



REPORT SUBMITTED BY THE BOARD OF DIRECTORS OF IBERDROLA, S.A. FOR PURPOSES OF THE PROVISIONS OF SECTION 286 OF THE COMPANIES ACT, REGARDING THE RATIONALE FOR THE PROPOSED AMENDMENT OF THE BY-LAWS INCLUDED IN ITEM TEN ON THE AGENDA FOR THE GENERAL SHAREHOLDERS' MEETING CALLED TO BE HELD ON 28 AND 29 MARCH 2014, 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. (the “**Company**”) pursuant to the provisions of section 286 of the Companies Act (*Ley de Sociedades de Capital*), in order to provide a rationale for the proposed amendment of the *By-Laws* submitted to the shareholders for approval at the General Shareholders’ Meeting of the Company.

Section 286 of the Companies Act requires the preparation by the directors of a report providing a rationale for the proposed amendment of the *By-Laws*. To facilitate the shareholders’ understanding of the changes that give rise to this proposal, a description of the purpose of and rationale for such amendment is provided, and the proposed resolution submitted to the shareholders for approval at the General Shareholders’ Meeting is included below.

In addition, in order to facilitate a comparison between the new text of the articles proposed to be amended and the current text thereof, 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. Rationale for the Proposal

The amendments to the *By-Laws* proposed to the shareholders for approval at the General Shareholders’ Meeting are the following:

1.- Amendment of article 34.5 of the *By-Laws*, which article governs the powers of the Board of Directors, in order to make technical improvements to the text of letter c) of section A, letter c) of section c, and letter d) of section D and to replace the reference to preparation of the *Dividend Policy* with a broader reference to the shareholder remuneration policy in letter a) of section E.

2.- Amendment of article 44.3 of the *By-Laws*, which governs the Audit and Risk Supervision Committee, to set at four years the maximum term for the position of chair of such committee, such that it coincides with that of the position of director and of

member of the Audit and Risk Supervision Committee, pursuant to additional provision eighteen of Law 24/1988 of 28 July on the Securities Market.

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 TEN ON THE AGENDA

Amendment of the By-Laws.

RESOLUTION

A.- Amendment of article 34.5 of the By-Laws to make technical improvements to the text thereof.

To amend article 34.5 of the By-Laws, which shall hereafter read as follows:

“5. In particular, the Board of Directors, acting upon its own initiative or at the proposal of the corresponding internal decision-making body, shall occupy itself with the matters set forth below (as an example only):

- A) With respect to the General Shareholders' Meeting:*
 - a) Call the General Shareholders' Meeting.*
 - b) Propose the amendment of the By-Laws to the shareholders at a General Shareholders' Meeting.*
 - c) Propose to the shareholders at a General Shareholders' Meeting the amendment of the Regulations for the General Shareholders' Meeting.*
 - d) Submit to a decision by the shareholders at a General Shareholders' Meeting the transformation of the Company into a holding company, through “subsidiarisation” or the assignment to dependent entities of core activities theretofore carried out by the Company, even though the Company retains full control of such entities.*
 - e) Submit to a decision by the shareholders at a General Shareholders' Meeting all transactions for the acquisition or disposition of essential operating assets when they involve an effective change in the object of the company.*

- f) *Propose to the shareholders at a General Shareholders' Meeting the approval of transactions having an effect equivalent to liquidation of the Company.*
 - g) *Carry out the resolutions approved by the shareholders at a General Shareholders' Meeting and perform any duties that the shareholders have entrusted thereto.*
- B) *With respect to the organisation of the Board of Directors and the delegation of powers and the granting of powers of representation:*
- a) *Approve and amend the Regulations of the Board of Directors.*
 - b) *Define the structure of general powers to be granted by the Board of Directors or by the representative management decision-making bodies.*
- C) *With respect to information to be provided by the Company:*
- a) *Manage the provision of information regarding the Company to the shareholders and the markets in general, pursuant to standards of equal treatment, transparency, and truthfulness.*
 - b) *Prepare the Company's annual accounts, management report, and proposal for the allocation of profits or losses, as well as the consolidated accounts and management report and the financial information that the Company must periodically make public due to its status as listed company, ensuring that such documents provide a true and fair view of the assets and liabilities, the financial position, and the profits or losses of the Company in accordance with the provisions of law.*
 - c) *Approve the Company's Annual Corporate Governance Report, as well as the annual sustainability report, the annual director remuneration report, and any other report that the Board of Directors deems advisable in order to better inform shareholders and investors or that is required by legal provisions applicable at any time.*
- D) *With respect to the directors and senior officers:*
- a) *Designate directors to fill vacancies by interim appointment and propose to the shareholders at a General Shareholders' Meeting the appointment, ratification, re-election, or removal of directors.*
 - b) *Designate and renew internal positions within the Board of Directors and the members of and positions on the committees established within the Board of Directors.*

