

## 3.2 Networks

### Regulatory environment of the business

#### Spain

- 2019 saw the conclusion of the process to revise remuneration for the distribution activity for the second regulatory period (2020-2025). The new circulars approved by the CNMV provide a new methodology for calculating the continuing financial remuneration rate (WACC), based on remunerating audited investments, recognising efficient operating expenses and establishing incentives to improve losses and the quality of supply. The remuneration rate for the distribution activity is set at 6.003% for 2020 and 5.58% for the remaining years.
- In December 2019 a Ministerial Order was published extending the electricity access tariffs beginning 1 January 2020 on a temporary basis until the publication of new network tariffs and new charges.

#### United States

- New tariffs entered into force in January 2019 for the gas distribution company CNG (Connecticut), and will be in effect for the next 3 years, with financial profitability (ROE) of 9.3%, an equity percentage of 54% and planned investments of \$150 million.
- New tariffs entered into force in February 2019 for the gas distribution company BCG (Massachusetts), and will be in effect for the next 3 years, with an ROE of 9.7% and an equity percentage of 54%.
- In October 2018 a new 1-year tariff proposal was presented for the electricity distribution company CMP (Maine). The final determination by the regulator and the entry into force is expected during the first quarter of 2020. The same conditions set in 2014 were maintained during 2019, with an ROE of 9.45% and an equity percentage of 50%.
- The tariff conditions for the gas distributors of the State of New York (NYSEG and RG&E) were maintained during 2019, with a recognised ROE of 9.0%. In May 2019 a new 1-year tariff proposal was presented and is now being negotiated with the regulator and would enter into force in April 2020.

#### United Kingdom

- Ofgem continues the process of designing the RII02 regulatory framework. The new periods will be 5 years instead of the current 8 years, and the cost of equity, which will be decided in 2020, is linked to the CPIH (inflation) index. RII0-T2 for transmission is in a more advanced state of development and will enter into force in 2021, while RII0-D2 relating to distribution will apply beginning in 2023.
- Until then, SP Transmission Ltd. as well as SPD Ltd. and SPM Plc continue to perform their activities under the RII0-T1 and RII0-D1 tariff frameworks, complying with all investment and quality goals agreed with Ofgem.

#### Brazil

- In August 2019 the 5th Tariff Review of Elektro was approved and will be in effect for the next 4 years beginning on 27 August 2019. The regulatory asset base (RAB) is R\$3,900 million and is expected to increase to R\$5,800 million by the end of the regulatory period, with an investment effort of R\$2,800 million during the period.
- In April there was an annual period adjustment for Coelba, Cosern and Celpe that mainly reflects the change in the General Price Index and recognises the improvement in supply quality.
- Neoenergia won a transmission projects in the auction by the Brazilian regulator ANEEL in December 2019 for the construction of a 210 km line and a 1,000 MVA substation.
- Neoenergia has been awarded a total of 11 projects in auctions from 2017, 2018 and 2019 for a total investment of approximately R\$8,000 million.
- The Energy Research Office (*Empresa de Pesquisa Energética*) has also published the schedule of new auctions (two per year), which will take place until the end of 2021.

## Objectives, risks and principal activities

### Objectives

- Zero accidents.
- Offer our customers excellent service based on the quality of supply and information regarding the network.
- Maximise efficiency in system operations through operational excellence and the digitisation of our assets.
- Lead the energy transition towards a cleaner model favouring a more efficient integration of renewable energy (centralised and distributed) and the penetration of electric vehicles through the use of smart grids.

### Significant risks

- Operational risks: impacts on supply as a result of meteorological events and work-related and third-party accidents at owned facilities.
- Technological and cybersecurity risks affecting the security of the facilities and service to our customers.

### Principal activities 2019

- **Spain:** After the deployment of 10.8 million smart meters, which was completed in 2018, the digitisation of the low-voltage network is being extended to favour the penetration of renewables, which extension is expected to be completed in 2020.
- **United Kingdom:** Implementation of investments set out in RIIO-T1 and RIIO ED1. Joined the *Low Carbon Strategic Partnership*, focused on the role of electricity networks in favouring the energy transition. Investment of £20 million within the *Green Economy Fund* to finance 33 local projects in Scotland to favour decarbonisation and £8 million to accelerate the deployment of electric vehicle recharging infrastructure.
- **United States:** Progress in obtaining permits for the *New England Clean Energy Connect (NECEC)* project awarded in 2018, with a planned investment of \$950 million, for the construction of a 233 kilometre transmission line between Canada and New England, which will allow for the supply of 1,200 MW of 100% hydroelectric power to Massachusetts beginning in 2022.
- **Brazil:** Progress as planned in the construction of 10 transmission projects awarded in the 2017 and 2018 auctions, completing the startup of one of these projects in 2019.

