



Annual Report
2005

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EMPRESARIAL





2005 Annual Report
Red Eléctrica de España



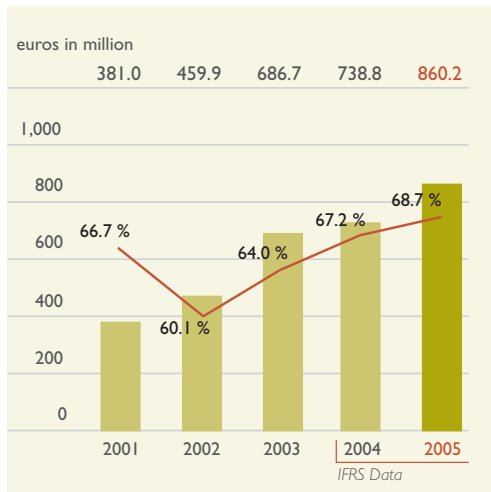
The activities reported in this annual report have been reviewed by the Fundación del Español Urgente (Fundéu).

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2005 main values

Net sales



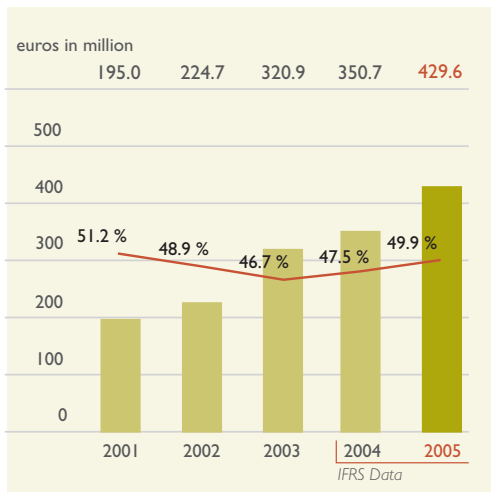
■ Net sales
— EBITDA / Net sales

Profit after taxes



■ Profit after taxes (PAT)
— ROE (PAT / Shareholders equity)

Cash-flow



■ Cash-flow (from operations less paid profit taxes)
— Cash-flow / Net sales

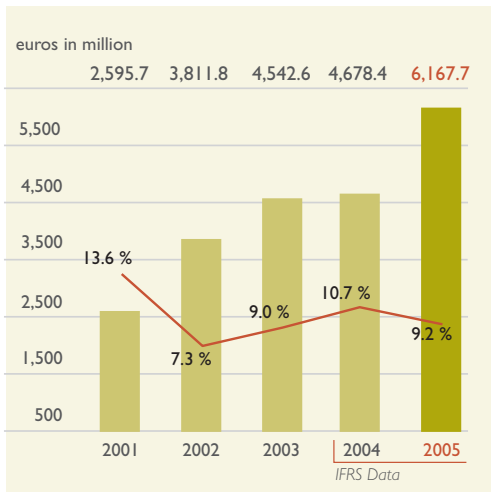
Net financial liabilities



■ Net financial liabilities
— Net financial liabilities / (Net financial liabilities + Shareholders equity)

IFRS (International Financial Reporting Standards)

Tangible fixed assets



■ Tangible fixed assets gross
— ROA (EBIT / Net assets)

Dividends per share*



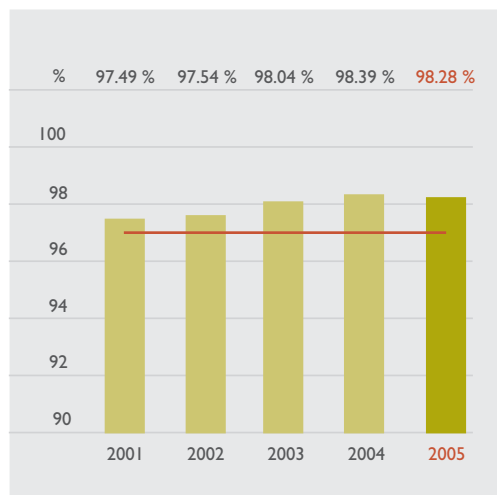
■ Dividends per share

Grid physical quantities*



■ Number of busbar connections in substations
■ Lines circuits in kilometres

Grid performance*



■ Availability rate
— Reference value (R.D. 1995/2000)

