



TITLE II

MAIN ASPECTS OF
CORPORATE GOVERNANCE
AT RED ELÉCTRICA
AND RELATED PRINCIPLES
AND PRACTICES





CHAPTER I

PRINCIPLES AND PRACTICES OF RED ELÉCTRICA IN MATTERS OF CORPORATE GOVERNANCE

Principles of corporate governance: The Corporate Governance Policy

At its meeting on 25 November 2014, the Board of Directors approved Red Eléctrica's **Corporate Governance Policy**, which states the principles that must govern its relations with stakeholders. Those principles are as follows:

- To consolidate, develop and promote symmetrical mechanisms for dialogue and engagement with shareholders, investors and leading stakeholders in order to improve relations, strengthen commitment and reinforce trust.
- To promote the informed participation of company shareholders at Shareholders' General Meetings.
- To adopt the necessary measures to ensure the proper exercise of shareholder rights at Shareholders' General Meetings.

- To exert the necessary control and supervision in the areas that are most critical and relevant to the Company, with certain responsibilities being reserved to the Board of Directors under the Board Regulations.
- To preserve an adequate balance and proportionality in the powers inherent to the Board of Directors' structure and composition, by adopting the necessary measures to enable action with unity of purpose and independence of judgement, pursuing the interests of the Company and its shareholders, as well as the Company's sustainability.
- To ensure that appropriate procedures exist to select directors, ensuring a reasonable balance and diversity among Board members when performing their task.
- To strengthen the Company's commitment to diversity of knowledge, experience and gender in Board and committee composition.
- To establish adequate mechanisms to define the duties and responsibilities of directors and to disclose and resolve any potential conflicts of interest between directors and the Company.

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



- To consolidate a remuneration policy for the Board of Directors, based on moderation, effective dedication and alignment with the long-term strategies and interests of the Company and its shareholders.
- To consolidate the practice of presenting the policy on directors' remuneration, the directors' remuneration for the year and the annual directors' remuneration report to the Shareholders' General Meeting for approval.
- To guarantee quality and efficiency in operation and performance of the Board of Directors, the Chairman of the Board and the Company's Managing director and Board committees, through an annual assessment, ensuring that support and assistance is received from independent external advisors.
- To arrange continuous training for directors in various fields and activities of the Company, through an annual training and information plan.
- To guarantee an orderly succession of the Company's Managing director, so as to ensure continuity and sustainability in the Company.
- To establish the necessary mechanisms and instruments to ensure that the Company identifies, analyses and adopts, as necessary, the best practices, principles and recommendations in corporate governance matters, following the Company's adopted principle of excellence in action.

- To guarantee transparency and utmost quality in information, in such a way that the Company's public information is presented in a clear, complete, simple, orderly and comprehensible manner for the various stakeholders.
- To continuously review, update and improve the content and structure of the corporate website, applying international standards.
- To encourage awareness of the principles and values behind the Company's Corporate Governance Policy, both internally within the organisation and externally among all stakeholders.

Red Eléctrica's main corporate governance practices

One of Red Eléctrica's main challenges is to implement the corporate governance practices demanded by its shareholders, in Spain and worldwide, proxy advisors and other bodies, both international [such as the OECD and the International Corporate Governance Network] and national [CBGSC].

Besides analysing the principles set out above, the Company's Corporate Governance Policy also states the practices the Company follows or has undertaken to adopt in compliance with those principles. Taken together, these principles and practices constitute Red Eléctrica's Corporate Governance Policy.



The best practices followed by the Company in relation to its Corporate Governance Policy principles are summarised below, although some of the commitments contained in this policy, which are part of Red Eléctrica's corporate governance roadmap, are described in more detail in a later section [Title IV].

In relation to the Company's shareholders:

> Engagement

Further to the *principle of consolidating, developing and encouraging symmetrical mechanisms for dialogue and engagement with shareholders and investors*, Red Eléctrica tries to fulfil the needs of foreign institutional shareholders, given their large presence in the Company's shareholding, as well as the most important proxy advisors and other stakeholders, in order to improve its relations, increase engagement and strengthen their trust, without prejudice to the guarantees and equal treatment enjoyed by other shareholders.

It should be briefly noted here (more detailed information is provided later) that in October 2016 the Board of Directors approved a document setting out the Criteria for communication with shareholders and proxy advisors, which are designed to make the communication more effective and more transparent.

> Shareholders' General Meeting

Further to the *principle of promoting the informed participation of shareholders at their General Meetings*, the Company publishes and makes available to its shareholders, sufficiently in advance, all documentation related to the various points included in Shareholders' General Meeting agendas.

Furthermore, in relation to the *principle of guaranteeing the adequate exercise of shareholder rights at their General Meetings*, the Company implements mechanisms and adopts measures to enable the performance of tasks and competences entrusted at all times, by law and best corporate governance practices, to the Shareholders' General Meeting.

Regarding the Board of Directors and its committees:

> Basic tasks and operation of the Board

In order to apply the *principle of exercising the necessary control and supervision in the areas that are most critical and relevant to the Company*, the Board has been entrusted with the following basic tasks, among other direct and reserved responsibilities (some of which are extended in the amendment to the Board of Directors Regulations approved on 20 December 2016):

- To approve the basic action guidelines and general policies and strategies of the Company and its Group, in particular the tax strategy and including, among others, the strategic or business plan of the Company and its Group, the investment and financing policy, the corporate governance policy of the Company and the Group of which it is the controlling company, the corporate responsibility policy, the remuneration policy for senior managers who report directly to the Board, the Chairman or the Managing director, the policy on the performance assessment of the Board and directors, and the policy on communication and contact with shareholders, institutional investors and proxy advisors.
- Likewise, to approve a policy to control and manage the main risks of the Company and its Group and to supervise all internal control, prevention and information systems.
- To effectively supervise the senior management team.

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



In order to perform its direct responsibilities and other tasks and responsibilities, the Board of Directors ordinarily convenes once a month and no less than eight times a year.

Furthermore, at the Chairman's request, it may meet as many times this is deemed appropriate for the Company's adequate operation.

Likewise, it will meet whenever a meeting is requested by the Lead Independent director or three directors.

The Board draws up an annual schedule of ordinary meetings and prepares its agenda in accordance with a structured list of matters to be discussed.

> Balance of powers in the structure and composition of the Board of Directors

The Board carries out its tasks further to the *principle of action with unity of purpose and impartiality, pursuing the interests of the Company and of its shareholders, as well as the sustainability of the Company*. To do this, it preserves an adequate balance and proportionality in the powers entrusted to Board members.

The main counterbalancing measure in the composition of the Company's Board of Directors is the separation of the positions of Chairman of the Board (non-executive) and Managing director, following the separation of the two positions initiated at the Shareholders' Extraordinary General Meeting held on 17 July 2015 and completed at the Shareholders' Annual General Meeting of 15 April 2016.

In addition, Red Eléctrica imposes a requirement on itself to have a majority of independent directors on the Board. The principle of having an effective majority of independent directors on Board committees, which is derived from the principle of having a majority of independent directors on the Board, applies to all Board committees, irrespective of their legal or regulatory name and type. Furthermore, each committee is chaired by an independent director and all the members are non-executive directors.

The structure of Red Eléctrica's Board of Directors includes a Lead Independent director, approved by the Shareholders' General Meeting and regulated in its corporate rules. The Lead Independent director is entrusted with organising possible common positions adopted by non-executive directors and acts as a channel for interlocution or as a spokesman of such common positions before the Board Chairman, the Board itself and its committees. One of the functions of the Lead Independent director is that of calling Board of Directors meetings, for properly justified reasons, if the request for a meeting has not been met by the Board Chairman.

Under the Board Regulations, the Board of Directors also has a wide range of reserved responsibilities, which cannot be delegated, and the Company is committed to permanently examining other possible additional measures to ensure a proper balance of powers and responsibilities on the Board. [This applies particularly when the positions of Chairman of the Board and Managing director are held by the same person, although currently they are separated].



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA



TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE



OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA

TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE

OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

> Appointment of directors

Red Eléctrica applies the *principle of ensuring that appropriate procedures exist to select directors, guaranteeing a reasonable balance and diversity within the Board of Directors in order to adequately perform its tasks.* Accordingly, when assessing candidates in the selection process, the competences, experience, professionalism, suitability, independence of judgement, knowledge, qualities, abilities and availability of the members of the Board of Directors are taken into account at all times.

> Directors' responsibilities

Further to the *principle obligating the Company to establish adequate mechanisms to define directors' duties and responsibilities* in general, and the duties of care and loyalty in particular, complete internal regulations have been established in accordance with the provisions of current law at all times.

Following the entry into force of Act 31/2014 of 3 December, amending the LSC for the improvement of corporate governance, the duties of care and loyalty have been amended, which is why in December 2016 the Board of Directors Regulations were adapted to the new rules on directors' duties.

> Conflicts of interest

Further to the *principle of establishing adequate mechanisms to disclose and resolve potential conflicts of interest between directors and the Company*, the Company has control mechanisms and measures in place to prevent any potentially affected director from participating in matters in which he or she may directly or indirectly have a personal interest, giving priority to the corporate interest at all times.

> Remuneration policy of the Board of Directors

The Company applies the *principle of setting a remuneration policy for the Board of Directors based on moderation, effective dedication and alignment with the long-term strategies and interests of the Company and its shareholders and other stakeholders*, so that the remuneration is sufficient to act as an incentive without compromising the directors' independence. To do this, it conducts comparative analyses with other comparable companies and keeps permanent contact with its shareholders and proxy advisors.

Further to the *principle of submitting the annual remuneration, the remuneration report and the remuneration policy for the Board of Directors to the Shareholders' General Meeting for approval*, the Company for several years now has been following the practice of bindingly submitting these matters as separate items on the agenda at Shareholders' Annual General Meetings.

> Diversity on the Board of Directors

The Company applies the *principle of promoting diversity in knowledge, experience and gender among Board and committee members*, as an essential factor to enable it to achieve its objectives from a plural and balanced perspective.

> Assessment of the Board of Directors

For many years Red Eléctrica has applied the *principle of conducting an annual assessment of the functioning and performance of the Board of Directors, the Chairman of the Board and the Managing director and the Board committees, ensuring that support is received from independent external advisors* (as has been the case in the last three years). The process is carried out under the supervision of the



Appointments and Remuneration Committee, in coordination with the Lead Independent director, and a summary of the conclusions is published voluntarily in this report.

> Directors' training and information plan

Further to the *principle of arranging continuous training of directors on the Company's various fields and activities*, the Company has undertaken to keep an updated Annual Training and Information Plan for Directors, enabling them to expand their knowledge of the Company's various fields and activities, particularly those that are predominantly technical. For years now, informative meetings are held prior to ordinary Board meetings and arranged visits are made to Red Eléctrica centres and facilities, so that directors have direct knowledge and experience of the Company's activities.

> Succession Plan for the Company's Board Chairman

Following the *principle of ensuring an orderly succession of the Company's Chief Executive, so as to preserve long-term business continuity and sustainability*, the Company is committed to arranging an orderly succession of its Board Chairman. To do this, the Company has a Succession Plan for the Board Chairman, which is periodically updated. As mentioned in Chapter II of Title I above, a review of the Succession Plan was started in 2016, with the support of an international outside consultant, with a view to keeping the plan up to date and in line with the Company's Corporate Governance Policy, the reforms of the LSC and the abovementioned amendments to the Board of Directors Regulations and, in particular, to adapt

it to the new non-executive role of the Chairman of the Board of Directors; and also with a view to preparing a specific new succession plan for the managing director, following completion of the separation of the two positions approved at the Shareholders' Annual General Meeting held in April 2016 and the attribution of new functions to each position.

> Secretary of the Board of Directors

Further to the principle, adopted by Red Eléctrica, of establishing the necessary mechanisms and instruments to ensure that the Company identifies, analyses and adopts the relevant best practices, principles and recommendations in good corporate governance matters, the secretary of the Board of Directors, further to the duties entrusted in the Bylaws and Board Regulations, provides the Board of Directors and its committees with the necessary mechanisms and instruments to identify, analyse and, where appropriate, propose the adoption of corporate governance best practices, principles and recommendations, allowing the Company to monitor developments in those practices and adequately disseminate them among its stakeholders.

Regarding the principles of information transparency and dissemination of corporate governance policy:

The starting point is the principle of guaranteeing transparency and utmost quality in information, in such a way that the Company's public information is presented in a clear, complete, simple, orderly and comprehensible manner for the various stakeholders, undertaking a commitment to encourage awareness of Corporate Governance Policy principles and values.



Further to the principle establishing a commitment to *review, update and permanently improve the content and structure of the corporate website*, international standards are taken into account in order to include the most relevant information for the Company's stakeholders, improving the accessibility, functioning and information quality of the website.

The Company undertakes to prepare the annual corporate information in accordance with the main international standards and, where there is no audit obligation, considers the possibility of having external audits conducted by specialised consultants and auditors.

In 2016 the Company published on the corporate website a brief history of its Corporate Governance since the 1999 IPO, further details of which will be provided later in this report.

Some of the foregoing practices, set out in the Corporate Governance Policy, are described below as they relate to shareholders, the Board of Directors and its committees and relations with the external auditor, with a special section on the process of separation of positions, which was completed at the Shareholders' Annual General Meeting held in April 2016.

Relations with shareholders and institutional investors

Over the last few years, Red Eléctrica has significantly progressed in transparency and good governance matters. Good governance requires that its stakeholders have regular and prompt access to relevant, sufficient and reliable information, both in relation to the rules and governance of the Company and the results obtained.

Consequently, in addition to keeping the market regularly informed during 2016 by sending the relevant market memos and organising activities with institutional investors, Red Eléctrica has included all relevant information and communications on its corporate website.

The best practices followed in 2016 in corporate governance matters, focusing on dialogue and engagement with shareholders, are described below:

- Update and continuous improvement, under international standards, of the information contained on the corporate website in relation to corporate governance.
- Participation in national and international corporate governance forums, working groups and initiatives [International Corporate Governance Network, Institute of Directors, Spanish Issuers, etc.].
- *Roadshows with foreign shareholders and proxy advisors on corporate governance.*

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



- International external advice in corporate governance matters.
- Self-assessment of the Board, with specialised external support.

In 2013 the Company became a member of the world organisation for corporate governance, the International Corporate Governance Network, which brings together foreign institutional investors, large corporations, regulators, academics, proxy advisors and other corporate governance specialists. It considers its growing participation in this organisation to have been very positive.

The Company's relations with its shareholders and institutional investors are generic, not particularly or specifically held with any of these.

The Company also ordinarily arranges roadshows presented by the Company's top level managers, on leading financial markets in Spain and abroad, with a larger presence of institutional investors, in order to provide information on its activities and business development, trying to thus approach this specific group of investors.

In light of the high percentage of foreign institutional shareholders (close to 70%), in January and February 2016 and 2017, as in previous years, the Company launched a programme of contacts with and visits to investors and proxy advisors in order to gather relevant and up-to-date information and also to directly explain the Company's practices and actions in corporate governance matters.

The aim is to consolidate adequate mechanisms for regular exchange of information with national and foreign institutional investors and the most prominent proxy advisors, thereby adjusting to the latest international standards in corporate governance.

Under no circumstances does the Company provide institutional shareholders with information that is liable to place them in a privileged or advantageous situation with respect to other shareholders; the information it provides is always public information, presented in a rational and ordered form.

On 25 October 2016, at the proposal of the Appointments and Remuneration Committee and in fulfilment of its commitment to implement Recommendation 4 of the Code of Good Governance of Listed Companies, the Board of Directors approved the Criteria for communication with shareholders, institutional investors and proxy advisors.

This document contains the policy on communication with the abovementioned stakeholders and includes principles and guidelines to ensure that they are able to exercise their rights, protect their interests and promote engagement with them through open, transparent and sustainable dialogue.

The Criteria for communication with shareholders, institutional investors and proxy advisors are published on the Company's website [www.ree.es].



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA



TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE



OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER



Separation of the positions of Chairman of the Board of Directors and Managing director (Chief Executive) of the Company

At its meeting on 12 June 2015, at the proposal of its Chairman, the Company's Board of Directors approved the 'Report on the separation of the positions of Chairman of the Board of Directors and Managing director of the Company', which assesses the benefits of this organisational model for Red Eléctrica and its shareholders, with a view to improving the Company's existing corporate governance structure. The Shareholders' Extraordinary General Meeting held on 17 July 2015 analysed the separation process and, in order to put it into effect, agreed to increase the number of directors by one (setting the total at twelve) and appointed Mr. Juan Francisco Lasala Bernad as an executive director of the Company. At its meeting on 28 July 2015, the Board of Directors appointed the new executive director to be Managing director of the Company.

The reasons that led the Board of Directors to approve the separation of the positions of Chairman of the Board of Directors and Managing director were as follows:

- The Company had been taking steps and implementing new measures in its corporate governance structure since 2012 and, in 2015, considered that the time had come to define and implement a clear, transparent process for transitioning to the new model of separation of roles, which would improve on previous experience and had the backing of its shareholders.
- A growing international current of opinion in the corporate governance field, especially in Europe, recommends that listed companies separate the positions of Chairman of the

Board of Directors and Chief Executive (Managing director), so that each is held by a different person.

- The basic aim is to prevent an excessive concentration of power in the hands of a single person who is both Chairman of the Board of Directors and Managing director, as this could prevent the Board of Directors and the senior management team from performing their supervisory and management functions properly, with the necessary independence and objectivity.
- The accumulation of power in the hands of a Chairman/ Managing director could cause distortions in the performance of the functions of the Board (guided by its Chairman) and the senior management team (led by the Managing director), giving rise to conflicts of interest which, if not properly resolved, might lead to destruction of shareholder value.
- Although the proxy advisors of the most important international investors and prominent institutional shareholders accepted the temporary adoption of counterbalancing measures to mitigate the excessive accumulation of power, such measures were justified only as a temporary solution, combined with a commitment to formally separate the two roles within a reasonable period. What initially was merely a recommendation to separate the positions has de facto become a demand of institutional shareholders and is gradually being adopted by most listed companies that have a significant proportion of foreign shareholders, as is the case of Red Eléctrica, around 70 % of whose share capital is held by foreign shareholders.
- Added to the demands of shareholders and proxy advisors are those of recognised international bodies and institutions, such as the RobecoSam Dow Jones Sustainability World



Index [DJSI], which annually assess the corporate social responsibility practices adopted by large international groups and industrial corporations and listed companies, penalising in their corporate governance scores and classifications those companies that have failed to effectively separate the positions of Chairman and Managing director, as was the case of Red Eléctrica.

- At the time the separation was approved, there was in Spain a growing movement among Ibx 35 companies in favour of separating the two roles, as can be seen in the report published by the CNMV on the 'Corporate Governance Reports of Issuers of Securities Admitted to Trading on Official Secondary Markets' for 2014, which shows that approximately 40 % of Ibx 35 companies had implemented the separation.

The plan provided for a transitional period, which started at the Shareholders' Annual General Meetings held on 17 July 2015 and ended at the Shareholders' Annual General Meeting held on 15 April 2016, when the separation of positions between the Chairman of the Board and the Managing director was completed. Since the 2016 Shareholders' Annual General Meeting, the Chairman of the Board of Directors has had exclusively the responsibilities attached to the position of Chairman.

Transitional period:

► During the transitional period the Chairman of the Board continued to have his executive powers and status as Chairman of the Board of Directors, with the responsibilities and functions pertaining to that position.

As Chairman of the Board, besides the powers established in the LSC [Article 529 *sexies*], the Bylaws [Article 20, 21 and 25] and the Board of Directors Regulations [Article 9], the Chairman also had the following basic powers:

- Power to direct and steer the Board's general oversight function.
- Power to guide and steer the approval by the Board of Directors of the Company's and the Group's Strategic Plan and proper supervision of its execution.
- Power to direct and coordinate the approval by the Board of Directors of the Company's and the Group's risk control and management system and the necessary supervision of its implementation and proper functioning.
- Power to guide the Board's actions in relation to proposals for the appointment and removal of senior managers and to direct and steer the supervision of senior management by the Board.

As regards the executive functions during the transitional period, the Chairman of the Board focused on the management, oversight and supervision of the transfer of powers and the effective exercise of executive responsibilities by the Managing director, so that both processes took place in a rational and orderly fashion.

For the duration of the transitional period, the Chairman of the Board retained the necessary powers to ensure that the organisational unit Red Eléctrica de España, S.A.U., which acts as electricity system operator, had the necessary operational autonomy in the required functions, in accordance with

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



applicable regulations. During that period, consideration was given to the functions that by their nature were transferred directly to the Managing director.