### Customer service

- In Spain, the new brand *i-DE Redes Eléctricas Inteligentes, S.A.U.* has been launched to favour identification by customers and avoid confusion with the retailers of the group. The digital channels have also been renewed, providing customers with all of their consumption information in real time.
- A record quality level was once again reached in Brazil, with a 10% decrease in the Equivalent Duration of Interruption (DEC) compared to 2018.
- 2019 was a year with strong storms in all of our distribution areas, which required tremendous efforts to restore supply. The good performance of the electric grid in view of the strong "cold drop" (*gota fría*) in the southeast of Spain during September is noteworthy.
- The companies UI and CMP received the *EEI Emergency Recovery Award* for their extraordinary response to the strong storms of May 2018 and October 2019, respectively.
- SPEN achieved the prestigious BSI (British Standards Institution) Kitemark quality certification mark, becoming the first utility to receive this mark. At the end of November 2019, SPD and SPM are in 1st and 3rd place in customer service among UK distributors, according to the regulator.

### Operational excellence

- The adjusted evolution of operating expenses continues in order to maintain and improve efficiency ratios in all countries.
- New plans and models have been launched to end electricity fraud in electricity consumption in Spain and Brazil, and also to comply with the parameters defined by the regulators.
- They improve the loss indicators in Brazil as a result of the fraud reduction plan.

### Digitisation of the network

- In Spain the *Smart Cities* initiative has launched in order to contribute to the country's main municipalities advancing in their transition towards smart cities. Collaboration agreements have been reached with eight government administrations, including the municipalities of Madrid and Murcia and the Provincial Council of Castellón, to expand the possibilities of a smart and digitalised grid.
- Six Electric Mobility Control Centres have also been created to monitor and evaluate the impact of electric vehicles on the distribution network.

## Key figures of the Networks Business

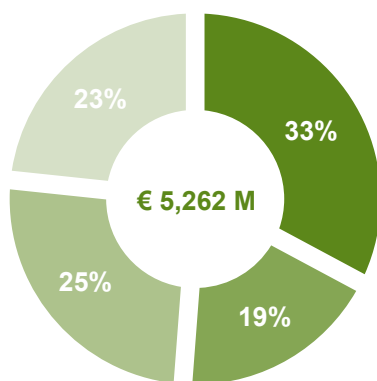
Item	Unit	Spain		United Kingdom		United States		Brazil		Total	
		2019	2018	2019	2018	2019	2018	2019	2018	2019	2018
Gross margin	€M	2,117	2,109	1,311	1,222	2,875	2,780	1,828	1,530	8,131	7,641
EBITDA	€M	1,711	1,709	987	919	1,330	1,331	1,234	955	5,262	4,915
Distributed electricity	GWh	93,516	93,881	33,670	34,659	38,441	39,579	67,875	65,290	233,502	233,409
Supply Points (Electricity) <sup>1</sup>	Millions	11.1	11.1	3.5	3.5	2.3	2.3	14.1	13.8	31.0	30.7
Gas supply	GWh	--	--	--	--	64,234	65,140	--	--	64,234	65,140
Supply Points (Gas)	Millions	--	--	--	--	1.0	1.0	--	--	1.0	1.0
Gross investments	€M	537	458	736	625	1,435	1,165	916	811	3,624	3,059
Workforce	No. of people	3,574	3,743	3,000	2,963	5,375	5,325	11,310	10,360	23,259	22,391

🕒 Quarterly Results Report

International Financial Reporting Standard (IFRS) 11 has been applied to the financial information.

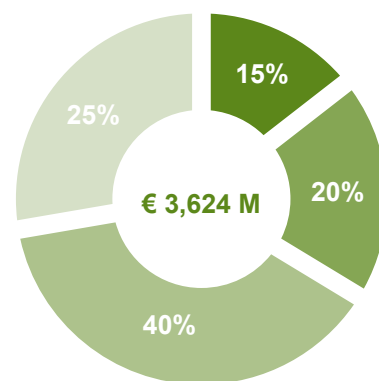
(1) Supply points in Spain include Conquense and other small distributors.

### EBITDA of the Networks Business by geographical area 2019



■ Spain ■ United Kingdom ■ United States ■ Brazil

### Gross investments of the Networks Business by geographical area 2019



■ Spain ■ United Kingdom ■ United States ■ Brazil