900 risks of error in financial information that have been prioritised) and to monitor, analyse, adjust, and assess the ICFRS.

Furthermore, approximately 70 officers who participate in the process of certification of the accuracy of information under their responsibility do so by using an electronic signature directly on the computer application.

As a consequence of all of the foregoing, the final result of the certification process, which is based on the situation of internal control proper, can be reviewed by the Board of Directors of Iberdrola as one of the significant guarantees of reliability in connection with the preparation of the Group's annual and interim financial information.

F.7 External audit report

Report on:

F.7.1. Whether the information on the internal control over financial reporting system has been reviewed by the external auditor, in which case the entity should include the respective report as an exhibit. Otherwise, it should provide the reasons therefor.

The information on the internal control over financial reporting system sent to the markets has not been reviewed by the external auditor for reasons of consistency with the fact that the rest of the information set forth in the Annual Corporate Governance Report is only reviewed by the auditor in connection with the accounting information contained in said Report. It is also believed that having the information on the internal control over financial reporting system reviewed externally would in a certain manner overlap the internal control review to be performed by the external auditor, according to technical auditing standards, within the context of the audit of the accounts.

G. DEGREE TO WHICH CORPORATE GOVERNANCE RECOMMENDATIONS ARE FOLLOWED

State the company's degree of compliance with the recommendations of the Good Governance Code of Listed Companies.

If the company does not comply with any recommendation or follows it partially, there must be a detailed explanation of the reasons providing shareholders, investors, and the market in general with sufficient information to assess the company's course of action. Generalised explanations will not be acceptable.

1. The bylaws of listed companies should not place an upper limit on the votes that can be cast by a single shareholder, or impose other obstacles to the takeover of the company by means of share purchases on the market

Complies ☐ Explain ☒

Article 29.2 of the By-Laws provides that "No shareholder may cast a number of votes greater than those corresponding to shares representing ten (10%) per cent of share capital, even if the number of shares held exceeds such percentage of the share capital. This limitation does not affect votes corresponding to shares with respect to which a shareholder is holding a proxy as a result of the provisions of article 23 above, provided, however, that with respect to the number of votes corresponding to the shares of each shareholder represented by proxy, the limitation set forth above shall apply".

Section 3 of such article adds: "The limitation set forth in the preceding section shall also apply to the maximum number of votes that may be collectively or individually cast by two or more shareholders that are entities or companies belonging to the same group. Such limitation shall also apply to the number of votes that may be cast collectively or individually by an individual and the shareholder entity, entities, or companies controlled by such individual. A group shall be deemed to exist under the circumstances provided by law, and also when a person controls one or more entities or companies".

Iberdrola believes that the limitation on the maximum number of votes that may be cast by a single shareholder, or by several shareholders belonging to the same group or, if applicable, acting in concert, is a measure to protect the many minority shareholders, whose investment is thus guarded from any transaction that is contrary to the corporate interest of Iberdrola. In this regard, it should be noted that approximately one-fourth of Iberdrola's capital is held by retail investors, who thus have little room to manoeuvre and respond to a possible influence-seeking shareholder that owns a non-controlling interest and does not reach the threshold requiring a takeover bid, and whose interest is not totally in line with the corporate interest.

It should also be noted that such voting limitation has been in effect since 16 June 1990, the date on which the General Shareholders' Meeting was held at which it was resolved, by unanimous vote of the attendees, to bring the By-Laws of the Company (then doing business as Iberduero, S.A.) into line with the restated text of the Companies Act approved by Royal Legislative Decree 1564/1989 of 22 December. This shows the level of corporate consensus that has existed on such voting limitation from the very beginning, which has been confirmed by the fact that such limitation has remained unchanged through various by-law amendments passed by the shareholders at General Shareholders' Meetings. In turn, it reflects the will of the shareholders to increase their bargaining power in the event of hostile offers or transactions.

In any event, article 50 of the current By-Laws establishes the instances of removal of such voting limitation in the event that the Company is the target of a takeover bid that receives the required shareholder approval, in which case the provisions of section 527 of the Companies Act prevail. Pursuant to the foregoing, it cannot be deemed that the limitation on the maximum number of votes that may be cast by a shareholder constitutes an obstacle to a takeover bid.

2. When a dominant and subsidiary company are both listed, they should provide detailed disclosure on:

a) The activity they engage in and any business dealings between them, as well as between the listed subsidiary and other group companies.

b) The mechanisms in place to resolve possible conflicts of interest.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

3. During the annual general meeting the chairman of the board should verbally inform shareholders in sufficient detail of the most relevant aspects of the company's corporate governance, supplementing the written information circulated in the annual corporate governance report. In particular:

a) Changes taking place since the previous annual general meeting.

b) The specific reasons for the company not following a given Good Governance Code recommendation, and any alternative procedures followed in its stead.

Complies ☐ Complies in part ☒ Explain ☐

Iberdrola is a very proactive company in maintaining direct contact with its shareholders.

As reported in the Engagement Report, the contact occurs throughout the year, beyond just the holding of the General Shareholders' Meeting. Within this context, the communication is bilateral and with all types of shareholders: institutional, retail, domestic, and foreign. The Engagement Report sets out the various channels used for these purposes.

These encounters are reported with a description of Iberdrola's practices and new techniques. This also includes the level of compliance with the recommendations of the Good Governance Code of Listed Companies.

The chairman's speech at the 2016 General Shareholders' Meeting covered various topics, including the Company's corporate governance. A general reference was made to the level of compliance with the Good Governance Code of Listed Companies, with special emphasis on the explanation for non-compliance with recommendation 1, as it is a key element in the Company's corporate governance strategy.

