REPORT SUBMITTED BY THE BOARD OF DIRECTORS OF IBERDROLA, S.A. REGARDING THE PROPOSED AMENDMENTS OF THE BY-LAWS INCLUDED IN ITEM NUMBERS FIVE AND SIX ON THE AGENDA FOR THE GENERAL SHAREHOLDERS’ MEETING CALLED TO BE HELD ON 31 MARCH AND 1 APRIL 2017, ON FIRST AND SECOND CALL, RESPECTIVELY

1. Purpose of the Report

This report has been prepared by the Board of Directors of IBERDROLA, S.A. (“Iberdrola” or the “Company”) pursuant to the provisions of section 286 of the Companies Act, in order to provide a rationale for the proposed amendments of the By-Laws included in item numbers five and six on the agenda.

Pursuant to the aforementioned section, the Board of Directors prepares this report explaining the purpose of and rationale for the proposed by-law amendments, attaching such proposals below. In addition, in order to provide the shareholders with a clear view of the scope of the amendment and a comparison between the new text of the articles proposed to be amended and the text currently in effect, attached to this report as an Annex is a verbatim transcription of both texts organised in a two-column table, for information purposes. The text contained in the right-hand column shows the changes proposed to be made to the text currently in force, which is contained in the left-hand column.

2. Purpose of and Rationale for the Proposals

2.1 Introduction

The challenges facing Iberdrola -and the social impact thereof- have been growing in parallel with the group’s triumphs in all of the countries in which it does business: today, Iberdrola produces and supplies electricity in a clean, reliable, and responsible manner to some one hundred million people, mainly in the United Kingdom, the United States, Mexico, Brazil, Spain, and Portugal, which in turn drives their economic and social progress.

Iberdrola has always been quite conscious of the significance of its activities for the communities in which it does business, and of the challenges this entails.

When it was founded at the beginning of the 20th century, access to electric energy was a key element decisively favouring progress and the creation of wealth. This same energy permitted the activation of the economy, supported the creation of increasingly qualified jobs, fostered the education and training of the group’s professionals and improved their quality of life, and developed both culture and art.

The generation and distribution of electric energy improved the society that gave birth to Iberdrola and in which its beginnings were bundled.

This is the same energy with which Iberdrola, now a global actor, today faces the main environmental, social, and economic challenges threatening the future of the planet, through initiatives such as the inclusion within its business strategy and its Sustainability Policy of the Sustainable Development Goals defined by the United Nations for the 2015-2030 period.

In harmony with its activity, Iberdrola focuses its efforts on the supply of accessible and non-polluting energy (goal 7) and climate action (goal 13): the emissions intensity of the Iberdrola group is 34% lower than the European average - it is one of the European electric utilities with the lowest ratio of emissions per MWh. Iberdrola also hopes to achieve a 30% reduction in its greenhouse gas emissions intensity by 2020 compared to 2007 levels and a 50% reduction by 2030.

The effective realisation of this desire to improve the communities in which it lives, and ultimately to improve the planet, is Iberdrola’s social dividend, the maximisation of which has been, is, and must continue to be an essential part of the Company’s raison d’etre.

Hardly a year ago, Iberdrola formalised its commitment to its Mission, Vision, and Values within its foundational document, its By-Laws, thus becoming the first large Spanish multinational to acknowledge the importance thereof as a business, institutional, and social reality and its firm commitment to face the challenges involved thereby.

The proposal that the Board of Directors now submits to the shareholders at the General Shareholders’ Meeting is one more step along this path of commitment to the social dividend as an essential part of its strategy and of its business enterprise.

The proposed by-law amendments go into more detail on the maximisation of Iberdrola’s social dividend as an essential part of its strategy and its business enterprise, and complete the definition of its corporate governance model, taking into account all of the stakeholders related to the Company.
In particular, the reform provides for the insertion of a new preamble, which confirms and makes explicit this commitment, and the development of the concept of a social dividend, conceived as the sustainable creation of value for all stakeholders affected by the activities of the Group in carrying out its businesses, the advancement of the business communities which the Company participates in and leads, both from the economic viewpoint and from the perspective of business ethics, the promotion of equality and justice, the encouragement of innovation and protection of the environment, as well as through the generation of quality employment, its strategy of social responsibility, and its effort in the fight against climate change.

The proposed by-law reform deepens Iberdrola’s explicit commitment to its Mission, Vision, and Values and completes the redefinition of its corporate governance model, focusing it on the maximisation of its social dividend, conceived as the sustainable creation of value for all stakeholders affected by the activities of the Iberdrola group in carrying out its businesses, the advancement of the business communities which the Company participates in and leads, both from the economic viewpoint and from the perspective of business ethics, innovation, and protection of the environment, and through its strategy of social responsibility and its economic, social, and cultural contributions to such communities.