- ▶ In July 2015, following the Shareholders' Extraordinary General Meeting, the Board of Directors appointed the new executive director as Managing director of the Company and approved the delegation of executive authority and responsibilities to the Managing director, thus initiating the process that should ensure stability in the transition to the new organisational model.

- ▶ The Managing director, for his part, assumed the functions of his position, which were governed by the Chairman of the Board, who retained executive authority for that purpose throughout the transitional period.

The powers of the Managing director were focused on:

- ▶ Executive management, coordinating and driving the management of the Company's and the Group's business areas.
- ▶ Leadership, initiative and guidance of the execution and implementation of the Company's and the Group's Strategic Plan.
- ▶ Efficient implementation of the risk control system approved by the Board of Directors in the Company and the Group and proper oversight of its functioning.
- ▶ Regular reporting to the Board of Directors on the degree of execution and implementation of the Strategic Plan, the functioning of the risk management system and progress in the management of the Group's business areas, so that the Board was able to adequately and effectively exercise its general oversight and control function.

Completion of the process:

- ▶ The transfer of executive functions and responsibilities to the new Managing director was completed at the Shareholders' Annual General Meeting held on 15 April 2016, which approved the re-election of Mr. José Folgado Blanco, Chairman of the Company's Board of Directors, as an 'other external' director for a period of four years. Mr. Folgado thus ceased to be an executive director.
- ▶ Following said Shareholders' General Meeting, as a result of the final transfer of the Chairman's executive functions to the Managing director, the Board of Directors adopted the necessary resolutions for the distribution of responsibilities and functions between the two positions on the terms approved in the separation process. In particular, it resolved to revoke the Board authority delegated to the Chairman and the authorities currently granted to the Chairman, given the eminently executive nature of those authorities, and maintained the delegation of all the authorities to the Managing director.
- ▶ In addition, the Board of Directors granted new authorities and powers to the nonexecutive Chairman of the Board of Directors, in accordance with the responsibilities of the position.

The Board of Directors

- ▶ Small number of directors [122 members following the Shareholders' Extraordinary General Meeting held on 17 July 2015, which resolved to increase the number of directors by one and appoint a new executive director].
- ▶ One executive director [since the Shareholders' Annual General Meeting held on 15 April 2016, which resolved to re-elect Mr. José Folgado Blanco as a director in the 'other

[2] As of 31 December 2016, the Board of Directors was made up of 11 members, as an independent director position was left vacant by the resignation of the Independent director Mr. Agustín Conde Bajén, which was accepted by the Board of Directors on 29 November 2016.

At its meeting on 31 January 2017, the Board of Directors appointed Mr. Arsenio Fernández de Mesa y Díaz del Río, an independent director, to fill that vacancy until the next Shareholders' Annual General Meeting.



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA



TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE



OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA

TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE

OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

external' category, so that he lost his status as an executive director. As already mentioned, before that Shareholders' General Meeting and ever since the Shareholders' Extraordinary General Meeting held on 17 July 2015, there had been temporarily two executive directors. The executive director is the Managing director. The authorities and responsibilities of the executive director are limited by:

- The responsibilities reserved to the Board of Directors, 58.3% of which consists of independent directors (counting the independent director vacancy existing at 31 December, following the resignation of Mr. Agustín Conde Bajén in November 2016).
 - The effective control exercised by the Board of Directors, at each monthly meeting, over the ordinary activities of the executive directors.
 - The immediate effective control exercised by the Board of Directors, at each monthly meeting, over any extraordinary or urgent measures taken by the executive director.
 - The functions and responsibilities assigned to the Board committees, a majority of whose members are independent directors, under the Bylaws and Board of Directors Regulations.
 - The responsibilities of the Lead Independent director.
- The core responsibilities for the administration of the Company are expressly reserved to the full Board of Directors. These responsibilities, which are listed in Article 5 of the Board of Directors Regulations, were expanded following the amendment to the Board of Directors Regulations passed on 20 December 2016, which adapted that article, mainly in line with Articles 249 *bis* and 529 *ter* of the LSC. The reserved responsibilities cannot be exercised either by the executive director or by the Board committees.

- The percentage of independent directors (58.3%) is greater than required by international standards.
- The Board of Directors has for many years been committed to gender diversity targets. Four of its eleven members, who at 31 December 2016 represent 36.4% of the Board, are women. This puts the Company in one of the leading positions among IBEX 35 companies. The Board of Directors prepares and approves an annual gender diversity report, which this year has been made available on the Company's website.
- A participative and proactive Board.
- A very high rate of attendance and dedication to the exercise of their responsibilities on the part of the directors.
- Use of new technologies to facilitate the work of the Board and provide directors with information and documentation, through the Director's Portal, which was reviewed and updated during 2016.



The Managing director

- Under the Company's corporate regulations, the Board of Directors, at the proposal of the Appointments and Remuneration Committee, may appoint one or more Managing directors from among its members.
- Under the Company's corporate regulations, the Managing director or directors may be directors other than the Chairman of the Board of Directors and may have such authority delegated to them as is deemed appropriate, although with the necessary scope for the day-to-day conduct and effective management of the Company's business lines, always specifying the content, limits and types of delegated authority.
- Without prejudice to the powers belonging to the Chairman of the Board, the Managing director will act as the Company's Chief Executive and will be responsible for the day-to-day conduct and effective management of the organisation and of the Company's businesses, always in accordance with the decisions and criteria set by the Shareholders' General Meeting and the Board of Directors, each within its remit.
- The position of Managing director and the related delegation of authority is regulated in Articles 22 to 25 of the Bylaws and the responsibilities of the position are regulated in the new Article 11 of the Board of Directors Regulations, following the amendment passed on 20 December 2016.
- Following the appointment of Mr. Juan Francisco Lasala Bernad as executive director of the Company by the Shareholders' Extraordinary General Meeting held on 17 July 2015, the Company's Board of Directors, at its

meeting on 28 July 2015, appointed Mr. Juan Francisco Lasala Bernad as Managing director of the Company, a position he continues to hold at the date of this Annual Corporate Governance Report.

- At its meeting on 31 May 2016 the Board of Directors resolved to revoke the authority granted to Mr. José Folgado Blanco on the grounds that he had ceased to be an executive director at the Shareholders' Annual General Meeting held on 15 April 2016.

The Lead Independent director

- The Lead Independent director is appointed by the Board of Directors from among the independent directors, at the proposal of the Appointments and Remuneration Committee.
- The Lead Independent director's main task is to organise any common positions of the non-executive directors and to serve as a channel or spokesperson for those positions to the Chairman of the Board of Directors, the Board and its committees.
- The term of office is three years and the position holder may be reappointed.
- The Lead Independent director role is currently held by the independent director Carmen Gómez de Barreda Tous de Monsalve, who was reappointed for a further three-year term by resolution of the Board of Directors on 31 May 2016.
- The Lead Independent director convenes and chairs meetings of the independent directors, a role that was exercised in 2016.



- > The roles and responsibilities of the Lead Independent director are set forth in Article 25 *bis* of the Bylaws and are implemented in the new Article 10 [formerly Article 9 *bis*] of the Board of Directors Regulations, as amended on 20 December 2016. The amendment of that article of the Board of Directors Regulations consisted mainly of adapting it to Articles 529 *sexies*, para. 2 and 529 *septies*, para. 2 of the LSC, as well as to Recommendation 34 of the CBGSC.
- > Following completion of the separation of the positions of Chairman of the Board and Managing director of the Company, it has been considered appropriate to maintain this role because, among other things, the Lead Independent director helps maintain the checks and balances within the Board of Directors in favour of the independent directors and because it is a role that has been very well received by shareholders and proxy advisors.

Board committees

- > Formed by the Board of Directors to assist in highly technical matters and provide greater efficiency and transparency, the Board committees support the Board in the performance of its duties.
- > They are made up of qualified professionals who have exercised important responsibilities in other institutions or corporations outside the Company.
- > All their members are non-executive directors.
- > In 2013, the composition of the committees, as specified in the Board of Directors Regulations, was formally adapted to the demands of shareholders, so as to reinforce the

committees' independence. A requirement that both committees have a majority of independent directors was introduced.

- > In December 2016, the functions of the Board committees, as set out in the Board of Directors Regulations, were adapted to the latest reforms of the LSC and the CBGSC and certain adjustments were made to help the committees operate more effectively.
- > The committees are chaired by independent directors, as stipulated by the Bylaws and the Board of Directors Regulations. The committee chairperson's term of office is limited to three years, after which a director may not be re-elected as chairperson until after at least one year's break in service.
- > Since 24 November 2015, each of the two Board committees [Audit Committee and Appointments and Remuneration Committee] has five members. At 31 December 2016, three of the five members of the Audit Committee were independent directors and three of the four members of the Appointments and Remuneration Committee were independent directors [following the resignation of an independent director in November 2016, there was a vacancy on the committee].
- > No directors belong to both committees, thus ensuring their total independence.
- > The committees have monthly meetings, although sometimes, when circumstances so require, they hold extraordinary sessions and are truly specialised technical bodies of great value to the Board.



- ▶ The term of office of all committee members is three years; members may be reelected.
- ▶ The roles and responsibilities of the committees are established in the Bylaws and further specified in the Board of Directors Regulations.
- ▶ Following the reform of the LSC and the approval of the CBGSC, the Company amended its Bylaws in 2015 and the Board of Directors Regulations in 2016, so as to adapt them more completely to the new rules and recommendations on matters that were not previously covered in these corporate regulations. Among the matters that were reviewed in the abovementioned internal regulations are the powers and functions of the committees; and the Board of Directors Regulations were also adapted to improve the organisation and functioning of the committees and the Board itself and to adapt them to the current organisation of the Red Eléctrica Group.

Directors' remuneration policy (non-executive and executive directors)

Reiterated practice followed by Red Eléctrica: Binding approval by the Annual General Meeting as a separate item on the agenda

Since 2010, Red Eléctrica voluntarily submits the Annual Directors' Remuneration Report and, since 2007, the annual remuneration of the Board of Directors to the Shareholders' Annual General Meeting for approval, as separate and independent items on the Shareholders' General Meeting agenda. Consequently, all proposals and opinions on these matters have never been presented to the shareholders on a consultative basis.

This practice continued in 2016, with the submission of the directors' remuneration for 2016, an amendment to the Directors' Remuneration Policy and the Annual Directors' Remuneration Report to the shareholders for approval (in a binding vote), as three separate and independent items on the Shareholders' Annual General Meeting agenda. Red Eléctrica Corporación S.A. thus continues to align itself with corporate governance best practices, giving shareholders the necessary autonomy and independence of opinion to be able to vote on each Shareholders' General Meeting resolution individually and separately.

Remuneration policy principles

The Directors' Remuneration Policy, which was approved by the Shareholders' Annual General Meeting held on 15 April 2015, is based on the following general principles:

- ▶ Balance and moderation.
- ▶ Alignment with the practices demanded by shareholders and investors.
- ▶ Transparency.
- ▶ Voluntary presentation of any decision related to directors' remuneration to the Shareholders' General Meeting for approval.



TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



As regards the remuneration of **executive directors**, the following principles have been established:

- ▶ Alignment of the executive director's remuneration with the Company's strategy.
- ▶ Maintaining a reasonable balance between the various components of [short-term] fixed remuneration and [annual and long-term] variable remuneration, reflecting an adequate assumption of risks combined with the achievement of defined objectives, linked to the creation of sustainable value.
- ▶ Alignment with the remuneration established by comparable companies.

As regards the remuneration of **non-executive directors**, the following principles have been established:

- ▶ Linked to effective time commitment.
- ▶ Linked to responsibility and performance of their tasks as directors.
- ▶ Absence of variable components in remuneration in order to ensure their complete independence with respect to the remuneration paid to the executive director and management team.
- ▶ Sufficient to act as an incentive, without limiting their independence.

On conclusion of the separation of the positions of Chairman and Managing director, the Shareholders' Annual General Meeting held on 15 April 2016 approved an amendment to the Directors' Remuneration Policy. Both the Directors' Remuneration Policy approved in 2015 and the amendment to that policy approved in 2016 are published on the corporate website.

The Appointments and Remuneration Committee deems it appropriate to periodically review the policy on remuneration of the Board of Directors, including in this review process a comparison with reference companies, selecting groups of comparable companies, and maintaining permanent contact with its shareholders and proxy advisors, in order to check the adequacy and moderation of the remuneration paid to directors and executive director in market terms.

All of the foregoing principles conform to the Company's Corporate Governance Policy, approved by the Board of Directors at its meeting of 25 November 2014 and published on the corporate website.

Moreover, said remuneration principles comply with the general rules laid down for capital companies in Article 217.4 of the LSC, regarding the need for remuneration to be commensurate with a company's size and importance, economic position, comparability, profitability and sustainability; and the need not to encourage excessive risk taking and not to reward adverse results.

For more information, please refer to the Annual Directors' Remuneration Report, as soon as it is available and published on the corporate website, and the resolutions on annual remuneration of the Board of Directors for 2017, which are due to be presented for approval to the 2017 Shareholders' Annual General Meeting of Red Eléctrica, as separate items on the agenda.



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA



TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE



OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER



Independence in relations with the external auditor

The Shareholders' Annual General Meeting held on 15 April 2015 approved an amendment to the Bylaws. One of the articles that was amended was Article 23, so as to adapt the powers of the Audit Committee to the requirements of the new Article 529 *quaterdecies* of the LSC, although many of these requirements were already addressed in Article 23 previously. Certain powers concerning the independence of the external were reinforced in sections iv) and v) of the abovementioned Article 23 of the Bylaws. The Board of Directors Regulations have also been amended along the same lines as the Bylaws. In particular, in order to reinforce the independence of the external auditor, the new Article 16.3 of the Board of Directors Regulations was amended to adapt it, above all, to Article 529 *quaterdecies* LSC (amended by Act 22/2015 of 20 July on Auditing) and Recommendation 42 CBGSC. Also, the new Article 16.3 c) of the Board of Directors Regulations establishes that the Audit Committee must each year receive from the external auditor a statement that neither the audit firm nor any of its partners have been convicted of criminal charges linked to the performance of their audit functions.

Similarly, the new Article 42 of the Board of Directors Regulations has been adapted, among other things, to Recommendation 8 of the CBGSC and now imposes an obligation on the external auditor of the Company and, where applicable, of the Group to tender its resignation to the Board of Directors and, if the Board so decides, to resign as auditor if either the audit firm or any of its partners are convicted of criminal offences in relation to the provision of their audit services to the Company or any other party.

The responsibilities of the Audit Committee, as set out in the Board Regulations, include that of receiving information on any non-audit services provided to the Company and the Group by the external auditor (the audit services are reported regularly to the markets through the relevant sections of the Annual Corporate Governance Report, Official Annex, in the form of Annex I of CNMV Circular 7/2015, paragraph C.1.37). Nevertheless, the general rule adopted by the Company, guided by the Audit Committee, is not to use the external auditor for non-audit services from the date on which the auditor is appointed as such by the Shareholders' General Meeting, unless there are exceptional reasons for doing so, which must be adequately explained in the Company's annual public reporting. The purpose of this rule, as stated in Article 42.3 of the current Board of Directors Regulations (formerly Article 45.3), is to minimize the use of the external auditor for non-audit services.

If it were considered necessary to engage the external auditor to provide non-audit services, the engagement would have to be expressly authorized by the Audit Committee.

Also, where there are contractual obligations between the Company and the external auditor that were acquired before the auditor was appointed as auditor, the reason for any payments to be made by the Company after the date



of appointment must be explained in the Annual Corporate Governance Report.

In any case, the requirements and limitations regarding the provision of non-audit services established by Act 22/2015 of 20 July on auditing, in relation to Regulation (EU) No 537/2014 of 16 April, must always be taken into account.

In January 2016, the Company's Audit Committee issued the report on the independence of the external auditor in relation to financial year 2015.

In January 2017, the Company's Audit Committee issued the report on the independence of the external auditor in relation to the financial year commenced 1 January 2016. The report will be published on the Company's corporate website well in advance of the Shareholders' Annual General Meeting of financial year 2016, in accordance with Recommendation 6 of the CBGSC.

As provided in the Audit Act, said report gave an assessment of the non-audit services, taken individually and as a whole, provided by the abovementioned auditors or persons or entities linked to them, in relation to the rules on auditors'

independence and other audit regulations. The report was published on the Company's corporate website.

As the term of the initial appointment had expired, the Shareholders' Annual General Meeting held on 15 April 2016, at the proposal of the Board of Directors, resolved to reappoint KPMG Auditores, S.L. as the auditors of the parent company, Red Eléctrica Corporación, S.A., and its Consolidated Group for a further period of three years, comprising financial years 2016, 2017 and 2018, in accordance with Article 264 of the current LSC.





CHAPTER II

THE SHAREHOLDER STRUCTURE

At the proposal of the Board of Directors, the Shareholders' Annual General Meeting of shareholders of the Company held on 15 April 2016 resolved on a share split that increased the number of the Company's shares by reducing their par value from two euros (€2) to fifty euro cents (€0.50) per share, in the proportion of four new shares for each old share, with no change in the amount of share capital. Consequently, a resolution was passed to amend Article 5.1 of the Bylaws. Following the split, the Company's share capital amounts to 270,540,000 euros, represented by 541,080,000 shares, all of the same class and series, with a par value of fifty euro cents (€0.50) per share, fully subscribed and paid, and represented by book entries. The share split resolution was executed on 11 July 2016.

At 31 December 2016, Sociedad Estatal de Participaciones Industriales (SEPI) directly owned a significant stake in the Company, holding 108,216,000 shares, representing 20% of the capital.

There are no individuals or legal entities that exercise or may exercise control over the Company, as provided in Article 5 of the Securities Market Act, in accordance with Article 42 of the Commercial Code.

The equity of the Company includes a 20% shareholding owned by SEPI, with the remaining 80% being free float, although, as explained below, no other shareholder may own a stake larger than 5%.

Within the free float, there is a high percentage of foreign shareholders, especially of institutional investors, which as of April 2016 accounted for almost 70% of the share capital (of which around 55% is located in the United Kingdom and the USA), which is why the Board of Directors attaches such importance to the international corporate governance practices and recommendations demanded by its shareholders.

The entry into force of Act 17/2007 of 4 July introduced various changes affecting the Company's shareholders. These amendments had, among other aims, that of guaranteeing the independence of the Company vis-à-vis all other electricity sector activities and agents, given that the activities carried on by Red Eléctrica (transport of electricity and operation of the electricity system) are considered by legislators to be an essential service. Royal Decree-Law 13/2012 of 30 March, transposing a number of directives, including Directive 2009/72 of 13 July, stipulating the mandatory independence of distributors and operators of European electricity systems, endorses the legal limitations on shareholdings and political rights applicable to the Company's shareholders and imposes a number





of additional restrictions on companies that perform generation or marketing functions. Royal Decree-Law 13/2012 of 30 March amended the second paragraph of the twenty-third additional provision and Article 34.1 of Act 54/1997 of 27 November. Said additional provision remains in effect pursuant to the express stipulation of the repealing provision of Act 24/2013 of 26 December on the Electricity Sector.

The equity limits stated in the twenty-third additional provision of Act 54/1997 of 27 November are as follows:

- Any individual or legal entity may hold shares in the Company, provided that the sum of their direct and indirect interests in the Company's capital does not exceed 5% of the capital and they do not hold more than 3% of the voting rights. These shares may not be pooled for any purpose whatsoever.
- Parties that engage in activities in the electricity industry, and those individuals or legal entities that directly or indirectly hold more than 5% of their capital, may not exercise more than 1% of the voting rights in the parent company.
- The special regime for SEPI is maintained, whereby it must hold at least ten percent (10%) of the share capital in all cases.

These legal provisions on the general and special shareholding regime are incorporated in Articles 5 and 14 and in the sole additional provision of the Bylaws, and in Article 6.3 of the Company's General Meeting Regulations.

The corporate website

Once again, the Shareholder Structure chapter of this report includes a special section on a basic modern tool for communicating with shareholders, namely, the corporate website.

Apart from the legal and regulatory requirements regarding the website, which are addressed in other sections of this report, it should be highlighted here how important it is for Red Eléctrica to continue to adapt and evolve in the area of corporate governance. The Annual Corporate Governance Report for 2012 emphasized the desirability of enhancing the corporate governance information provided on the Company's website, in line with international standards, and making the information easier for international shareholders and investors to find, understand and use.