4. The company should draw up and implement a policy of communication and contacts with shareholders, institutional investors and proxy advisors that complies in full with market abuse regulations and accords equitable treatment to shareholders in the same position.

This policy should be disclosed on the company's website, complete with details of how it has been put into practice and the identities of the relevant interlocutors or those charged with its implementation.

Complies ☒ Complies in part ☐ Explain ☐

5. The board of directors should not make a proposal to the general meeting for the delegation of powers to issue shares or convertible securities without pre-emptive subscription rights for an amount exceeding 20% of capital at the time of such delegation.

When a board approves the issuance of shares or convertible securities without pre-emptive subscription rights, the company should immediately post a report on its website explaining the exclusion as envisaged in company legislation.

Complies ☒ Complies in part ☐ Explain ☐

6. Listed companies drawing up the following reports on a voluntary or compulsory basis should publish them on their website well in advance of the annual general meeting, even if their distribution is not obligatory.

a) Report on auditor independence.

b) Reviews of the operation of the audit committee and the nomination and remuneration committee.

c) Audit committee report on third-party transactions.

d) Report on the corporate social responsibility policy.

Complies ☒ Complies in part ☐ Explain ☐

7. The committee should broadcast its general meetings live on the corporate website.

Complies ☒ Explain ☐

8. The audit committee should strive to ensure that the board of directors can present the company's accounts to the general meeting without limitations or qualifications in the auditor's report. In the exceptional case that qualifications exist, both the chairman of the audit committee and the auditors should give a clear account to shareholders of their scope and content.

Complies ☒ Complies in part ☐ Explain ☐

9. The company should disclose its conditions and procedures for admitting share ownership, the right to attend general meetings and the exercise or delegation of voting rights, and display them permanently on its website.

Such conditions and procedures should encourage shareholders to attend and exercise their rights and be applied in a non-discriminatory manner.

Complies ☒ Complies in part ☐ Explain ☐

10. When an accredited shareholder exercises the right to supplement the agenda or submit new proposals prior to the general meeting, the company should:

a) Immediately circulate the supplementary items and new proposals.

b) Disclose the model of attendance card or proxy appointment or remote voting form duly modified so that new agenda items and alternative proposals can be voted on in the same terms as those submitted by the board of directors.

c) Put all these items or alternative proposals to the vote applying the same voting rules as for those submitted by the board of directors, with particular regard to presumptions or deductions about the direction of votes.

d) After the general meeting, disclose the breakdown of votes on such supplementary items or alternative proposals.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

11. In the event that a company plans to pay for attendance at the general meeting, it should first establish a general, long-term policy in this respect.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

12. The board of directors should perform its duties with unity of purpose and independent judgement, according the same treatment to all shareholders in the same position. It should be guided at all times by the company's best interest, understood as the creation of a profitable business that promotes its sustainable success over time, while maximising its economic value.

In pursuing the corporate interest, it should not only abide by laws and regulations and conduct itself according to principles of good faith, ethics and respect for commonly accepted customs and good practices, but also strive to reconcile its own interests with the legitimate interests of its employees, suppliers, clients and other stakeholders, as well as with the impact of its activities on the broader community and the natural environment.

Complies ☒ Complies in part ☐ Explain ☐

13. The board of directors should have an optimal size to promote its efficient functioning and maximise participation. The recommended range is accordingly between five and fifteen members.

Complies ☒ Explain ☐

14. The board of directors should approve a director selection policy that:

a) Is concrete and verifiable.

b) Ensures that appointment or re-election proposals are based on a prior analysis of the board's needs.

c) Favours a diversity of knowledge, experience and gender.

The results of the prior analysis of board needs should be written up in the nomination committee's explanatory report, to be published when the general meeting is convened that will ratify the appointment and re-election of each director.

The director selection policy should pursue the goal of having at least 30% of total board places occupied by women directors before the year 2020.

The nomination committee should run an annual check on compliance with the director selection policy and set out its findings in the annual corporate governance report.

Complies ☒ Complies in part ☐ Explain ☐

15. Proprietary and independent directors should constitute an ample majority on the board of directors, while the number of executive directors should be the minimum practical bearing in mind the complexity of the corporate group and the ownership interests they control.

Complies ☒ Complies in part ☐ Explain ☐

16. The percentage of proprietary directors out of all non-executive directors should be no greater than the proportion between the ownership stake of the shareholders they represent and the remainder of the company's capital.

This criterion can be relaxed:

- a) In large cap companies where few or no equity stakes attain the legal threshold for significant shareholdings.
- b) In companies with a plurality of shareholders represented on the board but not otherwise related.

Complies ☒ Explain ☐

17. Independent directors should be at least half of all board members.

However, when the company does not have a large market capitalisation, or when a large cap company has shareholders individually or concertedly controlling over 30 percent of capital, independent directors should occupy, at least, a third of board places.

Complies ☒ Explain ☐

18. Companies should disclose the following director particulars on their websites and keep them regularly updated:

- a) Professional profile and biographical data.
- b) Directorships held in other companies, listed or otherwise, and other paid activities they engage in, of whatever nature.
- c) Statement of the director class to which they belong, in the case of proprietary directors indicating the shareholder they represent or have links with.
- d) Dates of their first appointment as a board member and subsequent re-elections.
- e) Shares held in the company, and any options on the same.