* Individual quantities of the head company

Letter from the President



Dear Shareholders:

The outstanding business achievements of Red Eléctrica during 2005, the Utility's 20th Anniversary, have been ratified by our shares excellent performance record in the stock exchanges. A year marked, too, by His Majesty the King Don Juan Carlos I visit to our Main Offices, on the 14th of December 2005. A visit that shows society acknowledges the crucial significance of our work to meet their daily needs.

In 2005, Red Electrica's leading position, as the first utility worldwide devoted exclusively to transmission operations, the service performed for the Spanish Electricity System, has been fully consolidated. The transmission assets purchased from other utilities, during the past few years, have contributed significantly to such purpose. The purchase of the remaining 75% of Redalta assets, the utility that owned Iberdrola's high voltage facilities, and the purchase of Viesgo assets have been implemented this year. We have, therefore, virtually completed the purchase of all the high voltage transmission facilities owned by other utilities. The mentioned transactions have changed significantly Red Electrica Group dimensions, since, in barely four years, transmission assets have increased three-fold. This is why our efforts have been

addressed to develop the business main operation: the supply of top quality service to the Spanish Electricity System. Furthermore, our business growth is based actually on that operation. This decision is disclosed, too, by the disinvestment in telecommunications that led to the subsidiary, Albura, being sold in June 2005.

The large capacity for business generation and value development that issues from the above-described new dimension, due to economies of scale and the attendant synergies, are one more year evidenced by the rather significant increase financial results show. The Group's profit after taxes has reached Euros 162.4 million, or 19.6% over that of the previous year. In this growth path, cash flow stands at Euros 429.6 million, which implies a 22.5% increase over 2004.

Red Eléctrica Group has scheduled sizeable investments to enlarge and improve Spain's transmission grid in line with the stated purpose of targeting resources in its main business. Through the mentioned investments, the electric system is expected, first of all, to achieve sufficient capacity and flexibility that will ensure electricity supply and meet the expected steady demand growth. And, secondly, to make available the transmission capacity required to carry the new wind farms and combined cycles generation plants output. In addition, international connections have to be strengthened and the high-speed railway lines expansion properly supported. This ambitious plan is evidenced, in 2005, by the record investment of Euros 420 million in new electricity facilities. Investment that is 73% larger than the 2004 one.

The highly satisfactory operating efficiency and service quality indexes achieved year in year out by the facilities that make up the transmission grid rank Red Eléctrica with the best utilities worldwide as concerns a safe and reliable supply. As shown by the strong electricity demand growth during the last few years, when both summer and winter historical peaks have been recorded, the Utility's performance remained excellent throughout and electricity supply quality and continuity well assured.

In the international area, the Group's development through its subsidiaries in Bolivia and Peru, TDE and REDESUR is proceeding rather favourably. Besides quality and efficiency, both utilities show, too, excellent management results that maximise shareholders returns, as evidenced

by the dividends paid out. Our efforts to find business opportunities abroad that contribute value to the Group will be continued. But Red Eléctrica investments in Spain's transmission grid are the driving force behind our short and medium-term growth.

In the financial sphere, during 2005, several credit transactions have been completed to raise the funds required for transmission assets purchases. This opportunity was used to reschedule the debt, increase the amounts, extend maturity terms, improve hedging arrangements against interest rates increases and set up a rather competitive longer term financial structure. It must be pointed out here that the strong and sound financial position of the Group has been ratified, again, by the credit rating agencies decision to uphold the assigned ratings levels.