- c) *Set, pursuant to the By-Laws and within the limits established therein, the Director Remuneration Policy and the remuneration of directors. In the case of executive directors, the Board of Directors shall establish the additional remuneration to which they are entitled for their executive duties and other basic terms that their contracts must include.*
- d) *Approve, upon a proposal of the chairman of the Board of Directors or of the chief executive officer, the determination and modification of the Company's organisational chart, the appointment and removal of senior officers of the Company, as well as set the compensation or indemnification, if any, payable to them in the event of removal.*

As an exception to the foregoing, based on a proposal made for such purpose by the chairman of the Board of Directors, the Audit and Risk Supervision Committee shall, if applicable, submit to the Board of Directors a proposal supported by the corresponding report regarding the selection, appointment, or removal of the director of the Internal Audit Area.

Senior officers shall be those who report directly to the Board of Directors, to the chairman thereof, or to the chief executive officer of the Company, and shall in any case include the director of the Internal Audit Area and any other officer given such status by the Board of Directors.

- e) *Approve the Senior Officer Remuneration Policy as well as the basic terms of the contracts with senior officers, based for such purpose on a proposal made by the chairman of the Board of Directors or the chief executive officer to the Appointments and Remuneration Committee in order for the latter to prepare a report thereon and submit it to the Board of Directors.*
- f) *Regulate, review, and decide upon possible conflicts of interest and related-party transactions between the Company and its directors and senior officers as well as with persons related thereto.*

E) Other powers:

- a) *Prepare the shareholder remuneration policy and submit the corresponding proposed resolutions on the allocation of profits or losses and other modes of shareholder remuneration to the shareholders at the General Shareholders' Meeting, as well as decide upon the payment, if any, of interim dividends.*

- b) *Take note of mergers, split-offs, concentrations, or overall assignments of assets and liabilities that affect any of the significant companies of the Group.*
- c) *Declare its position regarding all takeover bids for the Company's securities.*
- d) *Decide on proposals submitted thereto by the Executive Committee, the chairman of the Board of Directors, the chief executive officer, the lead independent director (consejero independiente especialmente facultado), and the committees of the Board of Directors.*
- e) *Make decisions regarding any other matter within its power that the Board of Directors believes to be in the interest of the Company or that the Regulations of the Board of Directors reserve to the Board as a whole."*

B.- Amendment of article 44.3 of the By-Laws to set at four years the maximum term for the position of chair of the Audit and Risk Supervision Committee.

To amend article 44.3 of the By-Laws, which shall hereafter read as follows:

- "3. The Board of Directors shall appoint a chair of the Audit and Risk Supervision Committee from among the independent directors forming part thereof, as well as its secretary, who need not be a director. The position of chair of the Audit and Risk Supervision Committee shall be held for a maximum period of four (4) years, after which period the chair may not be re-elected until the passage of at least one year from ceasing to act as such, without prejudice to the continuance or re-election thereof as a member of the committee."*

* * *

Bilbao, 18 February 2014



ANNEX – TWO-COLUMN TABLE SHOWING A COMPARISON FOR PURPOSES OF THE PROPOSED AMENDMENT OF THE BY-LAWS (CURRENT TEXT AND AMENDED TEXT SHOWING THE PROPOSED CHANGES)