Complies ☒ Complies in part ☐ Explain ☐

19. Following verification by the nomination committee, the annual corporate governance report should disclose the reasons for the appointment of proprietary directors at the urging of shareholders controlling less than 3 percent of capital; and

explain any rejection of a formal request for a board place from shareholders whose equity stake is equal to or greater than that of others applying successfully for a proprietary directorship.

Complies ☐ Complies in part ☐ Explain ☐ Not applicable ☒

20. Proprietary directors should resign when the shareholders they represent dispose of their ownership interest in its entirety. If such shareholders reduce their stakes, thereby losing some of their entitlement to proprietary directors, the latter's number should be reduced accordingly.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

21. The board of directors should not propose the removal of independent directors before the expiry of their tenure as mandated by the bylaws, except where they find just cause, based on a proposal from the nomination committee. In particular, just cause will be presumed when directors take up new posts or responsibilities that prevent them allocating sufficient time to the work of a board member, or are in breach of their fiduciary duties or come under one of the disqualifying grounds for classification as independent enumerated in the applicable legislation.

The removal of independent directors may also be proposed when a takeover bid, merger or similar corporate transaction alters the company's capital structure, provided the changes in board membership ensue from the proportionality criterion set out in recommendation 16.

Complies ☒ Explain ☐

22. Companies should establish rules obliging directors to disclose any circumstance that might harm the organisation's name or reputation, tendering their resignation as the case may be, and, in particular, to inform the board of any criminal charges brought against them and the progress of any subsequent trial.

The moment a director is indicted or tried for any of the offences stated in company legislation, the board of directors should open an investigation and, in light of the particular circumstances, decide whether or not he or she should be called on to resign. The board should give a reasoned account of all such determinations in the annual corporate governance report.

Complies ☒ Complies in part ☐ Explain ☐

23. Directors should express their clear opposition when they feel a proposal submitted for the board's approval might damage the corporate interest. In particular, independents and other directors not subject to potential conflicts of interest should strenuously challenge any decision that could harm the interests of shareholders lacking board representation.

When the board makes material or reiterated decisions about which a director has expressed serious reservations, then he or she must draw the pertinent conclusions. Directors resigning for such causes should set out their reasons in the letter referred to in the next recommendation.

The terms of this recommendation also apply to the secretary of the board, even if he or she is not a director.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

24. Directors who give up their place before their tenure expires, through resignation or otherwise, should state their reasons in a letter to be sent to all members of the board. Whether or not such resignation is disclosed as a material event, the motivating factors should be explained in the annual corporate governance report.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

25. The nomination committee should ensure that non-executive directors have sufficient time available to discharge their responsibilities effectively.

The board of directors regulations should lay down the maximum number of company boards on which directors can serve.

Complies ☒ Complies in part ☐ Explain ☐

26. The board should meet with the necessary frequency to properly perform its functions, eight times a year at least, in accordance with a calendar and agendas set at the start of the year, to which each director may propose the addition of initially unscheduled items.

Complies ☒ Complies in part ☐ Explain ☐

27. Director absences should be kept to a strict minimum and quantified in the annual corporate governance report. In the event of absence, directors should delegate their powers of representation with the appropriate instructions.

Complies ☒ Complies in part ☐ Explain ☐

28. When directors or the secretary express concerns about some proposal or, in the case of directors, about the company's performance, and such concerns are not resolved at the meeting, they should be recorded in the minute book if the person expressing them so requests.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

29. The company should provide suitable channels for directors to obtain the advice they need to carry out their duties, extending if necessary to external assistance at the company's expense.

Complies ☒ Complies in part ☐ Explain ☐

30. Regardless of the knowledge directors must possess to carry out their duties, they should also be offered refresher programmes when circumstances so advise.

Complies ☒ Explain ☐ Not applicable ☐

31. The agendas of board meetings should clearly indicate on which points directors must arrive at a decision, so they can study the matter beforehand or gather together the material they need.

For reasons of urgency, the chairman may wish to present decisions or resolutions for board approval that were not on the meeting agenda. In such exceptional circumstances, their inclusion will require the express prior consent, duly minuted, of the majority of directors present.

Complies ☒ Complies in part ☐ Explain ☐

32. Directors should be regularly informed of movements in share ownership and of the views of major shareholders, investors and rating agencies on the company and its group.

Complies ☒ Complies in part ☐ Explain ☐

33. The chairman, as the person charged with the efficient functioning of the board of directors, in addition to the functions assigned by law and the company's bylaws, should prepare and submit to the board a schedule of meeting dates and agendas; organise and coordinate regular evaluations of the board and, where appropriate, the company's chief executive officer; exercise leadership of the board and be accountable for its proper functioning; ensure that sufficient time is given to the discussion of strategic issues, and approve and review refresher courses for each director, when circumstances so advise.

Complies ☒ Complies in part ☐ Explain ☐

34. When a lead independent director has been appointed, the bylaws or board of directors regulations should grant him or her the following powers over and above those conferred by law: chair the board of directors in the absence of the chairman or vice chairmen give voice to the concerns of non-executive directors; maintain contacts with investors and shareholders to hear their views and develop a balanced understanding of their concerns, especially those to do with the company's corporate governance; and coordinate the chairman's succession plan.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

35. The board secretary should strive to ensure that the board's actions and decisions are informed by the governance recommendations of the Good Governance Code of relevance to the company.

Complies ☒ Explain ☐

36. The board in full should conduct an annual evaluation, adopting, where necessary, an action plan to correct weakness detected in:

- a) The quality and efficiency of the board's operation.
- b) The performance and membership of its committees.
- c) The diversity of board membership and competences.
- d) The performance of the chairman of the board of directors and the company's chief executive.
- e) The performance and contribution of individual directors, with particular attention to the chairmen of board committees.