As regards Red Eléctrica shares listed in the stock exchange, their performance, during 2005, has been excellent and reached, at year's end, a 58.5% revaluation over the previous year. The stock quoted far above most of the stock exchange reference indexes. Also, the dividends paid out to shareholders increased 19%. This fact shows the Utility strives to offer returns that shareholders find increasingly attractive.

Concerning stock ownership, the withdrawal of Hidroeléctrica del Cantábrico, which owned 3%, and the 8.5% stake sold by SEPI have to be highlighted. Due to the mentioned transactions, Red Eléctrica free-float shares amount now to 70%. This favours trading volume and provides for higher securities liquidity.

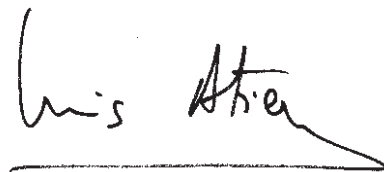
In Red Eléctrica, we are fully aware that our success issues from the highly qualified payroll and its large potential for development. This is why our human resources strategy is aimed to promote training programmes that encourage professional development and support know-how transfer. Special emphasis is made on implementing actions that help employees to share in the Corporate Project.

The management model based on excellence applied by the Group has been rewarded this year with the Príncipe Felipe Award to Entrepreneurial Excellence, in the Industrial Quality version. Also, the commitment to consolidate our Corporate Project through an ethic and accountable management approach to society, environment and people, led to the Group inclusion in the selective Dow Jones Stocks Sustainability Indexes. These acknowledgements endorse our corporate management model and rank the Utility with the European companies best rated for their corporate accountability. For all the mentioned reasons, Red Eléctrica is increasingly regarded as a model competitive Utility committed to both the environment and its stakeholders groups.

The strategic plans and economic targets issuing from this consolidated and efficient Corporate Scenario are firmly based and have led to a significant increase of the planned investments in transmission infrastructures over the initial amount. Besides, the situation allows for significant improvement in the operating margins and funds generation capacity, since the synergies issuing from integration of the purchased assets are used to advantage.

The mentioned funds generation combined with the sound financial position allowed to pay shareholders an attractive remuneration and increase the investment plan, while an efficient capital structure is kept in place. The above achievements are intended to render the best possible service to the electricity system and society at large, for these are the reasons why the Red Eléctrica Group exists.

Luis Atienza Serna
Chairman and CEO of Red Eléctrica de España

A handwritten signature in black ink, reading "Luis Atienza". The signature is written in a cursive style and is positioned above a horizontal line that extends across the width of the signature.



board of directors and senior management

31 · 12 · 2005

Executive President

Luis Atienza Serna

Proprietary Directors

Juan Gurbindo Gutiérrez (SEPI)

Manuel Alves Torres (SEPI)

Rafael Suñol Trepas (SEPI)

Independent Directors

Pedro Rivero Torre

Antonio Garamendi Lecanda

José Riva Francos

José Manuel Serra Peris

María de los Ángeles Amador Millán

Martín Gallego Málaga

Francisco Javier Salas Collantes

Non-voting Secretary

Rafael García de Diego Barber

Non-voting Deputy-Secretary

Fernando Frías Montejo

Senior Management

President and CEO

Luis Atienza Serna

General Manager of Transmission

Carlos Collantes Pérez-Ardá

General Manager of Operations

Alberto Carbajo Josa

General Manager of Administration and Finance

Esther Rituerto Martínez

main 2005 events

The Utility's Twentieth Anniversary

29th January 2005

For 20 years now, Red Eléctrica has ensured the Spanish electricity system overall operation. Since its inception, in 1985, its operations have been aimed to render the best possible quality and truly efficient service to society at large.

Purchase of transmission assets

16th February 2006

An agreement was reached by Red Eléctrica to purchase CVC's 75% stake in Redalta, the utility that controls the transmission assets owned, formerly, by Iberdrola. The Utility's position, as the sole transmission operator of the Spanish electricity system, has been strengthened by this purchase.