2.2 Purpose of the Proposals

Within this framework, a proposal is made to insert a new preamble that summarises and explains the inspirational principles guiding Iberdrola and which define its business enterprise, as well as the amendment of the current article 7 to formalise the Company’s strategy to maximise its social dividend and of article 8 to strengthen its commitment to the Mission, Vision, and Values of the Iberdrola group and to reflect the new structure of the Corporate Governance System after the most recent reforms approved by the Board of Directors during the month of July to strengthen the regulatory compliance function.

2.3 Structure of the Proposed Amendments

In order to facilitate the proper exercise of shareholders’ voting rights, pursuant to the provisions of section 197 bis of the Companies Act and article 40.1 of the Regulations for the General Shareholders’ Meeting, the creation of the new Preamble is submitted for the approval of the shareholders separately (item number five on the agenda) from the amendment of articles 7 and 8 of the By-Laws, which will be voted on together because they affect the same articles (item number six on the agenda).

3. Proposed Resolutions Submitted to the Shareholders at the General Shareholders’ Meeting

The proposed resolutions submitted to the shareholders for approval at the General Shareholders’ Meeting read as follows:

**ITEM NUMBER FIVE ON THE AGENDA**

Approval of the preamble to the By-Laws.

**RESOLUTION**

To approve the text of the preamble to the By-Laws, which shall read as follows:

**PREAMBLE**

Organised in 1901, Iberdrola represents a business model built on a mission, a vision, and certain values, the common denominator and main engine of which is a commitment to the sustainable creation of value in the performance of all of its activities for society, its professionals, its customers, its suppliers, its shareholders, and its other stakeholders.

These By-Laws, approved by the shareholders acting at a General Shareholders’ Meeting of the Company, the highest governance body through which the legitimate owners of Iberdrola express their will, constitute the core of its internal rules, and pursuant to the corporate autonomy recognised by law, governs the company contract that all shareholders accept upon acquiring their status as such, that binds them in their capacity as such, and that lays the foundations and principles determining the governance of Iberdrola as the controlling entity of a multinational entity group.

The By-Laws go much beyond the content required by law and what is customary for listed companies in that they define in their preliminary title the foundations of Iberdrola as an independent, open holding company of an international industrial group, which is decentralised and committed to a mission, a vision, and values, as well as a clear strategy to maximise its social dividend. The By-Laws also recognise the fact that Iberdrola, due to its size and importance, constitutes an institutional reality, a focal point for many stakeholders and for the economic and social environment in which it does business.
The text thereof is inspired by the Mission, Vision, and Values of the Iberdrola group, which governs the day-to-day activities of the Company, channels its leadership role in its various areas of activity, drives its strategy of maximising the social dividend, and guides the ethical behaviour of all personnel participating in the daily construction of Iberdrola’s business enterprise.

The Mission of the Group is based on the sustainable creation of value in carrying out all of its activities, 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, Iberdrola fosters their development, training, and measures of reconciliation, favouring a good working environment and equal opportunity. All of the foregoing is within the framework of its strategy of social responsibility and compliance with tax rules.

The Mission is complemented, on the one hand, by a Vision contemplating an ambition to play the lead towards a better future, sustainably creating value with a quality service for the people and for the communities in which the Group does business, and on the other, by certain specific Values, which include the sustainable creation of value, respect for ethical principles, good corporate governance and transparency, development of its human resources, social commitment, encouragement of the stakeholders’ sense of belonging, safety and reliability of supply, quality, innovation, respect for the environment, customer focus, and institutional loyalty.

In turn, these By-Laws are the basis on which the Company has built its Corporate Governance System, a regulatory structure that ensures the effective articulation of the principles set out in the Mission, Vision, and Values of the Iberdrola group in the form of a true regulatory system that is subject to continuous review and update in order to immediately conform to regulatory changes and to the most stringent international standards.

The Corporate Governance System makes up a business model that combines a decentralised decision-making structure, inspired by the principle of subsidiarity, with robust coordination mechanisms ensuring the global integration of all of the Group’s businesses, all on the basis of an effective system of checks and balances that prevents the centralisation of power within a single governance body or a single person.

To the extent applicable thereto, Iberdrola’s By-Laws and the other provisions of its Corporate Governance System bind its shareholders, directors, officers and other professionals, as well as any persons validly linked thereto on a general basis. All have the duty to comply with them, as well as the right to demand compliance therewith.