The evaluation of board committees should start from the reports they send the board of directors, while that of the board itself should start from the report of the nomination committee.

Every three years, the board of directors should engage an external facilitator to aid in the evaluation process. This facilitator's independence should be verified by the nomination committee.

Any business dealings that the facilitator or members of its corporate group maintain with the company or members of its corporate group should be detailed in the annual corporate governance report.

The process followed and areas evaluated should be detailed in the annual corporate governance report.

Complies ☒ Complies in part ☐ Explain ☐

37. When an executive committee exists, its membership mix by director class should resemble that of the board. The secretary of the board should also act as secretary to the executive committee.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

38. The board should be kept fully informed of the business transacted and decisions made by the executive committee. To this end, all board members should receive a copy of the committee's minutes.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

39. All members of the audit committee, particularly its chairman, should be appointed with regard to their knowledge and experience in accounting, auditing and risk management matters. A majority of committee places should be held by independent directors.

Complies ☒ Complies in part ☐ Explain ☐

40. Listed companies should have a unit in charge of the internal audit function, under the supervision of the audit committee, to monitor the effectiveness of reporting and control systems. This unit should report functionally to the board's non-executive chairman or the chairman of the audit committee.

Complies ☒ Complies in part ☐ Explain ☐

41. The head of the unit handling the internal audit function should present an annual work programme to the audit committee, inform it directly of any incidents arising during its implementation and submit an activities report at the end of each year.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

42. The audit committee should have the following functions over and above those legally assigned:

1. With respect to internal control and reporting systems

- a) Monitor the preparation and the integrity of the financial information prepared on the company and, where appropriate, the group, checking for compliance with legal provisions, the accurate demarcation of the consolidation perimeter, and the correct application of accounting principles.
- b) Monitor the independence of the unit handling the internal audit function; propose the selection, appointment, re-election and removal of the head of the internal audit service; propose the service's budget; approve its priorities and work programmes, ensuring that it focuses primarily on the main risks the company is exposed to; receive regular report-backs on its activities; and verify that senior management are acting on the findings and recommendations of its reports.
- c) Establish and supervise a mechanism whereby staff can report, confidentially and, if appropriate and feasible, anonymously, any significant irregularities that they detect in the course of their duties, in particular financial or accounting irregularities.

2. With regard to the external auditor:

- a) Investigate the issues giving rise to the resignation of the external auditor, should this come about.
- b) Ensure that the remuneration of the external auditor does not compromise its quality or independence.
- c) Ensure that the company notifies any change of external auditor to the CNMV as a material event, accompanied by a statement of any disagreements arising with the outgoing auditor and the reasons for the same.
- d) Ensure that the external auditor has a yearly meeting with the board in full to inform it of the work undertaken and developments in the company's risk and accounting positions.
- e) Ensure that the company and the external auditor adhere to current regulations on the provision of non-audit services, limits on the concentration of the auditor's business and other requirements concerning auditor independence.

Complies ☒ Complies in part ☐ Explain ☐

43. The audit committee should be empowered to meet with any company employee or manager, even ordering their appearance without the presence of another senior officer.

Complies ☒ Explain ☐

44. The audit committee should be informed of any fundamental changes or corporate transactions the company is planning, so the committee can analyse the operation and report to the board beforehand on its economic conditions and accounting impact and, when applicable, the exchange ratio proposed.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

45. The risk control and management policy should identify at least:

- a) The different types of financial and non-financial risk the company is exposed to (including operational, technological, financial, legal, social, environmental, political and reputational risks), with the inclusion under financial or economic risks of contingent liabilities and other off- balance-sheet risks.
- b) The determination of the risk level the company sees as acceptable.
- c) The measures in place to mitigate the impact of identified risk events should they occur.
- d) The internal control and reporting systems to be used to control and manage the above risks, including contingent liabilities and off-balance- sheet risks.

Complies ☒ Complies in part ☐ Explain ☐

46. Companies should establish a risk control and management function in the charge of one of the company's internal department or units and under the direct supervision of the audit committee or some other dedicated board committee. This function should be expressly charged with the following responsibilities:

- a) Ensure that risk control and management systems are functioning correctly and, specifically, that major risks the company is exposed to are correctly identified, managed and quantified.
- b) Participate actively in the preparation of risk strategies and in key decisions about their management.
- c) Ensure that risk control and management systems are mitigating risks effectively in the frame of the policy drawn up by the board of directors.

Complies ☒ Complies in part ☐ Explain ☐

47. Appointees to the nomination and remuneration committee - or of the nomination committee and remuneration committee, if separately constituted - should have the right balance of knowledge, skills and experience for the functions they are called on to discharge. The majority of their members should be independent directors.

Complies ☒ Complies in part ☐ Explain ☐

48. Large cap companies should operate separately constituted nomination and remuneration committees.

Complies ☒ Complies in part ☐ Explain ☐

49. The nomination committee should consult with the company's chairman and chief executive, especially on matters relating to executive directors.

When there are vacancies on the board, any director may approach the nomination committee to propose candidates that it might consider suitable.

Complies ☒ Complies in part ☐ Explain ☐

50. The remuneration committee should operate independently and have the following functions in addition to those assigned by law:

- a) Propose to the board the standard conditions for senior officer contracts.
- b) Monitor compliance with the remuneration policy set by the company.
- c) Periodically review the remuneration policy for directors and senior officers, including share-based remuneration systems and their application, and ensure that their individual compensation is proportionate to the amounts paid to other directors and senior officers in the company.
- d) Ensure that conflicts of interest do not undermine the independence of any external advice the committee engages.
- e) Verify the information on director and senior officers' pay contained in corporate documents, including the annual directors' remuneration statement.