Current Text of the <i>By-Laws</i>	Text of the Proposed Amendment
Article 34. Powers of the Board of Directors	Article 34. Powers of the Board of Directors
5. In particular, the Board of Directors, acting upon its own initiative or at the proposal of the corresponding internal decision-making body, shall occupy itself with the matters set forth below (as an example only):	5. In particular, the Board of Directors, acting upon its own initiative or at the proposal of the corresponding internal decision-making body, shall occupy itself with the matters set forth below (as an example only):
<p>A. With respect to the General Shareholders’ Meeting:</p> <p style="padding-left: 40px;">c) Propose to the shareholders at a General Shareholders’ Meeting the amendment of the Regulations for the General Shareholders’ Meeting.</p>	<p>A. With respect to the General Shareholders’ Meeting:</p> <p style="padding-left: 40px;">c) Propose to the shareholders at a General Shareholders’ Meeting the amendment<u>the amendment</u> of the Regulations for the General Shareholders’ Meeting.</p>
<p>C. With respect to information to be provided by the Company:</p> <p style="padding-left: 40px;">c) Approve the Company’s Annual Corporate Governance Report, as well as the Annual Sustainability Report, the <i>Annual Remuneration Policy Report</i>, and any other report that the Board of Directors deems advisable in order to better inform shareholders and investors or that is required by legal provisions applicable at any time.</p>	<p>C. With respect to information to be provided by the Company:</p> <p style="padding-left: 40px;">c) Approve the Company’s Annual Corporate Governance Report, as well as the Annual Sustainability Report, the Annual Remuneration Policy Report<u>annual director remuneration report</u>, and any other report that the Board of Directors deems advisable in order to better inform shareholders and investors or that is required by legal provisions applicable at any time.</p>
D. With respect to the directors and	D. With respect to the directors and

NOTICE. This document is a translation of a duly approved Spanish-language document, and is provided for informational purposes only. In the event of any discrepancy between the text of this translation and the text of the original Spanish-language document that this translation is intended to reflect, the text of the original Spanish-language document shall prevail.

<p>senior officers:</p> <p>d) Approve, upon a proposal of the chairman of the Board of Directors or of the chief executive officer, the determination and modification of the Company's organisational chart, the appointment and removal of senior officers of the Company, as well as set the compensation or indemnification, if any, payable to them in the event of removal.</p> <p>As an exception to the foregoing, based on a proposal made for such purpose by the chairman of the Board of Directors, the Audit and Risk Supervision Committee shall, if applicable, submit to the Board of Directors a proposal supported by the corresponding report regarding the selection, appointment, or removal of the director of the Internal Audit Area.</p> <p>Senior officers shall be those officers who report directly to the Board of Directors, to the chairman thereof, or to the chief executive officer of the Company, and shall in any case include the director of the Internal Audit Area and any other officer given such status by the Board of Directors.</p>	<p>senior officers:</p> <p>d) Approve, upon a proposal of the chairman of the Board of Directors or of the chief executive officer, the determination and modification of the Company's organisational chart, the appointment and removal of senior officers of the Company, as well as set the compensation or indemnification, if any, payable to them in the event of removal.</p> <p>As an exception to the foregoing, based on a proposal made for such purpose by the chairman of the Board of Directors, the Audit and Risk Supervision Committee shall, if applicable, submit to the Board of Directors a proposal supported by the corresponding report regarding the selection, appointment, or removal of the director of the Internal Audit Area.</p> <p>Senior officers shall be those officers who report directly to the Board of Directors, to the chairman thereof, or to the chief executive officer of the Company, and shall in any case include the director of the Internal Audit Area and any other officer given such status by the Board of Directors.</p>
<p>E) Other powers:</p> <p>a) Prepare the <i>Dividend Policy</i> and submit the corresponding proposed resolutions on the</p>	<p>E) Other powers:</p> <p>a) Prepare the <i>Dividend Policy</i> <u>shareholder remuneration policy</u> and submit the corresponding</p>

<p>allocation of profits or losses and other modes of shareholder compensation to the shareholders at the General Shareholders' Meeting, as well as decide upon the payment, if any, of interim dividends.</p>	<p>proposed resolutions on the allocation of profits or losses and other modes of shareholder compensation <u>remuneration</u> to the shareholders at the General Shareholders' Meeting, as well as decide upon the payment, if any, of interim dividends..</p>
<p>Article 44. Audit and Risk Supervision Committee</p>	<p>Article 44. Audit and Risk Supervision Committee</p>
<p>3. The Board of Directors shall appoint a chair of the Audit and Risk Supervision Committee from among the independent directors forming part thereof, as well as its secretary, who need not be a director. The position of chair of the Audit and Risk Supervision Committee shall be held for a maximum period of three (3) years, after which period the chair may not be re-elected until the passage of at least one year from ceasing to act as such, without prejudice to the continuance or re-election thereof as a member of the committee.</p>	<p>3. The Board of Directors shall appoint a chair of the Audit and Risk Supervision Committee from among the independent directors forming part thereof, as well as its secretary, who need not be a director. The position of chair of the Audit and Risk Supervision Committee shall be held for a maximum period of three (3) <u>four (4)</u> years, after which period the chair may not be re-elected until the passage of at least one year from ceasing to act as such, without prejudice to the continuance or re-election thereof as a member of the committee.</p>