The international corporate governance consultants hired by Red Eléctrica have confirmed that foreign institutional investors, which are so important to the Company, in places such as the UK, France, Holland, Germany and the United States, emphasise the difficulty they face in effectively analysing the information relating to the corporate governance structure that is made available on the corporate websites of Spanish listed companies.

**TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES**



Seeing this opportunity for improvement, in 2013 the Company implemented a project to update and improve the corporate website, in order to incorporate the latest practices at enterprise level, also taking into account the requirements and recommendations of the regulatory environment applicable to listed companies. Within the framework of this project, it also conducted an analysis of the corporate governance sections of the website, so as to incorporate leading international standards in terms of structure and content. The new website, with its new structure and design, was launched in October 2013.

The new corporate website most notably included a 'Corporate Governance' section, at the top level of the home page menu, which shows the content sections that are most important to the Company. The improvements to the corporate governance section focused on the structure of the information and the way it was presented, rather than expanding the content published on the website, which was already very extensive but dispersed and sometimes difficult to locate and understand.

The most important corporate governance-related plans for the future listed in the 2013 Annual Corporate Governance Report included a plan to 'Continuously analyse, update and improve the corporate governance information contained on the Company's website in line with international standards'.

The Corporate Governance Policy approved by the Board of Directors on 25 November 2014 also includes the principle of continuously reviewing, updating and improving the content and structure of the corporate website in line with international standards, so as to improve its accessibility, functioning and information quality.

In practice, this principle was effectively applied throughout the year and was applied in 2015: website sections were reviewed, content was improved and additional information was provided, as deemed appropriate.

The 'Corporate Governance' and 'Shareholders and Investors' sections of the corporate website were also reviewed in 2015, in accordance with CNMV Circular 3/2015 of 23 June. A new entry, 'Right of information', was added to the 'General Meeting' subsection of the Corporate Governance section, providing information about the channels of communication between the Company and its shareholders and explaining how shareholders can exercise their right of information.

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



The steps taken in 2016 to improve the information contained on the corporate website include the following:

- In order to meet the Company's commitment to greater transparency in relations with its shareholders and investors and provide more information on the Company's track record and progress in corporate governance, Red Eléctrica has published on its website an interactive section presenting a very visual and easy-access history of the Company's corporate governance, since its IPO in 1999.

This is a completely new practice among companies in Spain and Europe and testifies to the Board of Directors' firm commitment to the implementation and continuous improvement of good governance within the organisation over this period.

- The Company has also published on its website the 'Criteria for communication with shareholders, institutional investors and proxy advisors', which were approved by the Board of Directors on 25 October 2016. These criteria state the principles and guidelines governing the Company's communication with these stakeholders, so as to ensure that they are able to exercise their rights, protect their interests and promote an understanding with shareholders through open, transparent and sustainable dialogue.

- Lastly, a new section has been created called 'Recommendation No. 6 of the Spanish Code of Good Governance', containing all the specific annual reports which that recommendation suggests should be published before the date of the Shareholders' Annual General Meeting.

In summary, the Company is committed to continuously improving and adapting the corporate website as a channel for communication, dialogue and engagement with shareholders, in accordance with its Corporate Governance Policy, and for that reason has maintained that priority in Title IV of this report ['Future plans of Red Eléctrica in matters of corporate governance'].



CHAPTER III THE SHAREHOLDERS' GENERAL MEETING

The Shareholders' General Meeting, duly called and legally convened, represents all of the shareholders and exercises the functions corresponding to it within the Company.

Its resolutions, adopted pursuant to the Shareholders' General Meeting Regulations and the Bylaws, are binding on all shareholders, without prejudice to their legal right of withdrawal. The Shareholders' General Meeting has the power to adopt all resolutions specific to its status as the Company's sovereign body. In particular, and without limitation, it is responsible for:

- Approving the Company's individual and consolidated financial statements, its management by the Board of Directors, and the proposed allocation of profits.
- Appointing and removing directors, ratifying, as necessary, their appointment by cooptation, and appointing and reappointing the auditors.
- Approving plans or authorizing transactions involving treasury stock.
- Approving the establishment of remuneration systems linked to the share price for directors.
- Resolving to issue debentures, increase or reduce share capital, change the legal form, merge, spin off or wind up the Company, and make any amendment to the Bylaws.
- Authorising the Board of Directors to perform a capital increase pursuant to the provisions of the LSC.
- Approving operations whose effect would be equivalent to the modification of the Company's corporate purpose.



TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



Following the amendment approved by Act 31/2014 of 3 December, the LSC increased the number of matters reserved to the Shareholders' General Meeting, which include, on a general basis, the acquisition, disposal or contribution of essential assets to another company (Article 160.f) LSC) and, in the specific case of listed companies, the transfer to subsidiaries of essential activities previously carried out by the Company itself; transactions whose effect is equivalent to the liquidation of the Company; and approval of the Directors' Remuneration Policy (Article 511 *bis* LSC).

Furthermore, the rule contained in Article 161 LSC, previously reserved to limited liability companies, whereby the Shareholders' General Meeting may participate in management matters (giving instructions to the management body or presenting for its authorization the adoption of decisions or resolutions on certain management matters), was extended to all capital companies.

The rules on the organisation and functioning of the Shareholders' General Meeting are contained in the Bylaws (Article 11 through 18) and in the Shareholders' General Meeting Regulations.

For some time now, resolution proposals have been published in full, in Spanish and in English, together with the Notice of Shareholders' General Meeting, with all the relevant information for shareholders being posted on the Company website, which is designed to make it easier for shareholders to exercise their right of information. The Company's website is a suitable mechanism for communicating with shareholders and investors, given that the following information, among others, is posted on it:

- The quorum requirement and the result of the votes on each of the resolutions approved by previous Shareholders' General Meetings.
- Information relating to the right of attendance and procedures for granting proxies for Shareholders' General Meetings, in accordance with the provisions of the Bylaws and the Shareholders' General Meeting Regulations.
- Information on electronic voting and proxies.
- Information on issuances of securities.
- Information on the ratings granted by credit rating agencies.
- Increased information about the Company's shareholders, with greater detail on significant holdings, treasury stock and shareholder agreements.

TITLE III
THE YEAR 2016
IN RED ELÉCTRICA

TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE

OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



Act 25/2011 of 1 August introduced a number of changes relating to the website content of listed companies; in particular, as regards the information that must be published on the website when calling a Shareholders' General Meeting. Despite the fact that, in large part, such information was already published on the Company's website, the Shareholders' Annual General Meeting held on 19 April 2012 approved an amendment to the relevant article of the Shareholders' General Meeting Regulations to incorporate the content required under the Act.

The said Shareholders' General Meeting held on 19 April 2012 ratified the creation of the corporate website of the Company at the domain www.ree.es, for the purposes of the provisions of Article 11 *bis* of the revised LSC.

Order ECC/461/2013 of 20 March [which is currently in force, as it was not repealed with the approval of the latest amendments to the LSC], which determines the content and structure of the Annual Corporate Governance Report, the annual remuneration report and other reporting documents of listed companies, describes the relevant information to be included on the websites of listed companies; however, the current corporate website not only contains all the information identified in the said Order, but it has also been expanded and improved in 2013, 2014, 2015 and 2016.

By voluntarily creating the 'Corporate Governance' section in 2013, the quality of shareholder information was improved.

Furthermore, also worthy of note are the following actions conducted by Red Eléctrica to facilitate the exercise of the right of information of the shareholders at the Shareholders' General Meeting:

- Call notices are always posted more than one month in advance, which is the established statutory period.
- All documentation submitted for approval by the Shareholders' General Meeting and especially the financial statements and the Annual Corporate Governance Report, are made available to all shareholders at the corporate headquarters, on the website and at the Shareholder Information Office.
- An entire section of the Shareholders' General Meeting agenda is devoted to reporting on the principal characteristics of the Annual Corporate Governance Report.
- The annual reports on the activities of the Audit Committee and the Appointments and Remuneration Committee are made available to all shareholders in the Annual Corporate Governance Report and are published on the corporate website.
- A Shareholder Bulletin is published quarterly, containing the main news regarding the Company.
- The chairman of the Audit Committee is available to all shareholders during Shareholders' General Meetings to deal with any matters falling within his remit that may arise, a fact which is communicated to the shareholders during the Shareholders' General Meeting.



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA



TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE



OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER



- The items included on the agenda for the Shareholders' General Meeting are provided in as much detail as possible.
- Separate voting on each item is permitted, including remote voting, with a view to giving shareholders full decision-making freedom and independence in respect of each item submitted to a vote.
- The Shareholder Information Office specifically deals with requests made by company shareholders. Shareholders may also submit questions in writing regarding the information available to the public or notified to the competent authorities and make inquiries through the Shareholder Information Office.
- In 2016, the Annual Report on Related-Party Transactions, the Annual Corporate Responsibility Report (which has been published for several years already) and the Report on the Independence of the external auditor were published on the corporate website in time for the Shareholders' Annual General Meeting, all this in accordance with Recommendation No. 6 of the CBGSC.
- For several years now, an independent consultant (Deloitte) has conducted an audit of the Shareholders' Annual General Meeting management processes with a view to improving the protection of shareholder rights in their General Meetings. The auditor's reports are published on the website from the date of the Shareholders' General Meeting. Since the 2014 Shareholders' Annual General Meeting, shareholders have been offered the possibility of requesting a certificate confirming their vote, verified by the external auditor of the Shareholders' General Meeting. Once again at the Shareholders' Annual General Meeting held in April 2016, the General Meeting management processes were audited

and shareholders were offered the possibility of requesting a certificate confirming their vote, verified by the external auditor.

The rights of shareholders are regulated in Article 15 of the Bylaws, which refers specifically to the right of information and attendance at the Shareholders' General Meeting, and in Article 6 to 10 of the Shareholders' General Meeting Regulations. Specifically, the rights are as follows:

Right of information

The Company pays special attention to the right of information, as reflected in Article 15 of the Bylaws and Article 8 of the Shareholders' General Meeting Regulations. Article 8 of the Shareholders' General Meeting Regulations establishes the obligation for the Company to make documentation and information relating to the agenda available to shareholders, free of charge, both at the Shareholder Information Office and on the corporate website.

In addition, during the meeting, shareholders may orally request any reports or clarification they deem appropriate regarding the items on the agenda. If such requests cannot be satisfied at the time, the Board of Directors must provide the information in writing within seven days of the meeting.

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



The Company maintains an open, fluid and accessible dialogue with shareholders. Communications are made with the utmost transparency, providing all available information to shareholders at the same time as it is received by other participants in the securities and financial markets.

A specific Shareholder Information Office is in place to deal with any inquiries from minority shareholders.

The Company undertakes to make documentation and information relating to the meeting agenda available to shareholders, free of charge, both at the Shareholder Information Office and on the Company website, including:

- > The call notice of the Shareholders' General Meeting, containing the proposed resolutions and the related reports by the Board of Directors.
- > The Company's individual and consolidated management reports for the year, and the proposed allocation of results.
- > The separate and consolidated management report for the year, of the Company.
- > The audit reports on the Company's individual and consolidated financial statements.
- > The Annual Corporate Governance Report.
- > The Annual Corporate Responsibility Report.
- > The Annual Directors' Remuneration Report.

- > The environmental report.
- > The Procedures regulating the remote voting system at the Shareholders' Annual General Meeting.
- > The Operating Rules of the Shareholder E-Forum.
- > Any other report whose inclusion is obligatory or is decided by the Board of Directors.

Act 31/2014 of 3 December, amending the LSC, brought some changes that affect the right of information. The most important changes applicable to listed companies are as follows:

- > Clarification that all proposed resolutions on each and every item on the agenda must be continuously available on the Company website from the time of publication of the notice of Shareholders' General Meeting to the date of the meeting. Clarification that a report must be drawn up and published on the website on any items on the agenda that are informative only.
- > In particular, establishment of a duty to include on the website, from the moment the meeting is called, detailed information on the reports and proposed appointment, ratification or re-election of directors and on the Directors' Remuneration Policy.
- > Extension of the period in which shareholders may request information and clarifications until the fifth day prior to the date scheduled for the meeting (before, the period ended on the seventh day before the meeting).



- Obligation to post valid requests for information or clarification and questions submitted in writing, together with the directors' written answers, on the Company's website.
- When information is requested by shareholders that is already available on the Company website in Q&A form, directors may refer the inquirer to the information provided in that format (previously, directors were allowed not to reply to this type of question).

As already explained in Chapter II of Title I above, the Shareholders' Annual General Meeting held on 15 April 2015 approved the amendments to the Bylaws and the shareholders' General Meeting Regulations aimed at fully adapting them to the amended LSC with regard to the matters that were not previously covered by these corporate regulations.

At the 2016 Shareholders' Annual General Meeting there were amendments to the shareholders' right of information.

Right of attendance

Shareholders may attend the Shareholders' General Meeting if they are up to date in the payment of capital calls and evidence their share ownership, by way of a certificate made out in their name in the accounting register of book entries five days before the meeting is due to be held.

To this effect, Article 15 of the Bylaws and Article 10 of the Shareholders' General Meeting Regulations provide that shareholders with the right to attend may be represented at the Shareholders' General Meeting by any other person, in the manner established in the LSC. The condition that the proxy must be a company shareholder has been withdrawn, following the approval of the adaptation of its content to Act 25/2011, of 1 August, by the Shareholders' General Meeting held on 19 April 2012.

There is no Bylaw restriction requiring a minimum number of shares to be held in order to attend the Shareholders' General Meeting [the 'one share, one vote' principle applies].

Directors and senior managers are required to attend Shareholders' General Meetings.

As a general rule and in order for the proceedings of meetings and the resolutions adopted to reach the widest audience, the media are allowed access to Shareholders' General Meetings and their proceedings are broadcast in an audio-visual format, with simultaneous interpreting into sign language and into English.



Right of participation and new technologies

The Shareholders' General Meeting Regulations allow shareholders to participate to the fullest extent in matters of interest to them (right to attend, meeting calls, inclusion of items and proposals on the agenda, inquiries and requests for information, and voting).

In line with the most widely acknowledged recommendations in this area, the Shareholders' General Meeting Regulations are in keeping with the regime established by Act 26/2003, of 17 July, regarding the implementation of shareholder rights and the rules regarding the organisation and functioning of the Shareholders' General Meeting, and the current LSC, following the reforms introduced by Act 25/2011 of 1 August. This Act introduced certain adjustments and provisions aimed at strengthening the right of shareholders to participate at the Shareholders' General Meeting, which justified the adaptation thereto of the Shareholders' General Meeting Regulations and the Bylaws, at the Shareholders' General Meeting held on 19 April 2012.

Under the Shareholders' General Meeting Regulations (following their adaptation to the LSC at the Shareholders' Annual General Meeting of 15 April 2015), shareholders holding more than 3% of the share capital may apply to the Board, prior to the notice of Shareholders' General Meeting, to have particular items included in the Shareholders' General Meeting agenda. The Board of Directors must include the items requested in the manner that best suits the Company's interests, provided the items refer to matters falling within the scope of the powers of the Shareholders' General Meeting.

Shareholders may also submit proposals in relation to the matters on the agenda, in addition to making suggestions on the activities and interests of the Company which, in their view, should be discussed at the Shareholders' General Meeting. In both cases, shareholders may make proposals and suggestions through the Shareholder Information Office.

Red Eléctrica introduced an electronic voting system in 2005. It was one of the pioneers of this system, which allows shareholders to exercise their voting rights electronically via the Company website, www.ree.es. Since then, the Company has allowed shareholders to exercise their voting rights electronically at all Shareholders' General Meetings.

In line with this use by shareholders of advanced electronic means to exercise their rights, at its meeting on 23 February 2016 the Board of Directors approved the procedure on remote voting, proxy appointment and exercise of the right of information for the Shareholders' Annual General Meeting to be held on 15 April 2016. A total of 280 shareholders, holding 59,022 shares, exercised their right to vote or appoint a proxy electronically. This meant that 6.6% of the 4,226 shareholders present at the meeting in person or by proxy participated in the meeting by electronic means.

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



Furthermore, both the 2016 Shareholders' Annual General Meeting and the presentations to analysts were broadcast live via the Company's website. The presentations are available on the corporate website. The Shareholders' General Meeting has been broadcast by live webcast since 2006, with simultaneous interpretation into English. A sign language interpreter is also present at Shareholders' General Meetings to allow people with hearing difficulties to follow and participate in the proceedings.

In 2011 the Company launched the Shareholder E-Forum to facilitate communication between the shareholders of Red Eléctrica with a view to publishing proposals to supplement the agenda in the Shareholders' General Meeting call notice, issuing requests for support of such proposals, presenting initiatives to achieve the percentage needed in order to be able to exercise a minority right as provided by law or making offers or solicitations of voluntary representation.

This tool was incorporated into Article 8.4 of the Shareholders' General Meeting Regulations by means of a resolution adopted by the Shareholders' General Meeting of 13 April 2011. Consequently, the regulatory requirements of Article 539.2 of the LSC were met. The Forum has been available at all the Shareholders' General Meetings held by the Company since the Forum was created.

In 2016, the Company continued to use social networks [*Facebook and Twitter*] to publicise and provide information about the Shareholders' Annual General Meeting and the Shareholders' Extraordinary General Meeting.

In accordance with CNMV Circular 3/2015 of 23 June, in 2015 a 'Right of information' page was added to the 'Shareholders' General Meeting' section of the corporate website, with information about channels of communication between the Company and its shareholders and explanations on how to exercise the right of information.



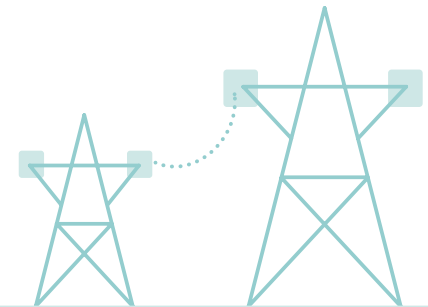
TITLE III
THE YEAR 2016
IN RED ELÉCTRICA



TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE



OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER





CHAPTER IV

THE BOARD OF DIRECTORS

Organisation and responsibilities

At 31 December 2016, the Board of Directors was made up of 12 ^[3] directors (1 executive, 3 proprietary, 7 independent ^[4] and 1 in the 'other external' category).

With the support of the Audit Committee and the Appointments and Remuneration Committee, the Board of Directors governs and represents the Company.

The Board's strategic decision-making processes are described below.

The rules on the organisation and functioning of the Board are contained in the Bylaws (Articles 19 to 26, inclusive) and the current Board of Directors Regulations (Articles 5 to 14, inclusive, and Articles 19 and 20). The amendment to the Board of Directors Regulations approved on 20 December 2016 extended the scope of the core responsibilities for the administration of the Company that are reserved expressly to the full Board of Directors, as specified in Article 5 of the Board of Directors Regulations, mainly in order to adapt those regulations to Articles 249 *bis* and 529 *ter* of the LSC.

Before the start of the year, at the proposal of its Chairman, the Board of Directors approves an indicative schedule of meetings for the year. Each director individually may propose other items not initially included in the agenda of each meeting, which is made available well in advance, together with the notice of the meeting and the related documentation.

Pursuant to the Bylaws and the Board of Directors Regulations, the principle guiding the Board's actions at all times is the corporate interest, understood as the Company's long-term profitability and sustainability, which enables the Company's long-term survival and the maximisation of its value (article 6 of the Board of Directors Regulations).

Specifically, the Board holds all powers to manage and represent the Company, both in and out of court, exercising such powers directly, via delegation or pursuant to a power of attorney in the terms established by law, the Bylaws and the Board of Directors Regulations.

The Board's policy is to delegate the ordinary management of the Company to the executive bodies and the management team and to concentrate on its general supervisory function, the approval of basic operating guidelines and strategies, and the decisions that are most relevant to the Company's interests.

[3] As of 31 December 2016, the Board of Directors had 11 members, as an independent director position was vacant following the resignation of the independent director Mr. Agustín Conde Bajén, which was accepted by the Board of Directors on 29 November 2016.

At its meeting on 31 January 2017, the Board of Directors appointed Mr. Arsenio Fernández de Mesa y Díaz del Río, an independent director, to fill that vacancy until the next Shareholders' Annual General Meeting.

[4] Counting the independent director vacancy as of 31 December 2016.



TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



In particular, the Board has expressly reserved to itself (Article 5 of the Board of Directors Regulations), and is not permitted to delegate, certain responsibilities that it must exercise directly, namely:

- a) Approve the general policies and strategies of the Company and the Group, specifically including:
 - i. The policies and strategies relating to the organisation and functioning of the Board and, in particular, the policies on the approval of and amendments to these Regulations.
 - ii. Approve the Strategic or Business Plan of the Company and its Group, as well as the annual budget and management objectives, and monitor compliance with the plan throughout the year.
 - iii. Determine the Company's general policies and strategies and, in particular, its tax strategy.
 - iv. Approve the investment and funding policy.
 - v. Approve the definition of the basic structure of the Group of companies of which the Company is the controlling company.
 - vi. Approve the Corporate Governance Policy of the Company and the Group of which it is the controlling company.
 - vii. Approve the Corporate Responsibility Policy.
 - viii. Approve the policy on remuneration of senior managers who report directly to the Board, the Chairman or the Managing director.
 - ix. Approve the main risk control and management policy of the Company and the Group and receive reports on and supervise the internal control, risk prevention and reporting systems.

The risk control and management policy must identify at least the following:

- The different types of risk (operational, technological, financial, legal and reputational, among others) that the Company and the Group face, including, among the financial and economic risks, any contingent liabilities and other off-balance sheet risks.
 - The level of risk the Company deems acceptable.
 - Planned measures to mitigate the impact of identified risks, in the event that they materialise.
 - The internal reporting and control systems to be used to control and manage the above risks, including contingent liabilities and off-balance sheet risks.
- x. Approve the policy on communication and contacts with shareholders, institutional investors and proxy advisors.
 - xi. Approve the policy on the appointment and assessment of candidates to the Board of Directors.
 - xii. Approve the policy on the performance evaluation of the Board and the directors.
 - xiii. Approve the policy on the dissemination of corporate governance, corporate responsibility, remuneration and risk management practices.
 - xiv. Approve the policy on the provision of non-audit services by the external auditor, without prejudice to the authority belonging to the Audit Committee.
 - xv. Approve and, where applicable, propose the dividend and treasury stock policies, especially the limits on treasury stock, to the General Meeting.
 - xvi. Other responsibilities specifically provided for in these regulations.

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA

TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE

OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

- b) The following decisions:
- i. Appointment and removal of the Company's Managing directors and the terms of their contract.
 - ii. Appointment and removal of senior managers of the Company who report directly to the Board or any of its members and the basic terms of their contracts, including their remuneration.
 - iii. The remuneration of directors, within the framework set by the Bylaws and the remuneration policy approved by the Shareholders' General Meeting, and in the case of executive directors, the additional remuneration for their executive functions and any other terms that must be included in their contracts.
 - iv. Authorization of activities prohibited by, or waiver of the obligations arising from, the duty of loyalty, as provided in Article 230 of the LSC.
 - v. The financial reports which, as a listed company, the Company must publish periodically or which it submits to the regulatory or market supervisory bodies for publication by them.
 - vi. Investments or transactions of any kind carried out by the Company or the Group which because of their amount or special characteristics are considered strategic, according to the criteria established by the Board of Directors, or which entail special tax risk, unless the approval of the General Meeting is required.
 - vii. The creation or acquisition of interests in special purpose vehicles or entities domiciled in countries or territories that are considered tax havens and any other similar transactions or operations which, on account of their complexity, could impair the transparency of the Company and the Group.
- c) Subject to a report by the Audit Committee, the approval of any transactions which the Company or any Group company may enter into with directors, in accordance with the LSC, or with shareholders who, individually or in concert with others, hold a significant interest, including shareholders represented on the Board of Directors of the Company or other Group companies, or with people associated with them. The directors affected, or those who represent or are associated with the shareholders affected, must refrain from participating in the deliberations and voting on the resolution in question. Only transactions that meet all of the following three criteria do not require such approval:
- They are carried out under contracts the conditions of which are standardised and apply *en masse* to a large number of customers.
 - They are carried out at prices or rates set on a general basis by the person supplying the good or service concerned.
 - Their amount does not exceed 1% of the Company's annual revenue.
- d) Authorization of the financial statements and presentation to the Shareholders' General Meeting.
- e) Calling of Shareholders' General Meetings and drafting of the agenda and proposals for resolutions.
- f) Delegation of any authority the Shareholders' General Meeting may have delegated to the Board of Directors, unless expressly authorised by the Shareholders' General Meeting to sub-delegate.



- g) The preparation of any kind of report required of the Board of Directors by law provided the operation to which the report refers cannot be delegated.
- h) Annual assessment of:
- i. The quality and efficiency of the functioning of the Board, the diversity of its composition and competencies, the performance of their functions by the Chairman of the Board and the Company's Managing director and, where applicable, the performance and contribution of each director, paying special attention to the chairpersons of the different committees, all this based on the report submitted to the Board by the Appointments and Remuneration Committee in coordination with the Lead Independent director, if any, or the Chairman, as the case may be.
 - ii. The composition and functioning of the Board's committees and of any other delegated body that may have been created, based on the report submitted to the Board by the Appointments and Remuneration Committee in coordination with the Lead Independent director or the Chairman, as the case may be.

The result of these assessments will be recorded in the minutes of the meeting or will be included in the minutes as an annex. Furthermore, based on the result of these assessments, the Board will prepare and present an action plan aimed at correcting any deficiencies and addressing any areas for improvement detected. The assessment process and the areas assessed will be described in the Annual Corporate Governance Report.

At least every two years, the Board of Directors will be assisted in carrying out the assessment by an outside consultant, whose independence will be verified by the Appointments and Remuneration Committee. Any business relationships the consultant or any company in its group may have with the Company or any Group company must be disclosed in the Annual Corporate Governance Report.

The Board must periodically review the general aspects of the assessment methodology used, the overall results of the assessment and any corrective measures adopted.

Tax responsibilities of the Board

Act 31/2014 of 3 December, amending the LSC for the improvement of corporate governance, made important changes to the responsibilities of the Board of Directors of listed companies in relation to tax matters.

Following the reform of the LSC, in listed companies, the responsibility for setting tax strategy, formulating policy on tax risk management and control, and approving investments or transactions which because of their amount or special characteristics are considered strategic or which entail particular tax risk is reserved to the Board of Directors and cannot be delegated, thus reinforcing the strategic role of Boards of Directors in tax matters, in line with the trend in other countries in our environment in this respect.

In accordance with the action plan in tax matters presented to the Audit Committee on 18 February 2015, the Company has acted in compliance with the LSC and a series of voluntary

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



measures have been implemented in order to improve and develop best tax practices, which are listed below:

- Approval by the Board of Directors of the Red Eléctrica Group's tax strategy at its meeting held on 30 June 2015.
- Approval by the Board of Directors, at its meeting held on 29 September 2015, of the Red Eléctrica Group's tax risk management and control policy and the inclusion of this policy in the Company's Enterprise Risk Management Policy.
- Approval by the Board of Directors of the tax aspects of investments or transactions which because of their amount or special characteristics are considered strategic or which entail special tax risk.
- Reporting on the tax policies applied in the annual corporate income tax return for 2014 and 2015. This was done before the annual tax filing, at the Audit Committee meetings held on 24 June 2015 and on 22 June 2016, respectively.
- Approval by the Board of Directors of the Red Eléctrica Group's becoming a signatory to the Code of Best Tax Practices, at its meeting on 29 September 2015.
- Reporting on the tax policies applied in the close of accounts for financial years 2015 and 2016. This was done in the Audit Committee meetings on 21 January 2016 and on 26 January 2017, respectively, before the financial statements for 2015 and 2016 were in turn authorised for issue.

Additionally, with a view to providing greater tax information transparency for its stakeholders, in 2015, for the first time, the Red Eléctrica Group published (in the 2014 Corporate Responsibility Report) its 2014 total tax contribution, demonstrating the important economic and social role the Red Eléctrica Group plays, through its tax contribution, in the various countries in which it operates.

In order to calculate its total tax payments, the Red Eléctrica Group uses PricewaterhouseCoopers's Total Tax Contribution (TTC) framework, which measures the total impact derived from a company's payment of tax. This appraisal is conducted in terms of the total contribution of taxes paid to the different tax authorities, directly or indirectly, as a result of the Red Eléctrica Group's economic activity.

The Red Eléctrica Group's total tax contribution for 2016 is published in the 2016 Corporate Social Responsibility Report.

The Red Eléctrica Group's tax strategy, which reflects the Group's vision and goals in tax matters, is based on the three fundamental values of transparency, good governance and accountability.





The vision driving the tax strategy can be summed up as follows:

‘Manage tax matters proactively, acting responsibly and transparently towards all stakeholders and in such a way as to comply with tax legislation and minimise reputational risk, making compliance compatible with protection of shareholder value.’

In 2015 the Board of Directors approved the Red Eléctrica Group’s tax risk control and management policy and its integration in the enterprise risk management policy. The tax risk control and management systems are described in section E of this Report.

The Red Eléctrica Group’s Code of Ethics and tax strategy establish a commitment not to create companies in countries considered tax havens in order to evade tax.

Furthermore, at its meeting on 29 September 2015, the Board of Directors of Red Eléctrica Corporación, S.A. approved a resolution requiring the Red Eléctrica Group to subscribe to the Code of Best Tax Practices adopted by the Spanish Tax Agency within the framework of the Large Businesses Forum.

In 2016 there were no changes affecting the regime described above.

Composition

At 31 December 2016 the Board of Directors was made up of 12 members, with one vacancy for an independent director, following the resignation of the Independent director Mr. Agustín Conde Bajén in November 2016.

Pursuant to the Bylaws, directors hold office for a term of four years.

A 12-year limit on the term of office of Independent directors was incorporated voluntarily in the Board of Directors Regulations several years ago (in 2010), following the recommendations of the Unified Code on Good Governance [5]. All other types of director may be reappointed indefinitely by the Shareholders' General Meeting. Act 31/2014, of 3 December, reforming the LSC, expressly specifies this limit, thus giving it legal status (Article 529 *duodecies* LSC). As the limit is now required by law, the new CBGSC no longer includes it among its recommendations.

Proposals for the removal of independent directors should not be made before the end of the statutory term of office for which they were appointed, except where there is sufficient cause, subject to a report by the Appointments and Remuneration Committee.

[5] Order ECC/461/2013 of 20 March, which determines the content and structure of the Annual Corporate Governance Report, the annual remuneration report and other reporting instruments of listed companies, savings banks and other entities issuing securities admitted to trading on official securities markets, incorporated said prohibition into law.



At 31 December 2016, the Board of Directors of Red Eléctrica had the following members:

Name of director	First appointed	Last appointed	Position on the Board	Type of director	Election procedure	Board committee membership
José Folgado Blanco	22.05.08	15.04.16	Chairman	Other external	Shareholders' General Meeting	-
Juan Francisco Lasala Bernad	17.07.15	17.07.15	Managing director	Executive	Shareholders' General Meeting	-
María Ángeles Amador Millán	26.05.05	18.04.13	Member	Independent non-executive	Shareholders General Meeting	Appointments and Remuneration General Meeting
Fernando Fernández Méndez de Andés	19.04.12	15.04.16	Member	Proprietary non-executive (SEPI)	Shareholders General Meeting	Audit General Meeting
Carmen Gómez de Barreda Tous de Monsalve	19.04.12	19.04.16	Member	Independent non-executive	Shareholders General Meeting	Appointments and Remuneration (chair)
María José García Beato	29.11.12	18.04.13	Member	Independent non-executive	Shareholders General Meeting	Audit (member)
Socorro Fernández Larrea	09.05.14	9.05.14	Member	Independent non-executive	Shareholders General Meeting	Appointments and Remuneration (member)
Antonio Gómez Ciria	09.05.14	9.05.14	Member	Independent non-executive	Shareholders General Meeting	Audit (member)
Santiago Lanzuela Marina	29.07.14	15.04.15	Member	Proprietary non-executive (SEPI)	Shareholders General Meeting	Audit (member)
José Luis Feito Higuera	13.02.15	15.04.15	Member	Independent non-executive	Shareholders General Meeting	Audit (chairman)
José Ángel Partearroyo Martín	22.12.15	15.04.16	Member	Proprietary non-executive (SEPI)	Shareholders General Meeting	Appointments and Remuneration General Meeting
Vacancy [6]	-	-	Member	Independent non-executive	-	-

[6] At its meeting on 31 January 2017 the Board of Directors appointed Mr. Arsenio Fernández de Mesa y Díaz del Río as an independent director to fill the vacancy arising from the resignation of Mr. Agustín Conde Bajén, which was accepted by the Board of Directors on 29 November 2016.



Directors' professional profiles

The Company's directors are professionals of high standing, with broad professional experience. They bring to their task the necessary experience and knowledge to enable the Company to carry on its activities effectively and efficiently.

Set out below are the principal activities pursued by Board members outside the Company at 31 December 2016:

CHAIRMAN OF THE BOARD AND MANAGING DIRECTOR



José Folgado Blanco, born 3 April 1944. Degree in Economics. Final-year award with special distinction. Doctorate in Economics, Universidad Autónoma de Madrid.

CURRENTLY

- Member of the Social Board, Universidad Autónoma de Madrid.
- Chairman of the Board of Directors of Red Eléctrica Corporación, S.A.

FORMERLY

- Tenured Professor of Public Finance and Tax Systems, Universidad Autónoma de Madrid.
- Head of the Economics Department of the CEOE.
- Member of the Economic and Social Board representing business organisations.
- Secretary of State for Budgets and Expenditure. Ministry of Economy and Finance, from May 1996.
- Secretary of State for Economy, Energy and Small and Medium-Sized Enterprises. Ministry of Economy, from April 2000.
- Secretary of State for Energy, Industrial Development and Small and Medium-Sized Enterprises. Ministry of Economy, since July 2002.
- Member of the Spanish Parliament representing the province of Zamora and Vice-Chairman of the Finance Committee since March 2004.
- Mayor of Tres Cantos (Madrid) since June 2007.

MANAGING DIRECTOR



Juan Francisco Lasala Bernad, born 25 February 1967. Degree in Business Studies, Universidad Complutense de Madrid.

CURRENTLY

- Managing director of Red Eléctrica Corporación, S.A.

FORMERLY

- A member of the Company since 2001, he has performed executive functions in the international area and in the Telecommunications area and has held the position of director of Planning and Control and corporate Finance Director.
- Director of Planning and Control of the Avanzit group and group CFO for Spain.
- CFO of Midas, Spain.
- Assistant CFO at Burger King, Spain.
- Auditor at KPMG Peat Marwick.



INDEPENDENT NON-EXECUTIVE DIRECTOR



M^a Ángeles Amador Millán, born 10 October, 1949. Law Degree, Universidad Complutense de Madrid Diploma in Human Rights, Institut International des Droits de l'Homme of Strasbourg. Research study on Industrial Property Law, Harvard Law School (Cambridge, Massachusetts).

CURRENTLY

- Practising lawyer.

FORMERLY

- Technical General Secretary, Ministry of Public Works and Urban Development.
- Deputy Secretary, Ministry of Health and Consumer Affairs.
- Minister for Health and Consumer Affairs.
- Member of the Spanish Parliament.
- Member of the Governing Council of the Madrid Bar Association.

PROPRIETARY NON-EXECUTIVE DIRECTOR PROPOSED BY SEPI



Fernando Fernández Méndez de Andés, born 10 February 1956. Doctorate in Economics, Universidad Autónoma de Madrid. Professor of Economics, IE Business School.

CURRENTLY

- International Consultant on macroeconomic, financial and regulatory issues.
- Collaborator with the Fundación de Estudios Financieros.
- Economic columnist and commentator in various media.
- Frequent speaker at international conferences and events related to his professional and academic activity, and the author of numerous related articles and publications.
- Independent director of Bankia, S.A.

FORMERLY

- Member of the Expert Committee for Tax Reform, 2013-2014.
- Member of the Bruegel Evaluation Committee, 2013.
- Principal Economist at the International Monetary Fund.
- Chief Economist and Director of the Research Department of Banco Central Hispano (BCH) and Banco Santander.
- Vice-Chancellor of the Universidad Europea de Madrid and the Universidad Antonio de Nebrija.
- Director of the European Business Programme.



INDEPENDENT NON-EXECUTIVE DIRECTOR (LEAD INDEPENDENT DIRECTOR)



Carmen Gómez de Barreda Tous de Monsalve, born 20 May 1968. Degree in Economics and Business Science from the Universidad Pontificia de Comillas (ICADE). Master in Business from the IESE (Executive MBA), University of Navarra.

CURRENTLY

- Director General of Corporación de Reservas Estratégicas de Productos Petrolíferos (CORES).

FORMERLY

- Head of the Cogeneration Department, Business Management, Enagás.
- Head of the International, Petrochemical and Marketing Departments of Repsol.
- Director of Services Development at Union Fenosa.
- Deputy Director of Oil Markets at Comisión Nacional de Energía (CNE).
- Institutional Relations and Communications Manager for BP Oil España.
- Member of the Spanish Delegation in the Emergency Questions Group and the Markets Group of the International Energy Agency (IEA).
- Representative on various international working groups on issues of energy regulation and security of supply (ARIAE and CEER).
- Professor at lectures and/or presentations on different Masters Courses (University of Barcelona, ICAI, Cesma, Spanish Energy Club).





INDEPENDENT NON-EXECUTIVE DIRECTOR



María José García Beato, born 27 May 1965. Law Degree, Universidad de Córdoba. State attorney.

CURRENTLY

- Non-director Vice-Secretary of the Board of Directors of Banco Urquijo, S.A.
- General Secretary and member of the Management Committee of Banco Sabadell, S.A.
- Secretary of the Board of Directors of Sabadell United Bank (Miami).
- Trustee of Fundació Privada Banc Sabadell.
- Trustee of Fundación Española de Banca para Estudios Financieros (FEBEF).
- Member of the Advisory Board of the publisher Wolters Kluwer España, S.A.
- Member of the Advisory Board of Fundación Cajasur.

FORMERLY

- State Attorney at the High Court of Justice in Madrid.
- Head of the Legal Services Department of the Data Protection Agency.
- Spanish representative on the Advisory Board of the European Committee on Data Protection.
- Advisor to the Board of Directors of the Fábrica Nacional de Moneda y Timbre for the CERES (Spanish certification of electronic transactions) project.
- State Attorney in the Sub-division of the State Legal Services Division.
- State Attorney in the Communications Secretariat at the Ministry of Development.
- Cabinet Chief at the Ministry of Justice.
- Director, Infoinvest, S.A.
- Director, Sociedad Estatal de Gestión Inmobiliaria de Patrimonio, S.A. (SEGIPSA).
- Director, Sociedad Estatal para Exposiciones Internacionales, S.A. (SEEI).
- Director, Sociedad Estatal Correos y Telégrafos, S.A.
- Director, Banco Guipuzcoano, S.A.
- Director, Banco CAM, S.A.
- Deputy Secretary for Justice.
- State Attorney in the Audiencia Nacional (National Court) Legal Department.
- Head of Legal Services, Banco Sabadell.
- Secretary of the Board of Directors of Retevisión, S.A.
- Secretary of the Board of Directors of Banco Urquijo, S.A.
- Director, Banco Gallego S.A.





INDEPENDENT NON-EXECUTIVE DIRECTOR



Mr. Antonio Gómez Ciria, born 25 March 1957. Degree in Economics and Business Studies, Universidad Complutense de Madrid. Degree in Mathematics, Universidad Complutense de Madrid. Masters in Business Administration & Management (Executive MBA), IESE. Accredited Accounting Expert – AECA.

CURRENTLY

- Member of the Advisory Board of Experts in Accounting and Financial Information (ECIF), General Council of the Association of Economists.
- Member of the Board of Directors of Mapfre Spain and of Mapfre Global Risks.

FORMERLY

- General Manager of Administration and IT, Member of the Management Committee of Grupo FCC.
- Representative of Grupo FCC at the Large Businesses Forum, Ministry of Finance and Public Administrations.
- Among other positions, he is General Manager for Administration and IT and belongs to the Management Committee of Grupo FCC.
- Head of Internal Audit of the FCC group.
- Member of the Advisory Council of the Internal Auditors Institute and a Member of its Executive Committee.
- General Technical Secretary of InverCaixa, investments management company of La Caixa Group.
- Chairman of Instituto de Contabilidad y Auditoría de Cuentas, ICAC.
- Director of Empresa Nacional de Uranio, S.A.
- Director of Empresa Nacional de Autopistas, S.A.
- Director of Tabacalera, S.A.
- Head of Market Inspection, Sociedad Rectora de la Bolsa de Valores de Madrid.
- Deputy Manager of Studies and Budgetary Planning, Radio Televisión Española.
- Head of the Auditing and Accounting Department of Banco de Crédito Agrícola.
- Auditor/Inspector of the General State Inspectorate.