Complies ☒ Complies in part ☐ Explain ☐

51. The remuneration committee should consult with the company's chairman and chief executive, especially on matters relating to executive directors and senior officers.

Complies ☒ Complies in part ☐ Explain ☐

52. The terms of reference of supervision and control committees should be set out in the board of directors regulations and aligned with those governing legally mandatory board committees as specified in the preceding sets of recommendations. They should include at least the following terms:

- a) Committees should be formed exclusively by non-executive directors, with a majority of independents.
- b) They should be chaired by independent directors.

- c) The board should appoint the members of such committees with regard to the knowledge, skills and experience of its directors and each committee's terms of reference; discuss their proposals and reports; and provide report-backs on their activities and work at the first board plenary following each committee meeting.
- d) They may engage external advice, when they feel it necessary for the discharge of their functions.
- e) Meeting proceedings should be minuted and a copy made available to all board members.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

53. The task of supervising compliance with corporate governance rules, internal codes of conduct and corporate social responsibility policy should be assigned to one board committee or split between several, which could be the audit committee, the nomination committee, the corporate social responsibility committee, where one exists, or a dedicated committee established *ad hoc* by the board under its powers of self-organisation, with at the least the following functions:

- a) Monitor compliance with the company's internal codes of conduct and corporate governance rules.
- b) Oversee the communication and relations strategy with shareholders and investors, including small and medium-sized shareholders.
- c) Periodically evaluate the effectiveness of the company's corporate governance system, to confirm that it is fulfilling its mission to promote the corporate interest and catering, as appropriate, to the legitimate interests of remaining stakeholders.
- d) Review the company's corporate social responsibility policy, ensuring that it is geared to value creation.
- e) Monitor corporate social responsibility strategy and practices and assess compliance in their respect.
- f) Monitor and evaluate the company's interaction with its stakeholder groups.
- g) Evaluate all aspects of the non-financial risks the company is exposed to, including operational, technological, legal, social, environmental, political and reputational risks.
- h) Coordinate non-financial and diversity reporting processes in accordance with applicable legislation and international benchmarks.

Complies ☒ Complies in part ☐ Explain ☐

54. The corporate social responsibility policy should state the principles or commitments the company will voluntarily adhere to in its dealings with stakeholder groups, specifying at least:

- a) The goals of its corporate social responsibility policy and the support instruments to be deployed.
- b) The corporate strategy with regard to sustainability, the environment and social issues.
- c) Concrete practices in matters relative to: shareholders, employees, clients, suppliers, social welfare issues, the environment, diversity, fiscal responsibility, respect for human rights and the prevention of illegal conducts.
- d) The methods or systems for monitoring the results of the practices referred to above, and identifying and managing related risks.
- e) The mechanisms for supervising non-financial risk, ethics and business conduct.
- f) Channels for stakeholder communication, participation and dialogue.
- g) Responsible communication practices that prevent the manipulation of information and protect the company's honour and integrity.

Complies ☒ Complies in part ☐ Explain ☐

55. The company should report on corporate social responsibility developments in its directors' report or in a separate document, using an internationally accepted methodology.

Complies ☒ Explain ☐

56. Director remuneration should be sufficient to attract individuals with the desired profile and compensate the commitment, abilities and responsibility that the post demands, but not so high as to compromise the independent judgement of non-executive directors.

Complies ☒ Explain ☐

57. Variable remuneration linked to the company and the director's performance, the award of shares, options or any other right to acquire shares or to be remunerated on the basis of share price movements, and membership of long-term savings schemes such as pension plans should be confined to executive directors.

The company may consider the share-based remuneration of non-executive directors provided they retain such shares until the end of their mandate. This condition, however, will not apply to shares that the director must dispose of to defray costs related to their acquisition.

Complies ☒ Complies in part ☐ Explain ☐

58. In the case of variable awards, remuneration policies should include limits and technical safeguards to ensure they reflect the professional performance of the beneficiaries and not simply the general progress of the markets or the company's sector, or circumstances of that kind.

In particular, variable remuneration items should meet the following conditions:

- a) Be subject to predetermined and measurable performance criteria that factor the risk assumed to obtain a given outcome.
- b) Promote the long-term sustainability of the company and include non-financial criteria that are relevant for the company's long-term value, such as compliance with its internal rules and procedures and its risk control and management policies.
- c) Be focused on achieving a balance between the delivery of short, medium and long-term objectives, such that performance-related pay rewards ongoing achievement, maintained over sufficient time to appreciate its contribution to long-term value creation. This will ensure that performance measurement is not based solely on one-off, occasional or extraordinary events.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

59. A major part of variable remuneration components should be deferred for a long enough period to ensure that predetermined performance criteria have effectively been met.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

60. Remuneration linked to company earnings should bear in mind any qualifications stated in the external auditor's report that reduce their amount.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

61. A major part of executive directors' variable remuneration should be linked to the award of shares or financial instruments whose value is linked to the share price.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

62. Following the award of shares, share options or other rights on shares derived from the remuneration system, directors should not be allowed to transfer a number of shares equivalent to twice their annual fixed remuneration, or to exercise the share options or other rights on shares for at least three years after their award.

The above condition will not apply to any shares that the director must dispose of to defray costs related to their acquisition.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

63. Contractual arrangements should include provisions that permit the company to reclaim variable components of remuneration when payment was out of step with the director's actual performance or based on data subsequently found to be misstated.