Stand against sex harassment

7th March 2005

The agreement reached by Red Eléctrica and the Utility-wide committee that shows the actions available to employees who might be subject to harassment, whether at home or on the job, due to their sex, has been ratified by the trade Unión General de Trabajadores (UGT).

Credit ratings

9th May 2005

The ratings assigned to Red Eléctrica by the credit rating agencies are confirmed. The A2 rating granted by Moody's is upheld for the third year in a row, while, the AA- for long and A-I+ for short-term are confirmed by Standard & Poor's. The outlook for both ratings is stable and stand amongst the highest awarded to European electrical utilities.

Albura sale

30th June 2005

The complete share capital of its subsidiary, Red Eléctrica Telecomunicaciones (Albura) was sold by Red Eléctrica to T-Online Internacional for Euros 61.5 million. Concurrently, a contract was subscribed by REE that assigns for an eleven years term and an annual Euros 5 million consideration the use of its fibre-optics system. The mentioned amount will be updated every year since it is pegged to the Consumer Prices Index.

New credit line

27th July 2005

A new credit line for Euros 900 million and a 7 years term has been signed by Red Eléctrica. The loan implies a substantial reduction from the previous funding cost and extends the maturity date by two years.

Migres Foundation agreement

16th August 2005

A cooperation agreement has been signed by the Migres Foundation and Red Eléctrica for implementing environment-related actions aimed to offset any effects issuing from the second submarine electricity exchange link between Spain and Morocco.

Dow Jones sustainability index

8th September 2005

Red Eléctrica is now included in the Dow Jones STOXX Sustainability Index, the European list of companies committed to sustainable development. The Index listing ranks the Utility amongst the best rated for their corporate accountability in the three following areas: financial, social and environmental.

Facilities located through satellite

27th September 2005

Worldwide, Red Eléctrica is the first electricity transmission utility that has geographically referenced its facilities to be located through satellite. The assets management process is improved by this project, which enhances the National Electricity System security.

SEPI sells 8.5% of Red Eléctrica

28th September 2005

An 8.5% of its stake in Red Eléctrica was sold by SEPI to UBS, the investment bank. In turn, the purchased shares are placed by the bank to different institutional investors. After this transaction, SEPI's stake in the Utility drops to 20%.

Bonds issuance

20th October 2005

Bonds for USD 500 million have been issued by Red Eléctrica for placement in the United States private market. The Utility diversifies, through this transaction, its funding, while maturity terms are extended to 30 years

Príncipe Felipe Award

27th October 2005

The Príncipe Felipe Award to Entrepreneurial Excellence, in the Industrial Quality version, that Red Eléctrica has received, not only acknowledges the Utility's products and services quality, but, underlines, too, its significant efforts to improve both the competitive edge and strengthen its relations with stakeholders groups.

Operators School

15th November 2005

The first course offered in Spain by Red Electrica's Operators School and the Higher Engineering School (ICAI) of the Comillas Pontifical University for training specialists in electrical systems operations has been completed. The Operations School is the only centre that provides this training.



14th of December 2005

His Majesty the King Don Juan Carlos I visits Red Eléctrica Main Offices as part of the events to celebrate the Utility's Twentieth Anniversary.



group operations

Red Eléctrica was set up to ensure the overall operation of the Spanish electricity system. For such purpose, the system real time operation is implemented to hold a continuous balance between the Country's power generation and consumption. The Utility operates, also, the high voltage electricity transmission system from generation plants to distribution centres. Red Eléctrica has been assigned, too, the Canary and Balearic Islands, Ceuta and Melilla electricity systems operation.

The Group engages abroad on transmission grids funding (through the Bolivian TDE and Peruvian REDESUR subsidiaries) and the specialised consulting services rendered to electricity systems in this sector.

electricity system operation

Peninsula-System Operation

As operator of the electricity system, Red Eléctrica is bound to ensure the supply continuity and reliability. To such purpose, the expected electricity demand is determined and electricity generation and transmission facilities are operated and supervised in a coordinated and real time basis to ensure that the scheduled output of electricity power plants is matched at all times to the consumers actual demand.