OTHER

- Member of the CNMV Work Group to prepare a 'Management report guide for listed entities'.
- Rewarded with a merits distinction, further to Ministerial Order of 3 November 2000, for his dedication and outstanding professional conduct, granted by the First Vice President of the Government for Economic Affairs and Minister of Economy.



INDEPENDENT NON-EXECUTIVE DIRECTOR



Ms. Socorro Fernández Larrea, born 7 April 1965. Civil Engineer, Universidad Politécnica de Madrid, and Senior Management Program, IESE.

CURRENTLY

- MANAGING DIRECTOR of the consultancy firm JUSTNOW, S.L., providing advice in the infrastructure construction sector, both in commercial and financial operations.
- Member of the Board of Directors of AMPER, S.A. (proprietary director), on behalf of Emilanteos, S.L.
- Member of the Board of Directors of the Spanish engineering firm SEG, S.A.
- Member of the Board of Directors of the Spanish construction and real estate firm ACR.
- Member of the advisory board of the Mexican engineering firm CAL Y MAYOR.
- Member of the advisory board of the real estate firm ZELTEX, with activity in Senegal.

FORMERLY

- MANAGING DIRECTOR at COPISA Constructora Pirenaica, S.A.
- Vice-Chairman of ANCI, the association of independent builders.
- Member of the governing council of the Civil Engineers Association.
- Regional Manager of the construction firm Seop, Obras y Proyectos, S.A.
- National representative, Ferrovial Conservación, S.A.
- Representative for Castilla-La Mancha, Ferrovial-Agroman, S.A.
- Representative for Castilla-La Mancha, Agroman Empresa Constructora, S.A.
- General Manager for Roads, Hydraulic Works and Transport, Regional Department of Public Works, Autonomous Community Board of Castilla-La Mancha.
- Site manager, Ferrovial, S.A.

OTHER

- Member of the advisory board of the daily newspaper EXPANSIÓN.
- Member of WCD, Women Corporate Directors, and co-chairman of the Spain chapter.
- Member of AED, Asociación Española de Directivos, and member of its Executive Committee.
- Member of CEAL, Consejo Empresarial de América Latina, and member of the Executive Committee of the Iberian chapter.
- Member of WPO-YPO, Young Presidents' Organisation, and member of the executive committee of the Eurolatam chapter.
- Member of IWF, International Women's Forum.



TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA

TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE

OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

PROPRIETARY
NON-EXECUTIVE DIRECTOR,
ON BEHALF OF SEPI



Santiago Lanzuela Marina, born 27 September 1948. Degree in Economics & Trade. Civil servant of the State.

FORMERLY

- Adjunct Professor, Faculty of Economics and Business Studies, Universidad de Valencia (1971-1973).
- Head of the Spanish Mission for Technical Cooperation in Nicaragua (1974-1976).
- Head of International Technical Cooperation Programmes, Ministry of Employment (1976-1981).
- Advisor to the President of Instituto de Cooperación Iberoamericana (1982).
- Head of the National Heritage Inspection Service (1987).
- Regional Councillor of Economy and Finance, Government of Aragón (1989-1993).
- Founder and Chairman of Instituto aragonés de Fomento (1990).
- President of Centro Europeo de Empresas e Innovación de Aragón (1992).
- Parliamentary Member for Aragón (1991-1999).
- President of the Autonomous Community of Aragón (1995-1999).
- Senator for the Autonomous Community of Aragón. Chairman of the Senate Economy and Finance Committee (1999-2000).
- Congressman, President of the Economics and Tax Commission in Congress (2000-2004).
- Congressman, Member of the Permanent Council, Vice-Chairman of the Committee for Foreign Affairs and Member of the Development Committee (2004-2008).
- Member of the Territorial Management Committee. Sponsor of the 'Deputy Committee to analyse Spain's energy strategy for the next 25 years' (2008-2011).
- Congressman, President of the Economics and Competition Commission, Member of the Committee for Foreign Affairs, Member of the Development Committee, and member of the Spanish Delegation in the Parliamentary Assembly to Organise Security and Cooperation in Europe-OSCE (2011-28/7/2014).

INDEPENDENT
NON-EXECUTIVE DIRECTOR



José Luis Feito Higuera, born on 13 April 1952. Degree in Economics and Business Studies, Universidad Complutense de Madrid. State Trade Expert and Economist. Ambassador of Spain.

CURRENTLY

- Chairman and General Manager of IEE (Instituto de Estudios Económicos) since 2009.
- Chairman of the Economic and Financial Policy Committee of the Spanish employers confederation CEOE and member of its Executive Committee and Management Board since 2001.
- Member of the Board of Directors of Bankia, S.A. and member of its Audit and Compliance Committee since 2012.
- Member of the editorial board of the daily newspaper Expansión since 2001.

FORMERLY

- Chairman of the concessionaires association ASETA, Asociación de Sociedades Españolas Concesionarias de Autopistas, Túneles, Puentes y Vías de Peaje (2001-2014).
- Ambassador of Spain to the OECD in Paris (1996-2000).
- Partner and Member of the Board of Directors of A.B. Asesores Bursátiles, S.A. in Madrid (Morgan Stanley), where he has been Chief Economist and head of various investment banking areas (1986-1996).
- Head of international financial institutions at the Banco de España, member of the European Monetary Committee (Brussels) and the Committee of Governors of the Central Banks of the European Economic Community in Basel (1984-1986).
- Technical Advisor and Executive Director of the International Monetary Fund in Washington (1980-1984).
- Head of the Foreign Sector Research and Data Processing Service of the Ministry of Economy and Finance in Madrid (1978-1980).
- Programmer, analyst and IT executive at Seresco, S.A. and Entel-Ibermática, S.A. in Madrid (1967-1978).



PROPRIETARY NON-EXECUTIVE DIRECTOR, ON BEHALF OF SEPI



José Ángel Partearroyo Martín, born 16 February 1974. Law degree from Universidad de Salamanca. Master's degree in Business Legal Advice (LLM) from Instituto de Empresa. Public service exams to qualify as a judge and public prosecutor.

CURRENTLY

- General Manager of SEPI.

FORMERLY

- Head of Investees of the Communication Division of SEPI.
- Associate Lawyer at KPMG Abogados, S.L.
- Associate Lawyer at Goñi y Cajigas Abogados, S.L.
- Senior Lawyer as Ramón y Cajal Abogados (in alliance with Mayer Brown).
- Senior Associate en BIRD & BIRD (Spain) LLP.
- Associate Professor of Company Law in the Law Faculty of the Colegio Universitario Cardenal Cisneros (attached to Universidad Complutense de Madrid).
- Associate Professor of Company Law in the Law Faculty of Universidad Rey Juan Carlos I.

NON-DIRECTOR SECRETARY OF THE BOARD OF DIRECTORS



Rafael García de Diego Barber, born 27 July 1951. He was appointed Secretary of the Board of Directors and legal advisor at the Board meeting held on 4 May 1995. Law degree, Universidad Complutense, Master's Degree in Tax Counselling for Businesses, Instituto de Empresa.

CURRENTLY

- Secretary General and of the Board of Directors of Red Eléctrica de España, S.A., Member of the Madrid Bar Association, Director of the Dutch company Red Eléctrica de España Finance B.V., Joint Director of Red Eléctrica Financiaciones, S.A.U. and Director of the Luxembourg company REDCOR Reaseguros, S.A.

FORMERLY

- Lawyer, Loss Department, Zurich, S.A., Lawyer and Secretary of the Boards of Directors of companies in the Inmobiliario Pradisa Group, Lawyer and tax advisor of Ageco, Sociedad de Gestión Financiera and a tax manager of Banco Internacional de Comercio, S.A., Lawyer of the Legal Department of Sociedad Española de Carbón Exterior, S.A. (CARBOEX), Lawyer of the Legal Department, Head of the Legal Department and Director responsible for Legal Affairs at Red Eléctrica de España, S.A.

NON-DIRECTOR VICE-SECRETARY OF THE BOARD OF DIRECTORS



Fernando Frías Montejo, born 11 March 1965. He was appointed Vice-Secretary of the Board of Directors at the meeting held on 21 April 2005. Degree in Law and Certificate in Business Studies, Universidad Pontificia de Comillas (ICADE-E-1).

CURRENTLY

- Member of the Madrid Bar Association, and Head of the Corporate Governance and Compliance Department of Red Eléctrica de España, S.A.

FORMERLY

- Lawyer in the Legal Department of Red Eléctrica de España, S.A. since 1990 and Secretary of the Board of Directors of Infraestructuras de Alta Tensión, S.A., Red de Alta Tensión, S.A. and Tenedora de Acciones de Redesur, S.A.



Attendance at Board of Directors and committee meetings

Set out below are data on the Company directors' attendance and non-attendance of meetings of the Board of Directors and the Audit and Appointments and Remuneration Committees in 2016.

► **Board of Directors:** Of the eleven [11] Board meetings held in 2016, there was one absence and two proxy attendances, bringing the number of attendances in person to 127, representing an attendance rate of 97.7%.

ATTENDANCE AT BOARD OF DIRECTORS MEETINGS

Director	Present	Represented
José Folgado Blanco	11	0
Juan Francisco Lasala Bernad	11	0
María Ángeles Amador Millán	10	1
José Luis Feito Higuera	11	0
Fernando Fernández Méndez de Andrés	10	1
Paloma Sendín de Cáceres	3	0
Carmen Gómez de Barreda Tous de Monsalve	11	0
María José García Beato	11	0
José Ángel Partearroyo Martín	11	0
Antonio Gómez Ciria	11	0
Socorro Fernández Larrea	10	0
Santiago Lanzuela Marina	11	0
Agustín Conde Bajén	6	0

With respect to the number of attendances, it should be noted that some directors did not hold their office throughout the whole of 2016, specifically the following:

- **Mr. Agustín Conde Bajén** was appointed independent director of Red Eléctrica Corporación, S.A. by the Shareholders' Annual General Meeting held on 15 April 2016 and at its meeting on 29 November 2016 the Board of Directors accepted his resignation, which he tendered on being appointed Deputy Minister of Defence.
- **Ms. Paloma Sendín de Cáceres** held the position of independent non-executive director of Red Eléctrica Corporación, S.A. until the Shareholders' Annual General Meeting of the Company held on 15 April 2016, when her term of office expired and she was not reappointed.

► **Audit Committee:** Of the eleven [11] Audit Committee meetings held in 2016, no directors failed to attend.

► **Appointments and Remuneration Committee:** The Appointments and Remuneration Committee held thirteen [13] meetings in 2016, with three [3] non-attendances.



Chairman of the Board

Since 8 March 2012 the position of Chairman of the Board of Directors of the Company has been held by Mr. José Folgado Blanco. Since the Shareholders' Annual General Meeting held on 15 April 2016 the Chairman of the Board has had no executive powers.

Until the Shareholders' Extraordinary General Meeting held on 17 July 2015, the Board of Directors included only one executive director, who was also the Company's Chairman. However, there were numerous checks and balances that helped maintain a balance of powers on the Board. The Managing director was subject to specific controls of his responsibilities by the Board of Directors, from which he had to request subsequent ratification regarding any urgent decisions he had to adopt or, as the case may be, request prior authorization for such decisions. The independent directors, who until July 2015 represented 64% of the Board of Directors, and the Board committees, which had specific powers, also contributed to that balance of powers. In this respect, the most important measures were approved in 2013, following international corporate governance recommendations, with the corresponding amendments to the Board of Directors Regulations and the Bylaws.

The relevant amendments made to the Board of Directors Regulations on 13 March 2013 were as follows:

- The possibility of creating the position of Lead Independent director and a procedure for appointing, removing and regulating the lead director's powers and responsibilities [a role that was appointed in May 2013].
- The introduction of specific measures for the separation of the positions of Managing director and Chairman of the Board of Directors.
- Express reservation to the Board of Directors of certain competences and powers which, for reasons of urgency, had previously been delegated to the Chairman of the Board of Directors.
- Provision requiring that the number of Independent directors must represent at least half of the total number of directors. When the Chairman of the Board is also the Managing directors of the Company, the independent directors should constitute a majority of the total number of directors.

The Shareholders' General Meeting held on 18 April 2013 amended the Bylaws by introducing counterbalancing measures similar to those introduced in the Board of Directors Regulations, in cases in which the Chairman is also the Managing director of the Company [regulating the role of Lead Independent director] and other measures that allowed the separation of the two offices.

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



The corporate legal regime approved in 2013 allowed the de facto separation of the positions of Chairman of the Board and Managing director of the Company and even allowed the appointment of one or more managing directors besides the Chairman. All these matters were resolved at the Shareholders' Extraordinary General Meeting held on 17 July 2015. At that meeting, having received the 'Report on the separation of the positions of Chairman of the Board of Directors and Managing director of the Company', which had previously been approved by the Board of Directors, the shareholders resolved to increase the number of directors by one, setting the total at twelve, and appointed a new executive director (who subsequently was appointed Managing director by the Board of Directors). Subsequently, at its meeting on 28 July 2015, the Company's Board of Directors appointed the new executive director, Mr. Juan Francisco Lasala Bernad, to be Managing director of the Company. That appointment marked the start of a transitional period, in which the Company had two executive directors (the Chairman of the Board and the Managing director) and which came to a conclusion at the Shareholders' Annual General Meeting held on 15 April 2016. At that meeting the Company's Chairman was re-elected as a director in the 'other external' category, thus losing his status as an executive director.

In Red Eléctrica the Chairman of the Board of Directors is chosen from among the Board's members, after consideration of a report by the Appointments and Remuneration Committee, and is the person responsible for leading the Board of Directors and ensuring that it functions effectively. Under the corporate regulations, if the position of Chairman falls upon an executive director, the appointment will require the vote in favour of two-thirds of the members of the Board of Directors.

Under the Board of Directors Regulations, the Board of Directors has reserved to itself, and is not permitted to delegate, the responsibilities and competencies it considers strategic, which in December 2016 were expanded with the approval of the amendment to the Board of Directors Regulations. The reserved responsibilities cannot be assumed by the Chairman of the Board, the Managing director or the Board committees.

Article 529 *sexies* of the LSC, which was added following the reform enacted by Act 31/2014 of 3 December, amending the LSC for the improvement of corporate governance, regulated the powers of the Chairman of the Board for the first time, naming the Chairman as the person ultimately responsible for the effective functioning of the Board of Directors. Besides the functions specified in law, the Bylaws and the Board of Directors Regulations, the LSC also gives the Chairman the following responsibilities:

- Convene and chair Board meetings, setting the agenda and conducting the discussions and deliberations.
- Chair the Shareholders' General Meeting.
- Ensure that directors receive sufficient information in advance to be able to deliberate on the business of the meeting.
- Stimulate debate and active participation by directors during Board meetings, safeguarding their freedom to take positions and express opinions.

TITLE III
THE YEAR 2016
IN RED ELÉCTRICA

TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE

OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER



The Shareholders' Annual General Meeting held on 15 April 2015 approved amendments to the Bylaws aimed at fully adapting them to the LSC and specifically amended Article 25 of the Bylaws to include the powers assigned to the Chairman of the Board in Article 529 *sexies* of the LSC.

Articles 20 and 21 of the Company's Bylaws assign to the Chairman of the Board the functions of representing the Board of Directors on a permanent basis, calling a vote on Board matters once they have been sufficiently debated and ensuring that Board resolutions are complied with.

Additionally, Recommendation 33 of the new CBGSC extends the powers of the Chairman of the Board to include the following:

- Prepare and submit to the Board a schedule of meeting dates and items of business to be transacted.
- Organise and coordinate the periodic assessments of the Board and, where applicable, the Managing director.
- Guide the Board and be responsible for its effective functioning.
- Ensure that sufficient time is given to discussion of strategic matters.
- Agree upon and review the Board members' professional development programmes.

Article 9 of the Company's Board of Directors Regulations assigns certain functions to the Chairman of the Board and, following its recent amendment, has been adapted to the content of Article 529 *sexies* of the LSC, the abovementioned Recommendation 33 CBGSC and the changes in the Board's organisation and functioning resulting from completion of the separation of the positions of Chairman of the Board and Managing director, among other things.

Under Article 12 of the Company's Shareholders' General Meeting Regulations, the Chairman of the Board of Directors has for many years been responsible for chairing the Shareholders' General Meeting, anticipating the new legal provision introduced with the recent reform of the LSC.

Directors' responsibilities and duties

The Board of Directors Regulations provides mechanisms in order to act against potential infringements of corporate governance rules on the part of directors.

As explained in Chapter I of Title I of this report, following the entry into force of Act 31/2014 of 3 December, there have been some changes to directors' duties, which have prompted amendments to the Board of Directors Regulations to adapt them to the LSC.



The main changes introduced by Act 31/2014 of 3 December, amending the LSC for the improvement of corporate governance, as regards the duties of directors were as follows:

- The duty of care of directors was described and specified.
- Obligations arising from directors' duty of loyalty (such as the duty of secrecy and the duty to abstain where there is a conflict of interest), which became mandatory, and the consequences of non-compliance were reformulated; other new obligations were added, such as the obligation of directors to act according to their free judgement, without accepting instructions from or ties with third parties; and, in general, the duty to adopt the necessary measures to avoid any potential conflict of interest with the Company.
- Further details were provided on obligations arising from the duty to avoid conflicts of interest, reformulating some of the current obligations arising from the duty of loyalty, which were already regulated by various provisions of the LSC.
- The cases where directors may be released from compliance with the obligations arising from the duty of loyalty and the duty to avoid conflicts of interest (such as transactions executed with the Company, taking advantage of a business opportunity or the possibility of competing with the Company) were regulated.

Through the amendment approved on 20 December 2016, the Board of Directors Regulations were adapted to the LSC, mainly to Articles 225, 227, 228, 229, 230, 529 *ter* and *quater*. The directors' duties regulated in Articles 30 to 38 of the Board Regulations are now as follows:

➤ General duty of care

Directors must exercise their office and perform the duties imposed by law with the care of prudent businessmen, in line with the nature of their office and the functions assigned to each one of them. In particular, they have an obligation to:

- a) Be properly informed and prepared for meetings of the Board and any committees of which they are members. For this purpose, directors have a duty to demand, and a right to receive, the information they need from the Company in order to be able to perform their obligations.
- b) Devote the necessary time and take the necessary steps to ensure that the Company is properly supervised and controlled. In particular, they must devote enough time to be able to perform their functions effectively and know the Company's business and rules of governance, taking part in any professional development programmes the Company may organise, as provided by Article 26 of the Board of Directors Regulations.
- c) Attend in person the meetings of the Board and any committees of which they are members and take active part in the deliberations, so as to make an effective contribution, with their judgment, to Board decision making.



If they are unable, for good reason, to attend a meeting to which they have been called, they must give instructions to the director who is to represent them, in accordance with Article 20 of the Board Regulations. Non-executive directors may only appoint another non-executive director to represent them and executive directors must try to appoint another executive director, if possible.

Non-attendances will be reported in the Annual Corporate Governance Report.

- d) Perform any specific task assigned to them by the Board of Directors that is reasonably within their time commitment.
- e) Sponsor the investigation of any irregularity in the management of the Company or any Group company that may come to their notice and the surveillance of any risk situation.
- f) Call on persons with the necessary authority to call an extraordinary meeting of the Board of Directors or of a Committee when they consider there to be matters that require discussion, or to add such matters to the agenda of the next meeting that is to be held.
- g) Have at their disposal and gather the information they need in order to perform their functions effectively and regularly monitor any issues arising out of the Company's activity, it being their responsibility to identify and request such information from the Chairman or the Secretary of the Board.
- h) Oppose any resolutions that are contrary to the law, the Bylaws or the corporate interest, expressing their opposition clearly. In particular, independent directors

and those unaffected by any potential conflict of interest must oppose resolutions that may be contrary to the interests of shareholders who are not represented on the Board. This obligation also applies to the Secretary of the Board, even if not a director. If the Board adopts significant or reiterated decisions about which a director or the Secretary has serious doubts, they must draw the necessary conclusions and, if they opt to resign, must explain the reasons as provided in Article 24.4 of the Board Regulations.

> Duty of loyalty

Directors must carry out their duties with the loyalty of a faithful representative, acting in good faith and in the best interests of the Company, and must comply with the duties imposed by law, the Bylaws and the Board of Directors Regulations.

In particular, the duty of loyalty obliges directors to:

- a) Not use their authority for any purposes other than those for which it has been granted.
- b) Keep secret all information, data, reports or records to which they may have access to the performance of their duties, even after they have left office, except where permitted or required by law.
- c) Refrain from deliberating or voting on resolutions or decisions in which they, or persons related to them, have a direct or indirect conflict of interest. Resolutions or decisions that affect a director as such, such as those concerning a director's appointment to or removal from positions on the Board of Directors or other such decisions, are excluded from the abovementioned obligation to refrain.



TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA

TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE

OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

- d) Carry out their duties in accordance with the principle of personal responsibility, exercising their own judgment, independently of any instructions from or ties to third parties.
- e) Take the necessary steps to avoid situations in which their activities, whether for their own account or on behalf of others, conflict with the interests of the Company and their duties to the Company.

> Duty to avoid conflict of interest situations

The duty to prevent conflicts of interest referred to in paragraph e) of the previous section obliges directors to refrain, in particular, from:

- a) Entering into transactions with the Company, except for small-scale, ordinary transactions carried out on the standard terms for customers, that is to say, transactions that do not need to be reported in order to give a true and fair view of the Company's assets and liabilities, financial position and results of operations.
- b) Using the Company's name or their status as directors to unlawfully influence the execution of private transactions.
- c) Using the Company's assets, including confidential information, for private ends.
- d) Exploiting the Company's business opportunities for their own benefit.
- e) Seeking advantages or remuneration from parties other than the Company or the Group for the performance of their duties, unless the advantages or remuneration consist of mere business courtesies.

- f) Carrying on activities for their own account or on behalf of others that actually or potentially bring them into competition with the Company or that in any other way place them in permanent conflict with the interests of the Company.

The above provisions will also apply if the beneficiary of the prohibited actions or activities is a person related to a director, within the meaning of applicable laws and regulations.

In any case, directors must notify the Board of Directors of any direct or indirect conflict that may exist between their own interests, or those of persons related to them, and the interests of the Company.

Any conflicts of interest directors may have will be reported in the notes to the financial statements.

> Non-public information

Directors must also refrain from performing, or suggest that anyone perform, a transaction involving securities of the Company or its subsidiaries, associates or related parties, on the basis of information obtained from their office, or insider or reserved information, as long as this continues to be non-public information.

This is without prejudice to the rules of the Internal Code of Conduct in the Securities Market that may be applicable in each case.



> Directors' duty of disclosure

Directors must disclose to the Company any interests they may have in the Company and any options on shares or derivatives linked to the value of the shares, whether held directly or through companies in which they have a significant interest. This disclosure will include any changes to such interests or associated rights, independently of compliance with securities market regulations.

Directors must also disclose to the Company their other professional obligations, in case those other obligations could interfere with their obligations as directors of the Company. In particular, they must disclose all the positions they hold and all the activities they carry out in other companies or entities whose business is the same, analogous or complementary to that of the Company or any Group company, or that are in any way competitors of the Company; as well as any ownership interest in such companies and, in general, any other circumstance or situation that could be relevant to their performance of their duties or their independence of judgment as directors of the Company.

Directors must notify the Company of any material change in their situation which affects the characteristic or condition that was the basis for their appointment as directors or which might entail a conflict of interest.

Director must disclose to the Company any proceedings brought against them in court, through administrative channels or in any other form that are of sufficient importance to have the potential to harm the Company's name and reputation, in particular any criminal proceedings in which they are the subject of investigation, as well as the progress and outcome of such proceedings.

Removals

Article 24 of the Board of Directors Regulations provides that the directors shall cease to hold office when the term for which they were appointed expires, or when so resolved by the shareholders at the Shareholders' General Meeting in the exercise of the powers legally granted to them.

Furthermore, a list was drawn up describing the cases in which the directors must tender their resignation to the Board of Directors and, if the Board so decides, resign.

In 2016 the independent director Mr. Agustín Conde Bajén gave notice that he had been appointed Deputy Minister of Defence and tendered his resignation, which was accepted by the Company's Board of Directors at its meeting on 29 November 2016, in compliance with the provisions of the former Article 22.4 (currently 24.4) of the Board of Directors Regulations. This resignation was reported to the CNMV as a Relevant Event on 29 November 2016.



Directors' Portal

The Directors' Portal is a project that began seven years ago, with a view to applying new technologies in the day-to-day work of the members of the Board of Directors and its committees.

The portal places the most modern electronic means at the disposal of the directors, so as to enhance efficiency in the functioning of the Board of Directors and its committees. The portal was designed to make the existing processes more efficient and ensure security of information.

The content of the portal is divided into sections, distinguishing between documentation relating to Board meetings, documentation relating to the Board's two committees and other documents of special interest to the Board. It also includes various sections with corporate information about the Company, the main legislation affecting the Company's activities, all the corporate information of interest to the directors in the exercise of their duties, information on the activities and functioning of the Company's various organisational areas, press information concerning the Company and other information which may help the directors gain a better understanding of the Company's activity and functioning and assist them in the performance of their duties as directors.

The content of the Directors' Portal has been extended several times to include information on corporate responsibility, expand the corporate documentation and make technical improvements, making it a highly-valued tool by the directors.

The Director's Portal is constantly reviewed to ensure it is always up to date and that all possible improvements are made.

In 2016, following a thorough review of the portal, a new tool was implemented: in view of the considerable advances in information technology in recent years and building on the experience acquired to date, the portal was subjected to a structural and functional review, with the aim of implementing technical improvements (software modernization, compatibility with new mobile electronic devices and browsers, etc.) that would make it more modern and more efficient.

Board assessment

In recent years, Red Eléctrica has been making large efforts in corporate governance by adopting applicable best practices, aiming to provide greater information transparency to investors and other stakeholders.

Red Eléctrica has been one of the first companies to implement a voluntary assessment of its governing body. For the last years it has used external advisers to bring a more objective, more independent point of view to bear on the Board's self-assessments, following the recommendations established by recent amendments to legislation and the good practices applicable in the field of corporate governance.

The self-assessment for 2015, which focused on the Board of Directors and its committees, addressed areas such as the performance of the functions of the governing bodies, the relations with shareholders and investors, and the Board of Directors' remuneration policy. In carrying out the assessment Red Eléctrica had the assistance, for the third time, of PricewaterhouseCoopers [PwC].



TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



The self-assessment was carried out through interviews conducted by PwC with the directors, under the supervision and coordination of the Appointments and Remuneration Committee and the Lead Independent director. During the interviews, the directors gave their opinion on the topics that were raised.

The final report on the conclusions was approved by the Board of Directors at its meeting on 28 June 2016, after a long period of debate and reflection.

As in previous years, the results of the self-assessment show that Red Eléctrica's governing bodies are highly efficient and work well, receiving very positive assessments for their internal structure and functioning and fulfilment of their assigned responsibilities.

It is worth noting that most of the directors have a good opinion regarding the involvement of the Board of Directors in the Strategic Plan approval processes and the separation of the positions of Chairman of the Board and Managing director of the Company, assessing the advantages of said organisation model for Red Eléctrica and its shareholders.

The performance of the functions assigned to the various governing bodies was also very positively regarded, highlighting the interaction between the Board of Directors and senior management, in particular the willingness of the Company's executives to make themselves available, the rigour and careful preparation of their appearances before the Board and their acceptance of the Board's guidance and supervision.

The 2015 self-assessment showed that the Company is advanced in terms of corporate governance and is currently in line with substantially all the recommendations of the new CBGSC, as approved by the CNMV at the beginning of 2015. Most of the directors are of the opinion that, generally speaking, the changes introduced by the reform of the LSC and the new CBGSC will require some slight adaptation but do not substantially affect the functioning of the Company.

As required by the LSC, the Board of Directors proposed an action plan specifying areas for improvement.

Once the results of the self-assessment had been analysed, the progress made to date and the areas for improvement were identified. The main challenges to be addressed in the short and medium term in order to continue improving in the matter of corporate governance are as follows:

- Continue to develop good practices within the Company's governance model, looking beyond the new regulatory requirements contained in the LSC.

TITLE III
THE YEAR 2016
IN RED ELÉCTRICA



TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE



OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



► Continue to implement professional development programmes for directors on subjects related to the energy sector, taxation, innovation and technology, risk management and corporate governance, and other matters of interest for the proper functioning of the Board.

► Continue to develop and strengthen the model of relations between Red Eléctrica's governing bodies and investors and proxy advisors, as well as the policy for communication and contacts with institutional investors and proxy advisors.

► Continue to organise and structure the relations and interactions between the Board of Directors and/or its committees and the Company's senior management.

► Monitor effective implementation of, among others, the following:

- Reflect on the Board of Directors' performance of its supervisory functions and senior management's performance of its executive functions, seeking to clearly separate responsibilities in each area, so as to prevent possible dysfunctions and align expectations.
- Review the functions of the Lead Independent director and their appropriateness to the new Company's governance structure.
- A more precise description of the responsibilities of the Appointments and Remuneration Committee in relation to the appointment of the Company's senior managers.
- Review the scope of the Board of Directors' self-assessment.

► Take further steps to design and put in place a succession plan that establishes the guiding principles and mechanisms of succession, with a special focus on the positions of Chairman and Managing director.

The firm of consultants that has assisted with the assessment of the Company's Board has other business relationships with the Company and companies in its Group. The fees earned by the consultants for the services provided in the assessment of the Company's Board of Directors represent 14.14% of the total fees for services provided by the firm to the Company and companies in its Group.

The assessment for 2016, currently under way, is being carried out with the help of a new external consultant, bringing a different point of view to the new self-assessment process, with the aim of continuously improving the functioning of the Board of Directors and its committees.

Board remuneration policy

The main elements and aspects of the policy on directors' remuneration are described in Chapter I of this Title II, to which readers are referred to avoid unnecessary repetition.





CHAPTER V

BOARD COMMITTEES

The committees created by the Board of Directors to support it in its duties are eminently specialised and are designed for efficiency and transparency.

Pursuant to the Bylaws and the Board of Directors Regulations, the Company has two Board committees: the Audit Committee and the Appointments and Remuneration Committee. The roles and responsibilities of these committees are established in the Bylaws, which at the Shareholders' Annual General Meeting held on 15 April 2015 were amended to bring them into line with the new rules introduced by Act 31/2014 of 3 December, amending the LSC for the improvement of corporate governance. The Board of Directors Regulations was also amended, on 20 December 2016, to fully adapt them to the recent reforms of the LSC and the CBGSC and improve the organisation and functioning of Board committees in line with the new organisational structure, among other things.

Following the recent reforms of the LSC, the latest international practices and recommendations regarding the composition and independence of the committees and the qualifications of their members have been consolidated. The main points were already covered in the amendments to the Bylaws and the Board of Directors Regulations approved in 2013. Nevertheless, these corporate regulations have been reviewed to fully adapt their content to the new act and to incorporate amendments required by Act 22/2015, of 20 July (the Audit Act).

As regards committee composition, at its meeting on 24 November 2015, further to a proposal made by the Chairman of the Board of Directors and subject to a prior opinion from the Appointments and Remuneration Committee, the Company's Board of Directors agreed to increase the number of members of each Board committee (the Audit Committee and the Appointments and Remuneration Committee) from four [4] to five [5]. The Board of Directors Regulations, which were amended on 20 December 2016, sets the number of members of Board committees at five (previously the number was set at no fewer than three and no more than five).



TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



This measure gives the Appointments and Remuneration Committee greater independence in the exercise of its functions [Article 24.3 of the Bylaws and the new Article 17 of the Board of Directors Regulations], as the independent directors [three out of five members, including the independent director vacancy] are more strongly represented [equivalent to 80%] and carry more weight in decision making. The presence of women on the Appointments and Remuneration Committee has also been increased [three out of four members, not counting the abovementioned vacancy], in compliance with the obligation established in the new Article 18.1. n) of the Board of Directors Regulations to ensure that gender diversity is taken into account when filling new vacancies by setting a target for the representation of the less well-represented gender and preparing guidelines on how to achieve that goal. The increase in the number of members of the Appointments and Remuneration Committee from four to five, all of them non-executive directors and a majority of them independent, also meets the demands of Article 529 *quindecies* of the LSC, which establishes that 'the Appointments and Remuneration Committee shall be composed exclusively of non-executive directors appointed by the Board of Directors, at least two of whom shall be independent directors', and reinforces compliance with Recommendation 47 of the CBGSC, which recommends that a majority of the members of said committee be independent directors, given that the proportion of independent directors on the committee has increased.

With the increase in the size of the Audit Committee from four to five members and the inclusion of a proprietary director, the Company continues to comply with the rule that the committee be made up of a majority of independent

directors and continues to maintain the committee's independence in the exercise of its functions [Article 23.3 of the Bylaws and the new Article 15 of the Board of Directors Regulations], given that the independent directors [three out of five members] continue to have more weight in decision making. One of the five members of the Audit Committee is a woman. The expansion of the Audit Committee to five members, all of them non-executive directors and a majority of them independent, meets the demands of Article 529 *quaterdecies* of the LSC, which establishes that 'the Audit Committee shall be composed exclusively of non-executive directors appointed by the Board of Directors, at least two of whom shall be independent directors and one of whom shall be appointed based on his knowledge and experience in matters of accounting, auditing or both', and Recommendation 39 of the CBGSC, which recommends that the members of the Audit Committee, especially its chairman, be appointed having regard to their knowledge and experience in matters of accounting, auditing or risk management and that a majority of the members of the committee be independent directors.

At 31 December 2016, both Board committees were chaired by independent directors and the chairman of the Appointments and Remuneration Committee was a woman.

TITLE III
THE YEAR 2016
IN RED ELÉCTRICA

TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE

OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER



For more details, as usual, a copy of the annual activity report of both committees for 2016 is included in Chapter IV, Title III of this report. Both reports are due to be published, separately, on the corporate website.

1. Audit Committee

The Audit Committee is made up of five members, as provided in Article 23 of the Bylaws and Article 15 of the current Board of Directors Regulations, all of them appointed from among the non-executive directors and a majority of them being independent directors, for a term of no more than three years.

Throughout 2016, the committee was made up exclusively of non-executive external directors, with a majority of independent directors. The composition of the Company's Audit Committee at 31 December 2016 was as follows:

Director	Position	Type of Director
José Luis Feito Higuera	Chairman	Independent non-executive
Fernando Fernández Méndez de Andrés	Member	Proprietary non-executive (SEPI)
Antonio Gómez Ciria	Member	Independent non-executive
Santiago Lanzuela Marina	Member	Proprietary non-executive (SEPI)
María José García Beato	Member	Independent non-executive

The changes in the composition of the Audit Committee during 2016 were as follows:

- Ms. Paloma Sendín de Cáceres ceased to be a member of the Audit Committee when her term of office as an independent director of the Company expired at the Shareholders' Annual General Meeting held on 15 April 2016.
- At its meeting on 26 April 2016, the Board of Directors of Red Eléctrica appointed the independent director Ms. M^a José García Beato as a member of the Audit Committee for the three-year term specified in the Board of Directors Regulations, so as to fill the vacancy on the Audit Committee, following her removal as a member of the Appointments and Remuneration Committee.

The directors who make up the Audit Committee are particularly well qualified for office and have extensive professional experience, having held senior positions outside Red Eléctrica in functions related to those entrusted to the committee. Their professional profiles show their considerable knowledge and experience in accounting, auditing or both, which has been taken into account in their appointment, in accordance with Article 529 *quaterdecies* of the LSC and Recommendation 39 of the CBGSC. Article 15.2 of the new Board of Directors Regulations introduces an additional criterion: in assessing candidates for positions on the Audit Committee, especially the position of chairperson, the candidates' knowledge and experience of risk management must also be taken into consideration, as well as their knowledge and experience in the fields of accounting and auditing.



The committee's chairman is chosen by its members from among the independent directors on the committee and its secretary is the Secretary of the Board of Directors.

The secretary of the Audit Committee is the Secretary of the Company's Board of Directors.

During 2016, the Director of Audit and Risk Control, and the Corporate Director of Economics & Finance regularly attended meetings of the Audit Committee to report on various matters falling within the committee's remit.

In 2016, in connection with the review of the financial statements for 2015 of the Company and the Group, the external auditor of the Company and its Group explained the audit process and the final audit opinion, which is entirely clean and unqualified, distributing a report with the conclusions of the audit and responding to questions raised by the members of the committee. The committee agreed to issue a favourable opinion on the 2015 Annual Accounts.

Functions

Under Article 23 of the Bylaws and the recently amended Article 16 (formerly art.14) of the Board of Directors Regulations, the functions of the Audit Committee include those of providing support to the Board of Directors in its task of supervising the financial reporting process, monitoring the Company's internal control, verifying the independence of the external auditor, overseeing compliance with the law and with internal regulations and the rules governing relations with the Company's shareholders, and any other responsibilities expressly assigned to it by the Board of Directors.

Following the latest reforms of the LSC for the improvement of corporate governance, the minimum responsibilities of the Audit Committee are now regulated by law, which is why the Bylaws and Board Regulations have been amended in order to fully adapt them to the new LSC. The Shareholders' Annual General Meeting held on 15 April 2015 approved an amendment to the Bylaws, aimed at fully adapting the functions attributed to the Audit Committee to the new requirements of the LSC, most of which were already met by the Bylaws. A particularly relevant and important change is the express assignment of responsibility for supervision of the system for managing tax risks.

At its meeting on 20 December 2016, the Board of Directors approved a set of amendments to the Board of Directors Regulations in order to fully adapt them to the latest reforms of the LSC and the CBGSC, among other things.

2. The Appointments and Remuneration Committee

Act 31/2014 of 3 December introduced the obligation for listed companies to create an Appointments and Remuneration Committee, chaired by an independent director and made up exclusively of non-executive directors, including at least two independent directors. The Act also established certain minimum duties in relation to appointments and remuneration. In Red Eléctrica, the committee that for many years has performed all these functions and responsibilities is the Appointments and Remuneration Committee. Both in its composition and in its functions, the Appointments and Remuneration Committee substantially meets the requirements of the amended LSC





[Article 529 *quindecies* LSC], although at the Annual General Meeting held on 15 April 2015 the Bylaws were amended to bring them more fully into line with the LSC. The changes made to the Board of Directors Regulations on 20 December 2016 to adapt them to the latest legislative reforms, in line with the amendments to the Bylaws, also included some improvements to the organisation and functioning of this committee.

According to Article 24 of the Bylaws and Article 17 of the new Board of Directors Regulations, the Appointments and Remuneration Committee is composed of five members appointed from among the non-executive directors and a majority of its members are independent directors.

This composition is in line with the corporate governance best practices included in the LSC, which recommends that the committee have no executive members and that the majority of its members be independent directors.

It is worth noting that already in 2012, even before the Board of Directors Regulations were amended in 2013, the Board of Directors decided to adjust the composition of the Corporate Responsibility and Governance Committee so that, for the first time, it did not include the Company's Executive Chairman.

The chairman of the Appointments and Remuneration Committee is an independent director chosen from among its members and its secretary is the Secretary of the Board of Directors.

The secretary of the Appointments and Remuneration Committee is the Secretary of the Company's Board of Directors.

Committee members are appointed and removed by the Board of Directors, at the proposal of the Board Chairman. They hold office for a term of no more than three years and may be reappointed. They are removed from their position when they lose director status or when so agreed by the Board of Directors, further to a report issued by the Appointments and Remuneration Committee. The committee's chairman is appointed for a three-year period and may be re-elected after a one-year break in service.

The changes in the composition of the Appointments and Remuneration Committee during 2016 were as follows:

- At its meeting on 26 January 2016, the Board of Directors of Red Eléctrica Corporación, S.A. appointed Mr. José Ángel Partearroyo Martín, a proprietary director representing SEPI, to be a member of the Appointments and Remuneration Committee for a three-year term, in order to fill the vacancy arising on the committee as a result of the resignation of the proprietary director Mr. Francisco Ruiz Jiménez.
- At its meeting on 26 January 2016, the Board of Directors of Red Eléctrica Corporación, S.A. appointed Mr. Agustín Conde Bajén to be a member of the Appointments and Remuneration Committee for a three-year term, in order



to fill the vacancy arising on that committee as a result of the resignation of M^a José García Beato, who was appointed a member of the Audit Committee.

- At its meeting on 29 November 2016, the Board of Directors accepted the resignation of Mr. Agustín Conde Bajén, who had given notice of his appointment as Deputy Minister of Defence, giving rise to a vacancy on the Board of Directors and the Appointments and Remuneration Committee.

The members of the Appointments and Remuneration Committee at year-end 2016 were as follows:

Director	Position	Type of director
Carmen Gómez de Barreda Tous de Monsalve	Chairperson	Independent non-executive
Socorro Fernández Larrea	Member	Independent non-executive
María Ángeles Amador Millán	Member	Independent non-executive
José Ángel Partearroyo Martín	Member	External Proprietary
Vacant [7]	Member	Independent non-executive

[7] The vacancy on the Appointments and Remuneration Committee arose following the resignation of the independent director Mr. Agustín Conde Bajén, which was accepted by the Board of Directors at its meeting on 29 November 2016.