Complies ☒ Complies in part ☐ Explain ☐ Not applicable ☐

64. Termination payments should not exceed a fixed amount equivalent to two years of the director's total annual remuneration and should not be paid until the company confirms that he or she has met the predetermined performance criteria.

Complies ☐ Complies in part ☒ Explain ☐ Not applicable ☐

Contracts with executive directors and senior officers signed as from 2011 provide severance for contractual termination equal to a maximum of two times annual salary in the event of termination of their relationship with the Company, provided that termination of the relationship is not the result of a breach attributable thereto or solely due to a voluntary decision thereof.

The Company included guarantee clauses of up to five years in contracts with its key officers 16 years ago. Subsequently, in 2001, when the current chairman & CEO joined Iberdrola, he received the treatment in effect for such officers, in order to achieve an effective and sufficient level of loyalty. As chairman & chief executive officer, he is currently entitled to three times annual salary.

The Board of Directors has analysed this situation, the treatment of which is necessarily collective in nature. Any reduction in the salary multiples would carry high costs for the Company, for which reason the Board of Directors believes that it is most appropriate not to change the status quo. Any proposed reduction in the salary multiples would have a higher cost for the Company, as the amount of the contingency will gradually decrease due to the passage of time, resulting in payments far smaller than any possible reduction in the agreed severance payment, taking into account the average age of the affected group and the low likelihood of the guarantees being enforced. In this regard, it should be pointed out that at year-end 2014, there were 62 officers in this group. By year-end 2015, the number had decreased to 52. By year-end 2016, the number has decreased again to 45, without the enforcement of any guarantee clause.

H. OTHER INFORMATION OF INTEREST

1. If there are any significant aspects regarding corporate governance at the company or at entities of the group that is not included in the other sections of this report, but should be included in order to provide more complete and well-reasoned information regarding the corporate governance structure and practices at the entity or its group, briefly describe them.
2. In this section, you may also include any other information, clarification, or comment relating to the prior sections of this report to the extent they are relevant and not repetitive.

Specifically, state whether the company is subject to laws other than Spanish laws regarding corporate governance and, if applicable, include such information as the company is required to provide that is different from the information required in this report.

3. The company may also state whether it has voluntarily adhered to other international, industrial, or other codes of ethical principles or good practices. If so, identify the code in question and the date of adherence thereto. In particular, mention whether there has been adherence to the Code of Good Tax Practices of 20 July 2010.

MISSION, VISION, AND VALUES

Iberdrola is fully aware of its importance as a business, institutional, and social reality, and cannot nor does it want to be estranged from the challenges entailed in its position as the controlling company of one of the leading global groups in the electricity sector. The responsibilities arising from all of the above go beyond the strictly economic arena, fully reaching the social level.

Along these lines, the efforts of Iberdrola's Board of Directors since the General Shareholders' Meeting held in 2015 have been directed towards a consideration of the relations that the Company and the Group should maintain with its Stakeholders, beyond its shareholders and the financial community - its workforce, regulatory entities, its customers, its suppliers, the media, society in general, and the environment, among others.

Specifically, during the month of October 2015, the Board of Directors engaged in a profound review of the mission, vision, and values of the Group to better conform them to a complex business group, with the goal of leadership in all facets of its business (both economically and especially socially) using a new focus that stresses the sustainable creation of value and emphasises the social impact of its activities.

The content of the new mission, vision, and values of the Group have been incorporated into a new rule within the Corporate Governance System: the Mission, Vision, and Values of the Iberdrola group, which contains the corporate philosophy of the Group, inspires and takes form in the By-Laws and in the other rules of its Corporate Governance System, govern the day-to-day activities thereof, channel its leadership role in all of its areas of activity, focus its strategy of maximising social dividends, and guide the ethical behaviour of all personnel participating in the daily construction of the Company's corporate enterprise.

The Company seeks a social return on all of its activities. Its corporate values reflect its commitment to the sustainable creation of value, ethical principles, transparency and good corporate governance, the development of human resources, social commitment, a sense of belonging, safety and reliability, quality, innovation, protection of the environment, customer focus, and institutional loyalty.

The Company and the other entities belonging to the Group seek to engage all Stakeholders in its business enterprise in accordance with a policy on relations with all of them based on two-way communication and the principles of transparency, active listening and equal treatment, which allows for all of their legitimate interests to be taken into consideration and to effectively disclose information regarding the activities and businesses of the Group.

SECTION A.1

The shareholders acting at the General Shareholders' Meeting of the Company held on 27 March 2015 approved two increases in share capital by means of scrip issues in order to implement the shareholder compensation system called "Iberdrola Flexible Dividend" (*"Iberdrola Dividendo Flexible"*), which allows the shareholders to decide whether they prefer to receive all or part of their compensation in cash or in Iberdrola bonus shares.

The second increase in capital took place in January 2016, when the traditional interim dividend for financial year 2015 would otherwise have been paid, and the number of new shares that were issued and floated came to 60,327,000, par value 0.75 euro each, without a share premium, representing approximately 0.95% of the share capital prior to the increase.

The shareholders acting at the Company's General Shareholders' Meeting held on 8 April 2016 approved a reduction in share capital by means of the retirement of 157,197,000 treasury shares of Iberdrola representing 2.46% of the share capital.

As a result of such resolution, the share capital of Iberdrola was reduced by the amount of 117,897,750 euros through the retirement of 157,197,000 treasury shares (148,845,827 own shares already in treasury and 8,351,173 shares acquired from the shareholders through the buy-back programme), representing approximately 2.45% of the share capital prior to the reduction. The share capital resulting from the reduction was set at 4,680,000,000.00 euros, corresponding to 6,240,000,000 shares.