ITEM NUMBER SIX ON THE AGENDA

Amendment of articles 7 and 8 of the By-Laws to reflect the Company's commitment to maximisation of the social dividend and to the Mission, Vision, and Values of the Iberdrola group.

RESOLUTION

To amend articles 7 and 8 of the By-Laws to reflect the Company’s commitment to maximisation of the social dividend and to the Mission, Vision, and Values of the Iberdrola group. These provisions shall hereafter read as follows:

"Article 7. Social Dividend

1. The Company conceives of the social dividend as the sustainable creation of value for all stakeholders affected by the activities of the Group in carrying out its businesses, the advancement of business communities which the Company participates in and leads, both from the economic viewpoint and from the perspective of business ethics, the promotion of equality and justice, the encouragement of innovation and protection of the environment, as well as through the generation of quality employment, its strategy of social responsibility, and its effort in the fight against climate change.

2. The Company is conscious of the importance of the social dividend for all of the communities in which the Group is present. Maximisation of the social dividend and the Company’s commitment to the sustainable creation of value, ethical principles, transparency and good corporate governance, the development of its human resources, social commitment, a sense of belonging, safety and reliability, quality, innovation, protection of the environment, customer focus, and institutional loyalty are key values that the Board of Directors takes into account in order to define the strategy of the Group.

Article 8. Applicable Legal Provisions and Corporate Governance System

1. The Company is governed by the legal provisions relating to listed companies and other applicable laws and regulations, as well as by its Corporate Governance System.
2. The Corporate Governance System is the Company’s 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. It is intended to ensure through rule-making the best development of the corporate contract that binds its shareholders, and especially the corporate object and the corporate interest, as defined in the preceding articles.

3. The Corporate Governance System is made up of these 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 codes, regulations, and procedures making up and elaborating upon the Company’s regulatory compliance system.

4. The Mission, Vision, and Values of the Iberdrola group constitutes the corporate philosophy of the Company, contains the ideological and axiological foundation upon which its business enterprise is based, and expresses a desire to optimise its corporate and institutional reality, in the awareness that, due to its size and the importance of its activities, it is a focal point for many stakeholders and for the economic and social environment in which its companies do business.

5. The Mission, Vision, and Values of the Iberdrola group inspires and takes form in the Corporate Policies and in the other rules of the Corporate Governance System, governing the day-to-day activities of all companies of the Group and guiding their strategy and all of their actions.

6. The Board of Directors has approved a Code of Ethics that further develops the bylaw-mandated commitment of the Company to the Mission, Vision, and Values of the Iberdrola group and ethical principles.

7. Full or summarised versions of the rules making up the Corporate Governance System can be viewed on the Company’s corporate website.

8. The shareholders acting at a General Shareholders’ Meeting and the Board of Directors of the Company, within their respective purview, develop, apply, and interpret the rules making up the Corporate Governance System in order to ensure compliance at all times with the purposes thereof and, particularly, the fulfilment of the corporate interest.

* * *

In Bilbao, on 21 February 2017.
### Article 7. Social Dividend

1. **The Mission, Vision, and Values of the Iberdrola group** constitutes the corporate philosophy of the Group and expresses a desire to optimise its business, corporate, and institutional reality, in the awareness that, due to its size and the importance of its activities, it is a focal point for many stakeholders and of the economic and social environment in which its companies do business.

2. The **Mission, Vision, and Values of the Iberdrola group** inspire and take form in the Corporate Policies and in the other rules of the Corporate Governance System, governing the day-to-day activities of all companies of the Group and guiding their strategy and all of their actions.

3. The Company seeks a social return on all of its activities. Its corporate values reflect its commitment to the creation of value in a sustainable manner, 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.

4. The Board of Directors has approved a **Code of Ethics** that further develops the bylaw-mandated commitment of the Company to its corporate values and ethical principles.

### Article 8. Applicable Legal Provisions and Corporate Governance System

1. The Company is governed by the legal provisions relating to listed companies and other applicable laws and regulations, as well as by its Corporate Governance System.

2. The Corporate Governance System is the Company’s 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. It is intended to ensure through rule-making the best development of the corporate object of the Company and the fulfilment of the corporate contract that binds its shareholders, and especially the corporate
interest. The Corporate Governance System is made up of these By-Laws, the Mission, Vision, and Values of the Iberdrola group, the Corporate Policies, the internal corporate governance rules, which include the Regulations for the General Shareholders’ Meeting, the Regulations of the Board of Directors and those of its consultative committees, and of the other internal codes and procedures approved by the competent decision-making bodies of the Company.

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