The committee's members have been appointed by the Board of Directors at the proposal of its Chairman for a three-year term, subject to a prior report from the Appointments and Remuneration Committee.

All the committee members have a proven capacity to perform the tasks entrusted to the committee, based on their extensive experience and knowledge.

At 31 December 2016, given four members (not counting the vacancy), 75% of the committee's members were women, including its Chairperson. At that same date, independent directors (counting the vacancy for one independent director), accounted for 80% of the committee's members and the Chairperson was an independent nonexecutive director.

Functions

The minimum functions of the Appointments and Remuneration Committee are regulated in Article 24.2 of the Bylaws, following the amendment approved at the Shareholders' Annual General Meeting held on 15 April 2015 to fully adapt them to the reform of the LSC.

The committee's functions are specified in Article 18 of the recently amended Board of Directors Regulations. As already stated, during 2016 the Board of Directors Regulations were reviewed and adapted to the latest reforms of the LSC (bearing in mind that the main points of the reforms were already covered in the regulations) and the CBGSC and improvements were made to the organisation and functioning of the committee, among other things. As with the Audit Committee, the functions assigned to the Appointments and Remuneration Committee in the Board of Directors Regulations were amended.



CHAPTER VI

THE LEAD INDEPENDENT DIRECTOR

1. Introduction

In accordance with international standards of corporate governance, it is recommended that listed companies separate the positions of Managing director and Chairman of the Board of Directors.

The basic principle of this requirement is to avoid the risk of concentrating too much power in the hands of a single person, who performs both roles (Chairman and Managing director) at the same time, which could prevent or impede both the Board of Directors and senior management from performing their assigned functions appropriately and with the necessary independence.

At the proposal of the Appointments and Remuneration Committee, the Company's Board of Directors resolved to create the position of Lead Independent director. The Bylaws were amended accordingly at the Shareholders' Annual General Meeting held on 18 April 2013. At its meeting on 28 May 2013, the Board of Directors appointed Ms. Carmen Gómez de Barreda Tous de Monsalve as lead independent director for a period of three years. At its meeting on 31 May 2016, the re-election for a further three-year term of Ms. Gómez de Barreda was agreed.

In the 'Report on the separation of the positions of Chairman of the Board of Directors and Managing director of the Company' that was submitted to the Shareholders' Extraordinary General Meeting on 17 July 2015, the Appointments and Remuneration Committee and the Company's Board of Directors concluded that the role of Lead Independent director on the Board of Directors of Red Eléctrica Corporación, S.A. should be maintained even after the separation of roles was completed.

It is worth noting that the current Lead Independent director played an important role in the design, planning and implementation of the process of separation of positions.

Lastly, the Lead Independent director has been contributing in the annual Board self-assessment and the ongoing preparation and updating of the Succession Plans for the Chairman of the Board of Directors and the Managing director.

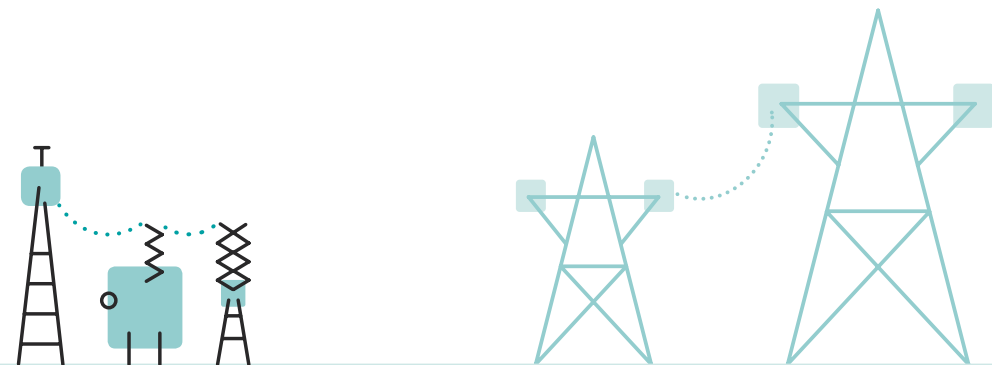


2. Functions

The core responsibility of Red Eléctrica's Lead Independent director, as established in Article 25 *bis* of the Bylaws, following the amendment adopted by the Shareholders' Annual General Meeting held on 15 April 2015 aimed at adapting them to the reform of the LSC, is to organise any common positions of the non-executive directors, in particular the independent non-executive directors, and to serve as a channel of communication or as spokesperson for such common positions to the Chairman of the Board of Directors, the Board as a whole and the Board committees.

The term of office of the Lead Independent director is three years and the position holder may be reappointed for further terms. The appointment will be terminated when the Lead Independent director ceases to be a director or loses his or her independent status or when the Board of Directors, at the proposal of the Appointments and Remuneration Committee, so decides.

In 2016 the Lead Independent director held various meetings with independent directors to hear their concerns and organise common positions on various matters discussed by the Board of Directors and took part in the road shows with proxy advisors organised by the Company in January 2016 and 2017.





CHAPTER VII THE MANAGING DIRECTOR

The Shareholders' Extraordinary General Meeting held on 17 July 2015 that approved the 'Report on the separation of the positions of Chairman of the Board of Directors and Managing director of the Company' also resolved to increase the number of directors by one and appointed Mr. Juan Francisco Lasala Bernad as executive director of the Company. Subsequently, at its meeting on 28 July 2015, the Company's Board of Directors appointed the executive director, Mr. Juan Francisco Lasala Bernad, to be Managing director of the Company.

According to the 'Report on the separation of the positions of Chairman of the Board of Directors and Managing director of the Company' and the provisions of the new Article 11 of the Board of Directors Regulations, the responsibilities of the Managing director, as Chief Executive of the Company, are as follows:

- a) Supervise, coordinate and drive the management of the organisation and business areas of the Company and the Group;
- b) Lead, drive and guide the execution and implementation of the Strategic Plan of the Company and the Group;
- c) Ensure efficient implementation of the risk control system approved by the Board of Directors in the Company and the Group and effective oversight of its operation;
- d) Regularly report to the Board of Directors on the degree of execution and completion of the Strategic Plan and the Budget, the functioning of the risk management system and the progress achieved in the management of the Group's business areas, so that the Board is able to adequately and effectively exercise its general oversight and control function.

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



The Board of Directors Regulations as amended on 20 December 2016 set out the basic responsibilities and powers of the Managing director. In particular, the responsibilities of the Managing director specified in the 'Report on the separation of the positions of Chairman of the Board of Directors and Managing director of the Company', indicated earlier in this section, were transferred to the new Article 11 of the Board of Directors Regulations.

That article also establishes that the Managing director will act as Chief Executive of the Company and will be responsible for the day-to-day running and effective management of the organisation and business areas of the Company and the Group, always in accordance with the decisions and criteria set by the Shareholders' General Meeting and the Board of Directors, each within the scope of its powers.

The managing director, Mr. Juan Francisco Lasala Bernad, has all the powers the Board of Directors is permitted by law and the Bylaws to delegate to the Managing director, pursuant to the Board of Directors resolution adopted on 28 July 2015.

The LSC sets forth a list of reserved responsibilities of the Board of Directors (arts. 249 *bis* and 529 *ter*) and the Company's Board Regulations provide likewise (art. 5, recently amended).

Following the separation of the positions of Chairman and Managing director and the transfer of executive functions to the latter, which was completed at the Shareholders' Annual General Meeting held on 15 April 2016, Mr. José Folgado Blanco was re-elected as a director in the 'other external' category. Consequently, at its meeting on 31 May 2016 the Board of Directors resolved to revoke the authority granted to him pursuant the Board of Directors resolution adopted on 26 April 2012.



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA



TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE



OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER



CHAPTER VIII SENIOR MANAGEMENT

The persons holding senior management positions at the Company at 31 December 2016, excluding the Managing director, are as follows:

Name	Position
Ms. Eva Pagán Díaz	General Manager, Transport
Mr. Miguel Rafael Duvison García	General Manager, Operations

Article 18.1 of the new Board of Directors Regulations establishes that one of the basic responsibilities of the Appointments and Remuneration Committee is to 'Report on the appointment [based on ability, trust and, as far as possible, internal promotion] and removal of senior managers who report directly to the Board, the Chairman or the Managing director, and the basic terms of their contracts'.

In the new organisational structure the senior managers named in the above table report directly to the Company's Managing director.

The remuneration policy applicable to these senior managers is intended to promote the achievement of the Company's strategic objectives of value creation by attracting, retaining and motivating the best talent available in the market. Under Article 5.5.a) viii] of the new Board of Directors Regulations it is a reserved responsibility of the Board of Directors to approve the policy on remuneration of senior managers who report directly to the Board, the Chairman or the Managing director.

Remuneration for the Company's senior managers is based on the principles of moderation, actual time commitment and linkage to the Company's results.

Information on the total remuneration paid to these senior managers is provided in the annual directors' remuneration reports, which are submitted to the Board of Directors and the Shareholders' Annual General Meeting for approval, and the Company's annual report.

Information on the remuneration of these senior managers for financial year 2016 is given in the annual directors' remuneration report approved by the Board of Directors in February 2017, which includes information on senior managers, along with the information contained in the Company's annual accounts for 2016.



CHAPTER IX

RISK MANAGEMENT POLICY AND INTERNAL CONTROL SYSTEMS

1. Scope of the Company's risk management system, including the system for managing financial risks

A risk management system has been in place since 2002 and the Company developed its first Risk Map in 2003.

The risk management system operates across the entire organisation and as an integrated whole and is consolidated at corporate level by business unit, subsidiary and support area.

The purpose of this integrated risk management system is to ensure that any risks affecting the Red Eléctrica Group's strategies and objectives are systematically identified, analysed, assessed, managed and controlled, applying uniform criteria, within the established risk limits, so that the Group's strategies and objectives can be accomplished.

The Red Eléctrica Group has an integrated risk management policy and a general procedure for enterprise risk management and control, based on the COSO II Integrated Framework for Enterprise Risk Management [Committee of Sponsoring Organisations of the Treadway Commission]. Both the policy and the procedure were updated at the end of 2016.

Integrated risk management policy

According to the Board of Directors Regulations of Red Eléctrica Corporación, approving the risk control and management policy is the responsibility of the Board of Directors.

The risk control and management policy identifies the different types of risk, sets the level of risk the Company considers acceptable and sets out action guidelines to manage and mitigate risk.

In September 2015 this policy was expanded to include the tax risk control and management policy and the action guidelines for managing and mitigating tax risks.

The tax risk control and management policy sets out the Group's tax strategy, as approved by the Board of Directors on 30 June 2015. In 2015, the Board of Directors decided that the Group should become a signatory to the Code of Best Tax Practices, which identifies practices that help to reduce significant tax risks and prevent behaviours liable to create such risks.



The updated version of this policy [5th edition] was approved by the Board of Directors in December 2016.

The integrated risk management policy is fully aligned with the Group's current Strategic Plan and is available in the 'Corporate Governance' section of the corporate website.

General procedure for integrated risk management and control

This procedure regulates the identification, analysis, assessment and control of the material risks faced by the Group. It establishes the purpose, responsibilities, activities and tasks of the integrated risk management system.

The procedure is intended to ensure that managers at all levels within the Group are aware of and assess the risks that threaten the Group's strategies and objectives, take those risks into account in their activities and keep them within the set levels of acceptable risk.

The updated version of this procedure [5th edition], which was approved by the Management Committee in November 2016, establishes the purpose, responsibilities, activities and tasks of the system.

In 2015 work started on a gradual review of the compliance of the five components of internal control, in accordance with the COSO Integrated Framework, May 2013. At the end of 2015 the audit firm Ernst & Young reviewed the first of these components ['control environment'] and in November 2016, the second ['risk assessment']. In both reviews the auditors came to the conclusion that the elements and activities relating to the control environment are formally structured and in place in all areas/operations of the organisation and that, furthermore, in many cases the best practices in this field have been implemented.



2. Company bodies responsible for the preparation and implementation of the risk management system (including the system for managing tax risks)

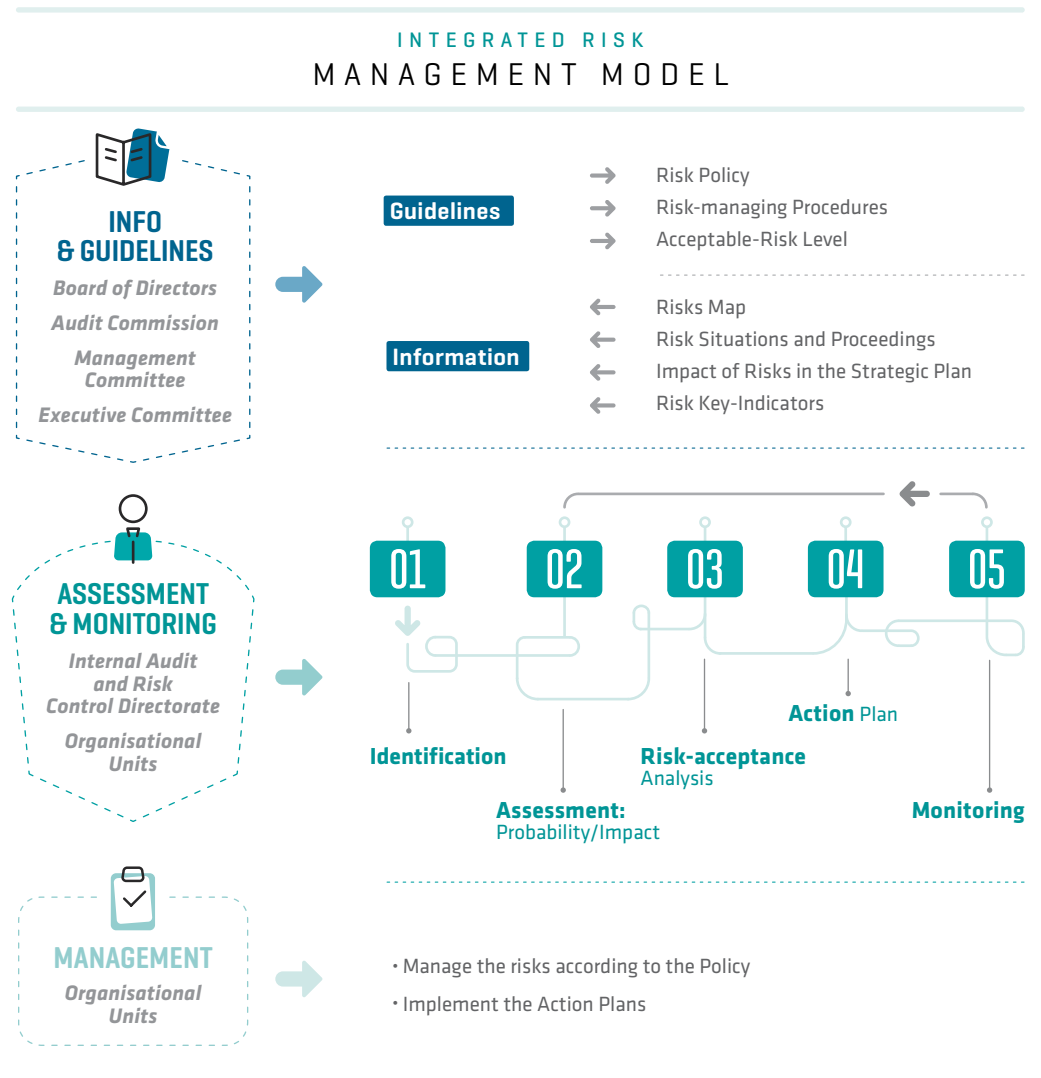
As previously stated, the risk management system is integrated in nature, insofar as all of the Group's business units participate in it, along with the various governing bodies, within a systematised management process, in line with the criteria and guidelines established in the General Policy and Procedure for Enterprise Risk Management and Control.

The policy and the procedure define the various responsibilities of each of the units and governing bodies of Red Eléctrica Group and also the information flows and activities to be carried out, in accordance with the model that appears in the graph below.

The Board of Directors Regulations expressly give the **Board of Directors** responsibility for approving the integrated risk management policy of the Company and the Group. This includes setting the level of acceptable risk and receiving reports on, and periodically monitoring, the internal control, prevention and reporting systems.

The Board reviews the risk control system and material risks, including tax risks, at least twice a year, notwithstanding the information it receives on a regular basis from the Audit Committee as part of the ongoing monitoring process carried out by that committee.

The **Audit Committee** is responsible for periodically supervising the effectiveness of the integrated risk management system (including tax risk) to ensure that material risks are identified, are kept within the established acceptable risk levels and are properly reported.





The **Management Committee**, made up of senior managers from the most important and strategic areas of the Company, is responsible for:

- Monitoring the material risks map.
- Ensuring that the risks classified as 'high' and other especially important risks, as well as the critical action plans to mitigate those risks, are properly controlled and monitored.

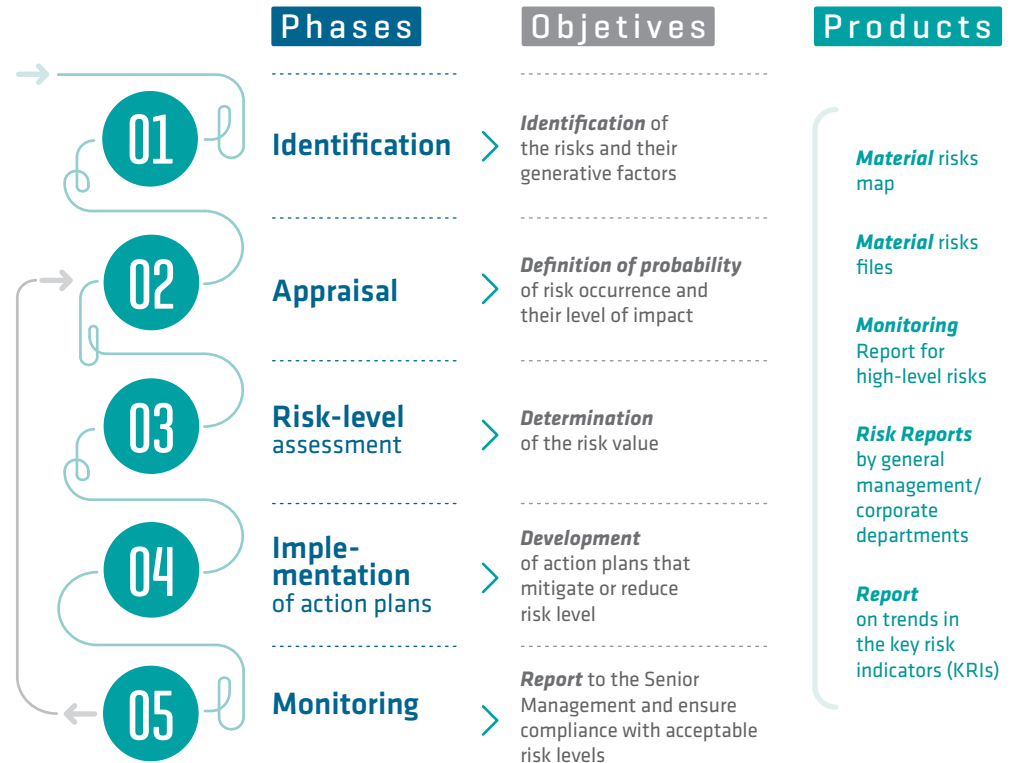
The **Internal Audit and Risk Control Directorate**, reporting to the Company's Chairman's Office, is responsible for coordinating and supporting the risk identification, analysis and assessment process and periodically controlling risks. This directorate submits the appropriate reports to the Management Committee, the Audit Committee and the Board of Directors. The information reported includes the following:

- Material risks map.
- Material risks files.
- Monitoring report for high-level risks and other especially important risks.
- Risk reports by general management and corporate departments.
- Report on trends in the key risk indicators [KRIs].

The **organisational units** re involved in the risk management system through the risk identification, analysis and assessment process, together with the **Internal Audit and Risk Control Directorate**, and also in the implementation of action plans.

Along with the responsibilities assigned to the Group's various units and control bodies, the risk management system establishes the necessary information flows, the actions to ensure systematic risk monitoring and control through a series of activities and deliverables, and the specific methodology for measuring the level of risk.