The purpose of the reduction in capital was to retire treasury shares, for which reason there was no return of contributions as the Company itself was the holder of the retired shares.

In addition, the shareholders acting at the General Shareholders' Meeting of the Company held on 8 April 2016 approved, under item six on the agenda, two increases in share capital by means of a scrip issue in order to implement, for the seventh consecutive year, the shareholder remuneration system known as Iberdrola Flexible Dividend.

The first increase in capital took place in July 2016, when the traditional supplementary dividend for financial year 2015 would otherwise have been paid, and the number of new shares that were issued and floated came to 122,079,000, par value 0.75 euro each, without a share premium, representing approximately 1.95% of the share capital prior to the increase. After said increase in capital, the share capital of the Company increased to 4,771,559,250 euros, divided into 6,362,079,000 shares.

The second increase in capital took place in January 2017, when the traditional dividend for financial year 2016 would have been paid. The number of new shares issued and floated came to 97,911,000, par value 0.75 euro each, without a share premium, representing approximately 1.54% of the share capital prior to the increase. After said increase in capital, the share capital of the Company increased to 4,844,992,500 euros, represented by 6,459,990,000 shares.

SECTION A.2

Given that the shares are represented by book entries, no information is available on a daily basis about the interest of shareholders in the share capital. However, since 7 May 2014, Iberdrola is a member within Iberclear of the Communication Service for securities holdings and the balanced list of buyers and sellers upon the terms set forth in Circular No 5/2013 of 27 November. The sources of the information provided are the notices sent by the shareholders to the CNMV and to the Company itself, and the information contained in their respective annual reports and press releases, as well as the information that the Company obtains from Iberclear.

Pursuant to the provisions of section 23.1 of Royal Decree 1362/2007 of 19 October, further developing Law 24/1988 of 28 July on the Securities Market, in connection with the transparency requirements relating to the information on issuers whose securities have been admitted to trading on an official secondary market or other regulated market in the European Union, it is deemed that significant shareholders are the holders of at least 3% of voting rights.

According to available information, the approximate breakdown of the interests in the share capital by type of shareholder is as follows:

- Foreign investors	62.8%
- Domestic entities	13.9%
- Domestic retail investors	23.3%

SECTION A.3

Data at the date of approval of this Report.

SECTION A.8

Iberdrola maintains in treasury 151,224,777 own shares and 1,624,221 shares accumulated through derivatives contracts pending settlement and that are recorded as treasury shares in the consolidated financial statements at 31 December 2016, representing 2.402% of the capital. It also maintains 1,867,929 shares in total return swaps with physical settlement.

Pursuant to the authorisations granted to the Board of Directors by the shareholders at the General Shareholders' Meeting, during financial year 2016 Iberdrola acquired 247,226,143 shares of its own stock for 1,450,724 thousand euros. Of those, 146,551,785 shares were acquired through discretionary market transactions, while the remaining 100,674,358 shares were acquired through derivatives contracts.

In addition, 6,440,532 own shares were sold for 39,360 thousand euros.

Under such authorisations, Iberdrola has also retired 157,197,000 own shares.

SECTION B.4

The percentage of absentee voting (others) only reflects the votes received by mail. In other words, the votes from non-resident investors (7.15%) and those collected through banks (1.3%) and shareholders service points (0.12%) are not included.

SECTION C.1.3

The complete professional profiles of all the directors are available on the Company's corporate website (www.iberdrola.com).

SECTION C.1.29

Within the framework of the process of evaluation of the Board of Directors, the lead independent director met individually with each of the directors in order to identify possible improvements in the operation thereof.

SECTION C.1.30

Below is the data on attendance of each and every one of the directors at the meetings of the Board of Directors and its committees during financial year 2016: See Annex.

SECTION C.1.31

The Iberdrola Group has established a certification process by which those responsible for financial information in the different areas of the Company certify that: (i) the financial information they deliver to Iberdrola for purposes of consolidation does not contain any material errors or omissions and provides a fair view of the results and the financial condition within their area of responsibility, and (ii) they are responsible for establishing the ICFRS within their area of responsibility and have found, upon evaluation, that the system is effective. The text of these certifications is inspired by the form of certification established in section 302 of the U.S. Sarbanes-Oxley Act.

The culmination of the process is a joint certification that the chairman & chief executive officer and the director of Administration and Control submit to the Board of Directors.

The process is carried out by means of electronic signature in a software application which manages the areas of responsibility and time periods and which serves as a repository of all the documentation generated, allowing for periodic review by the supervisory bodies of the Group.

SECTION C.1.36

The Board of Directors will submit to the shareholders at the 2017 General Shareholders' Meeting, as item 4 on the agenda, the proposed appointment of KPMG Auditores, S.L. as auditor of the annual accounts of the Company and of its consolidated group.

SECTION D.2

Transactions by shareholders exercising a significant influence on participation in the entity's financial and operating decisions, with significant influence being understood as having a member of the Board of Directors.

This consideration includes those shareholders that, given their equity interest in the Company, are able to exercise the proportional representation system.

As of the date of this report, only Qatar Investment Authority meets this condition, for which reason the amounts referred to in the period are with respect to the transactions with this shareholder.

The amounts set forth as "profits and other dividends paid" correspond to the cash dividend distributed by the Company and to the free-of-charge allocation rights stemming from the two increases in share capital by means of a scrip issue approved by the shareholders at the General Shareholders' Meetings, which were sold to the Company at a guaranteed fixed price pursuant to the terms and conditions of such increases.