RISK ASSESSMENT AND MONITORING





3. Main risks (including tax risks) that could affect the achievement of business objectives

The principal business of the Red Eléctrica Group is the transmission of electricity and the operation of the electricity system in Spain, which are regulated activities, insofar as they are critical to the security and continuity of electricity supply and are carried out on an exclusive basis.

This classification as a regulated activity affects both the setting of revenues and the environment and conditions in which it has to undertake its principal activities.

The types of risks the Red Eléctrica Group faces in its efforts to achieve its strategies and objectives can be classified as follows:

Operational risks:

- Operational risks that may affect the electricity system. Risks related to the correct functioning of the transmission network and system operation.
- Environmental and personal safety risks. Risks relating mainly to the environment in which the Group carries on its activities and the safety of the people involved in those activities.
- General security risks. This category groups together the risks related to physical security and cybersecurity.
- Other operational risks. Operational risks not included in the previous categories.

Regulatory risks:

- Regulatory risks as Spanish TSO. Risks associated with the regulations to which the Group is subject in its role as Spanish TSO.
- Other regulatory risks arising from regulations other than those indicated above. These specifically include tax risks. Tax risks: risks arising from the application of tax regulations, difficulties of interpreting those regulations or amendments to those regulations, and the impact the Company's management of its tax affairs could have on its reputation.

Financial and counterparty risks:

- Financial and counterparty risks. Financial risks, market risks and risks arising from the failure of counterparties to perform their contractual obligations.

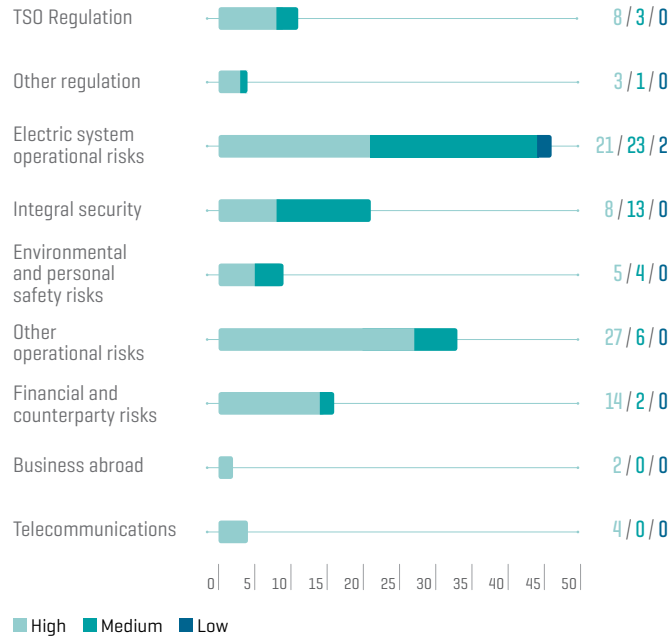
Business diversification risks:

- Risks associated with the telecommunications business.
- Foreign business risks. Groups together the risks arising in the activities carried out by the Group through its foreign subsidiaries.

As already mentioned, the Red Eléctrica Group's tax risk control and management policy was included in the integrated risk management policy in September 2015 and specific guidelines for managing tax risks were established.



Following the risk analysis performed by the Red Eléctrica Group, the latest **Risk Map** identifies 146 risks, distributed by risk type as shown in the following chart.



As in the previous chart, in accordance with the Red Eléctrica Group's risk assessment model (which is analysed in the following section), the risks are classified into three levels (high, medium and low).

The distribution of the risks by category is as follows:

TSO Regulation	8%
Other regulation	3%
System operational risks	31%
Integral security	14%
Environmental and personal safety risks	6%
Other operational risks	23%
Financial and counterparty risks	11%
Business - abroad risks	1%
Telecommunications' risks	3%



The current risk management system monitors risk by organising the surveillance of more than 500 action plans, aimed at reducing the level of risk, and monitoring the level of approximately 300 indicators.

4. Risk tolerance level (including tax risks)

The level of risk the Red Eléctrica Group is willing to accept is set for risks individually and for risks in aggregate (overall acceptable risk level).

Acceptable risk level for individual risks:

The Red Eléctrica Group's risk management system defines a methodology for setting the acceptable level of risk. All identified risks are thus classified in three categories:

- High-level risks
- Medium-level risks
- Low-level risks

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



Two parameters are used to classify risks in these categories: the probability of the risk occurring and the impact it would have on the Company if it did occur.

The probability of occurrence is classified into five levels, based on a specific probability distribution for each type of risk.

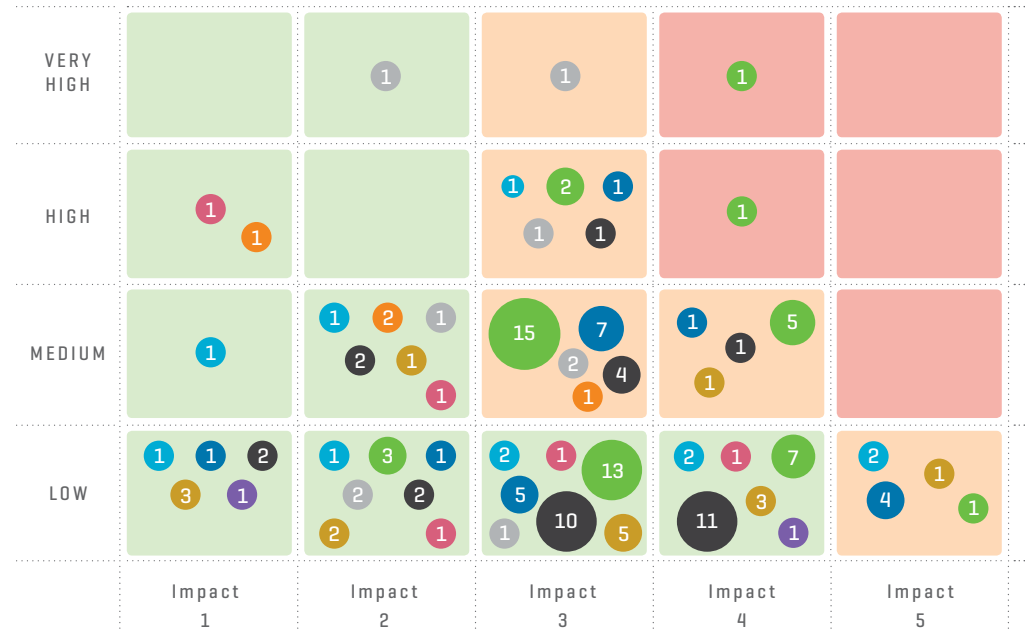
The impact is rated on the basis of the effect a risk could have on four key elements of the business:

- The electricity supply. Measured by Energy Not Supplied (ENS) as a result of the risk event.
- The achievement of basic strategies. Degree of impact on the achievement of basic strategies.
- Reputation. Degree of impact on reputation [geographical scope, duration and reparability].
- The income statement. Impact on the income statement before corporate income tax.

For each of these four elements, Red Eléctrica Group has produced a table showing five levels of effect or impact. For the electricity supply and the income statement, the measurement is quantitative [MWh and Euros], whereas for the achievement of basic strategies and reputation it is qualitative.

A risk's position in the probability/impact matrix, which depends on the probability of occurrence and the level of impact, automatically determines the level [red = high, orange = medium and green = low].

RISK MATRIX



- TSO Regulation
- Other regulation
- Electric system operational risks
- Integral security
- Environmental and personal safety risks
- Other operational risks
- Financial and counterparty risks
- Telecommunications' risks
- Business-abroad risks

This matrix reflects the distribution of the risks based on the year-end 2015 risk assessment. In 2016 the qualitative scale of probability [low, medium, high and very high] was replaced by a percent distribution in five levels, as indicated earlier. The risks will be distributed in the matrix using the new probability scale when the next Risk Map is prepared.



Individual acceptable risk:

The only risks considered acceptable according to the individual acceptable risk level defined by Red Eléctrica Group are those classified as 'low' in the above matrix. Under the risk policy, any risk that exceeds the acceptable level must be managed so as bring it below that level, insofar as it can be managed and the cost of the mitigating measures is justified by the impact the risk could have on the Group if it were to materialize. Every risk classified as acceptable is managed so as to maintain it at that level.

Overall acceptable risk:

In 2016 the Board of Directors approved the Group's overall acceptable risk level for each of the four types of impacts envisaged in the integrated risk management system.

- Impact on the electricity supply.
- Impact on the Group's strategies.
- Impact on reputation.
- Impact on results.

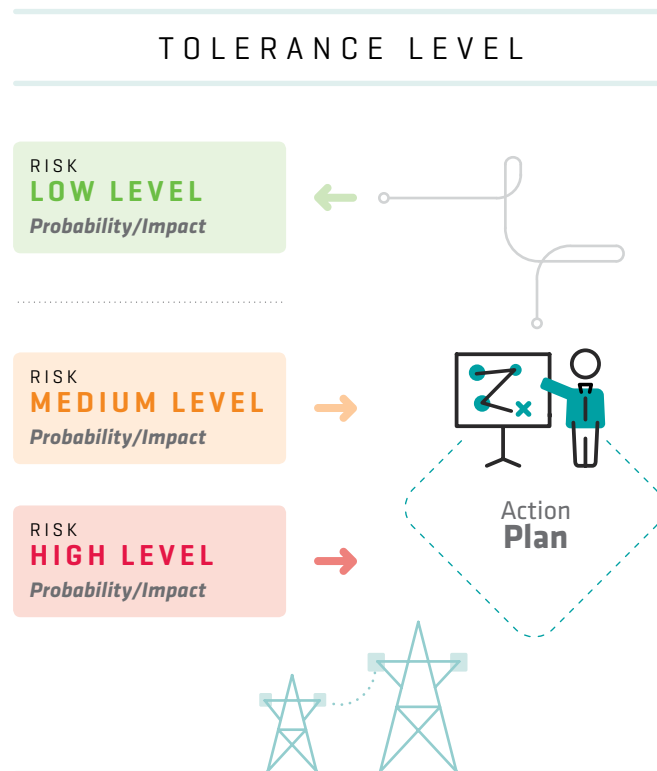
As a general risk management rule, the Group's overall risk level, calculated by statistically aggregating the individual risks, must not exceed the overall acceptable risk level.

5. Risks (including tax risks) that materialised in 2016

None of the risks that materialised in 2016 were significant.

The transmission network facilities are permanently exposed to operational events that may affect the continuity and security of the electricity supply.

During 2016 there were events that resulted in minor power cuts. These events are generally caused by third parties and meteorological phenomena.





The control systems responded appropriately to these events, as evidenced by the availability index of the peninsular transmission network, which in 2016 was 98.33% (provisional figure), close to the 97.93% recorded in 2015.

The Company also has insurance policies in place that limit the potential impact such events may have on the income statement.

6. Risk response and supervision plans for the Company's main risks

Prevention of risks in the design and functioning of Red Eléctrica Group processes

The Red Eléctrica Group's processes have been designed to incorporate elements to mitigate or reduce the abovementioned risks, including tax risks. These processes have been integrated into structured management systems based on international standards (ISO 9001, ISO 14001 and OHSAS 18001, among others). These systems are subject to systematic internal and external audits of the adequacy of their design and compliance and include mechanisms for controlling the objectives they must meet.

Risk response and supervision plans (including tax risks)

The risk identification, analysis, assessment and control process referred to above establishes the actions that must be taken in order to bring the level of risk down to the acceptable level and maintain it at that level.

Once every six months for high-level risks and once a year for other risks, the Internal Audit and Risk Management Department works with the management units to review the performance and impact of the preestablished action plans to reduce risk.

Contingency plans

Red Eléctrica has a general procedure – 'Crisis management (pre-alert, alert and emergency)' – for managing any crisis situations that could occur in the event of:

- An electrical incident that could affect the security of supply (Peninsula, islands or Ceuta and Melilla).
- A non-electrical incident that could affect the environment, people, the Company's ability to operate or its results, or any other event that could affect the Company's reputation.

Challenges for 2017

- Identify short, medium and long-term lines of improvement for Red Eléctrica's integrated risk management system, following best practices.
- Evolve and improve integrated risk reporting.
- Develop the risk identification and assessment methodology by improving the data acquisition process.

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA

TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE

OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

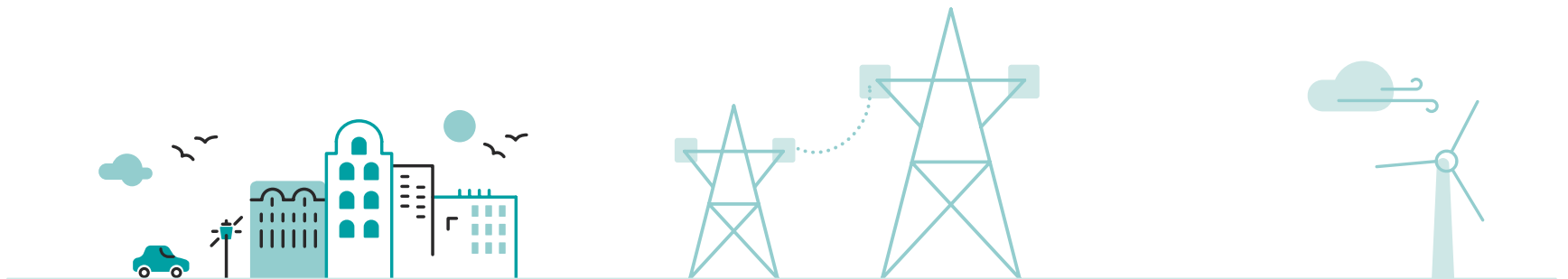
The crisis management procedure:

- ▶ Establishes in general terms the way in which crises are to be managed.
- ▶ Determines the pre-alert, alert and emergency phases for each type of risk that could affect the operation of, or the transmission of electricity through, the electricity system or that could affect people, the environment or the Company's ability to operate or its reputation.
- ▶ Establishes the composition of the committees responsible for managing each type of crisis and the roles and responsibilities of their members.
- ▶ Lists the specific contingency plans in place at Red Eléctrica for each type of event.

Red Eléctrica also has an Action Guide, 'Cyber Incident Management', which establishes the criteria and guidelines for managing cyber incidents, regardless of where they occur.

In addition, Red Eléctrica has a system of Internal Control over Financial Reporting (ICFR), whose purpose is to improve the efficiency and security of the processes involved in preparing financial reports about the Company, including early, voluntary adoption of international best practices. The ICFR system includes Red Eléctrica's tax information and processes and the associated controls.

The ICFR system is described in detail in "SECTION F. INTERNAL CONTROL AND RISK MANAGEMENT SYSTEMS IN CONNECTION WITH THE PROCESS OF FINANCIAL REPORTING (ICFR)", of the *Official Annex to this report, drafted according to the standard form provided in Annex I to CNMV Circular 7/2015 of 22 December* in force at the date of approval of this report.





CHAPTER X RELATED-PARTY TRANSACTIONS

As a result of the amendments to the LSC implemented by Act 31/2014 of 3 December, the obligations arising from the duty to avoid conflicts of interest have been specified in more detail and some of the obligations arising from the duty of loyalty that were already regulated in the LSC prior to the reform have been reformulated. The responsibilities of the Board of Directors and the Audit Committee in relation to transactions with directors have also been regulated in more detail. Following the reform of the LSC, on 20 December 2016 Articles 5, 14 (currently, Article 16) and 32 of the Board of Directors Regulations were amended to adapt them to the current state of the law.

Under the amended Article 5.5 c) of the Board of Directors Regulations, the Board of Directors has a direct responsibility, which cannot be delegated, for approving, subject to a report from the Audit Committee, any transactions the Company or any Group company may enter into with directors, as specified in the LSC, or with shareholders who individually or in concert with others hold a significant interest, including shareholders represented on the Board of Directors of the Company or any Group company and persons related to them. The directors affected, or those who represent or are associated with the shareholders affected, must refrain from participating in the deliberations and voting on the resolution in question. Only transactions that meet all of the following three criteria do not require such approval:

- ▶ They are carried out under contracts the conditions of which are standardised and apply *en masse* to a large number of customers.
- ▶ They are carried out at prices or rates set on a general basis by the person supplying the good or service concerned.
- ▶ Their amount does not exceed 1% of the Company's annual revenue.

Under the current Article 16.6 c) of the Board of Directors Regulations, the Audit Committee is responsible for reporting to the Board on proposed transactions with related parties.

In May 2010, at the proposal of the Audit Committee, the Board of Directors approved a related-party transaction control policy and set objective parameters for controlling related-party transactions (whether material or non-material), annual recurring related-party transactions and transactions that must be disclosed to the markets. The Audit Committee monitors this policy annually and reports to the Board of Directors.

TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES



In 2016, the Audit Committee's Annual Report on Related-Party Transactions for 2015 was published for the first time on the corporate website www.ree.es, in compliance with Recommendation 6 of the CBGSC.

In accordance with the new Article 36 of the Board of Directors Regulations, the Board of Directors has formally reserved the right to approve, subject to a report from the Audit Committee, any material transaction of the Company with significant shareholders, including shareholders represented on the Board of the Company or any Group company, and persons related to them, unless the nature and conditions of the transaction are such that, under Article 5.5 c) of said regulations, it requires the approval of the Shareholders' General Meeting.

Under the new Article 31 e) of the Board of Directors Regulations directors must take the necessary steps to avoid situations in which their activities, whether for their own account or on behalf of others, conflict with the interests of the Company and their duties to the Company and the new Article 32 of the Board of Directors Regulations specifies the duty to avoid conflicts of interest referred to in Article 31 e) by stating the situations which directors' must refrain from incurring.

In any case, directors must notify the Board of Directors of any direct or indirect conflict that may exist between their own interests, or those of persons related to them, and the interests of the Company.

Any conflicts of interest directors may have will be reported in the notes to the financial statements.

In addition, Article 2 of the Company's Internal Code of Conduct in the Securities Market includes within its scope of application directors, the secretary and deputy secretary of the Company's Board of Directors, executives (as defined in Chapter I of the Code) and any persons expressly designated by the Oversight Body created pursuant to the Code.

Under Article 7 of the Internal Code of Conduct in the Securities Market, Obligated Parties and Temporarily Obligated Parties must generally endeavour to avoid situations of direct conflict of interest or conflicts of interest concerning Related Persons and must notify the Oversight Body of any situations of conflict of interest that may reasonably arise within fifteen (15) days of such situations coming to their attention, so that the Oversight Body may adopt the appropriate decisions in advance. In the case of directors, they shall notify the situations described in the preceding paragraph through the Office of the Secretary to the Board of Directors.

Obligated Parties and Temporarily Obligated Parties must keep up to date the information on notified conflicts of interest, reporting all changes as and when they occur.

The Oversight Body must keep up to date an itemised register of any conflicts of interest notified by the various obligated parties and temporarily obligated parties and must adopt adequate security measures for its safe keeping and storage. In any event, access to the register will be restricted.



TITLE III
THE YEAR 2016
IN RED ELÉCTRICA



TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE



OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

**TITLE II
MAIN
ASPECTS OF
CORPORATE
GOVERNANCE
AT RED ELÉCTRICA
AND RELATED
PRINCIPLES AND
PRACTICES**



It should be noted that for the above purposes, in accordance with Article 11 of the Internal Code of Conduct in the Securities Market, the Oversight Body is the Directorate-General of Administration and Finance (following the Company's internal reorganisation, now the Corporate Economic and Financial Department), which will act in collaboration with the secretary of the Board of Directors as regards any legal issues resulting from the application or interpretation of the Code. In addition, the Oversight Body has been entrusted with the general functions of ascertaining, registering, disseminating and monitoring compliance with the obligations and duties established in the Internal Code of Conduct. The Oversight Body will have all necessary powers to perform the duties entrusted to it in the Internal Code of Conduct and must periodically report to the Audit Committee on the degree of compliance with the Code and any incidents that may have occurred.

In relation to the Company's senior managers, Article 2.1.3 of the Internal Code of Conduct in the Securities Market establishes that executives, as defined in said Code, are Obligated Parties.

Following the amendment to the Board of Directors Regulations on 20 December 2016 and the entry into force of the new Regulation [EU] No 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse, the adaptation of the Internal Code of Conduct in the Securities Market is being carried out.

TITLE III
THE YEAR 2016
IN RED ELÉCTRICA

TITLE IV
FUTURE PLANS
OF RED ELÉCTRICA
IN MATTERS OF
CORPORATE
GOVERNANCE

OFFICIAL ANNEX:
STANDARD FORM
OF ANNEX I TO
SPANISH SECURITIES
MARKET COMMISSION
(CNMV) CIRCULAR 7/2015
OF 22 DECEMBER