SECTION D.4

Transactions with subsidiaries and companies in which the Company has an interest that have not been eliminated in the process of consolidation were made in the ordinary course of business of the Company, were carried out under arm's-length conditions, and are of little significance to accurately reflect the assets, financial condition, and results of operations of the Company.

On 20 July 2010, the Company adhered to the Code of Good Tax Practices, a document approved at the full Forum of Large Businesses (*Foro de Grandes Empresas*) created by the National Tax Administration Agency (*Agencia Estatal de Administración Tributaria*) and certain large companies, and which was held on that date.

Pursuant to the provisions of section 2 of the annex of adherence to the Good Tax Practices Code and of subsection 5.b) of the Corporate Tax Policy, the Company reports that it has complied with the provisions of such Code as from the time of approval thereof.

Specifically, it is reported that, during financial year 2016, the Company's head of tax matters appeared on 22 February 2016 and 18 July 2016 before Iberdrola's Audit and Risk Supervision Committee to report on compliance with the Corporate Tax Policy, which includes the good tax practices contained in the aforementioned Code, all of which was reported to the Board of Directors.

This annual corporate governance report was approved by the Board of Directors of the company at its meeting of 21 February 2017.

State whether any directors voted against or abstained in connection with the approval of this Report.

Yes ☐ No ☒

Individual or company name of director that did not vote in favour of the approval of this report	Reasons (opposed, abstained, absent)	Explain the reasons

ANNEX – SECTION H

SECTION C.1.30

Below is the data on attendance of each and every one of the directors at the meetings of the Board of Directors and its committees during financial year 2016. Proxies granted with specific voting instructions are considered to be attendances.

Directors	Board	Committees				
		EC	ARSC	AC	RC	CSRC
MR JOSÉ IGNACIO SÁNCHEZ GALÁN	8/8	13/13	--	--	--	--
MR XABIER DE IRALA ESTÉVEZ	3/3	3/3	--	--	--	--
MR IÑIGO VÍCTOR DE ORIOL IBARRA	8/8	--	--	9/9	7/7	--
MS INÉS MACHO STADLER	8/8	13/13	--	--	7/7	--
MR BRAULIO MEDEL CÁMARA	8/8	--	--	--	--	12/12
MS SAMANTHA BARBER	8/8	--	--	--	--	12/12
MS MARÍA HELENA ANTOLÍN RAYBAUD	8/8	--	--	9/9		--
MR SANTIAGO MARTÍNEZ LAGE	8/8	--	--	--	7/7	--
MR JOSÉ LUIS SAN PEDRO GUERENABARRENA	8/8	13/13	--	--	--	--
MR ÁNGEL JESÚS ACEBES PANIAGUA	8/8	13/13	--	9/9	--	--
MS GEORGINA KESSEL MARTÍNEZ	8/8	--	13/13	--	--	--
MS DENISE MARY HOLT	8/8	--	13/13	--	--	--
MR JOSÉ WOLFREDO FERNÁNDEZ	8/8	--	13/13	--	--	--
MR MANUEL MOREU MUNAIZ	8/8	10/10	--	--	--	12/12
MR XABIER SAGREDO ORMAZA	5/5	--	8/8	--	--	--

Notes:

- The denominator indicates the number of meetings held during the period of the year in which the director served as such or as a member of the respective Committee.
- EC: Executive Committee.
- ARSC: Audit and Risk Supervision Committee.
- AC: Appointments Committee.
- RC: Remuneration Committee
- CSRC: Corporate Social Responsibility Committee.



IBERDROLA

Annual Financial Report

Directors' Liability Statement / Financial Year 2016

ANNUAL FINANCIAL REPORT STATEMENT OF RESPONSIBILITY

The members of the Board of Directors of IBERDROLA, S.A. state that, to the best of their knowledge, the individual annual accounts of IBERDROLA, S.A. (balance sheet, income statement, statement of change in equity, statement of cash flows and notes), as well as the consolidated annual accounts of IBERDROLA, S.A. and its subsidiaries (consolidated statement of financial position, consolidated income statement, consolidated statement of comprehensive income, consolidated statement of changes in equity, consolidated statement of cash flows and notes) for the fiscal year ended on December 31, 2016, issued by the Board of Directors at its meeting of February 21, 2017, and prepared in accordance with applicable accounting standards, present a fair view of the assets, financial condition and results of operations of IBERDROLA, S.A. as well as of the subsidiaries included within its scope of consolidation, taken as a whole, and that the management reports supplementing the individual and consolidated annual accounts contain a fair assessment of the corporate performance and results and the position of IBERDROLA, S.A. and of the subsidiaries included within its scope of consolidation, taken as a whole, as well as a description of the principal risks and uncertainties facing them.

Bilbao, February 21, 2017

Mr José Ignacio Sánchez Galán
Chairman & Chief Executive Officer

Mr Íñigo Víctor de Oriol Ibarra
Director

Ms Inés Macho Stadler
Director

Mr Braulio Medel Cámara
Director

Ms Samantha Barber
Director

Ms Maria Helena Antolín Raybaud
Director

Mr Santiago Martínez Lage
Director

**Mr José Luis San Pedro
Guerenabarrena**
Director

Mr Ángel Jesús Acebes Paniagua
Director

**Ms Georgina Yamilet Kessel
Martínez**
Director

Ms Denise Mary Holt
Director

Mr José Walfredo Fernández
Director

Mr Manuel Moreu Munaiz
Director

Mr Xabier Sagredo Ormaza
Director