The transmission of electricity generated in neighbouring countries is also handled through the transnational interconnections.

During 2005, the main values achieved by the Peninsula Electricity System are shown below:

Demand

The annual electricity demand reached 246,826 GWh. This implies a 4.8% growth over the previous years. After adjustments for labour and temperature effects, demand growth, in 2005, stands at 3.8%.

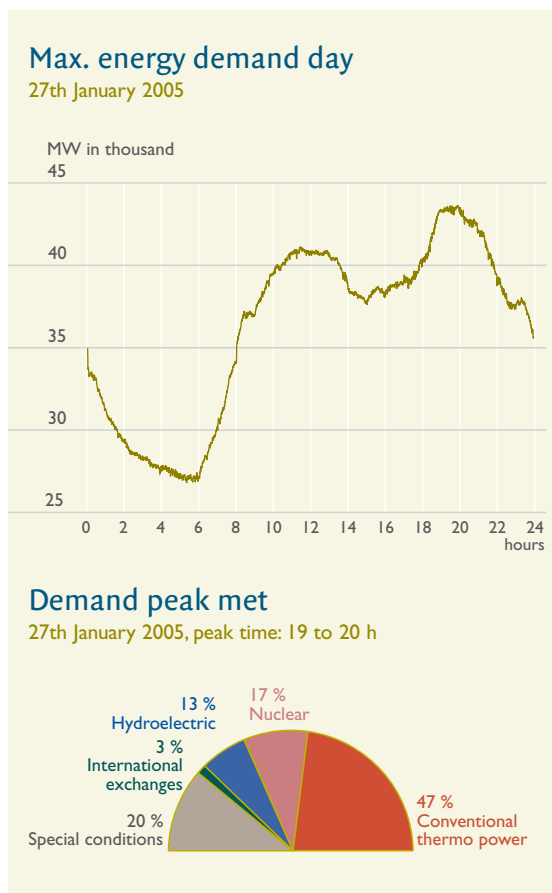
Monthly, daily and hourly electricity demand exceeded the respective historical peaks. During December, monthly demand reached 22,505 GWh. A maximum daily demand of 844 GWh was recorded on the 27th January, while on the same day, the 43,378 MW of mean maximum hourly power demand was also reached.

The historic summer peak values for both hourly mean power and daily energy demand, while stood at 38,542 MW and 770 GWh, respectively, were also recorded in July.

Generation

Installed power has increased by 5,255 MW, which implies a 7.7% over the 2004 amount. This increase is mainly due to the commissioning of eight new combined cycle power plants and increased number of wind farms.

The generation facilities structure has changed noticeably compared to that of 2004 due, on the one hand, to the heavy drought (the hydraulic impounded reserves were the second





lowest recorded since 1920) and reduced availability of nuclear power plants, while, on the other, new combined cycle power plants have been commissioned.

Gross generation from units operating under ordinary conditions reached 213,577 GWh, which implied a 3.5% increase over that of the previous year:

Generation from hydroelectric stations amounted to 19,647 GWh that shows a 34.0% increase from previous year. On the other hand, coal, gas and combined cycle generation units increased their outputs to 77,440 GWh,

10,027 GWh and 48,911 GWh, that imply a 1.4%, 30.3% and 68.8% increase over the previous year, respectively. Nuclear power plants generated 57,553 GWh, which shows a 9.5% decrease.

Electricity output from generation units operating under special conditions has continued its progressive increase and is currently meeting around 20% of the demand. A 40% of that power output was generated by wind farms.

International exchanges

For the second year in a row, a net export balance that reached 1,339 GWh has been achieved by the planned international exchanges. But the amount is still a 56% lower than that of 2004.

Planned imports reached 8,075 GWh, an amount that is quite close to that recorded for the previous year, as shown by the following break down: 7,306 GWh (90%), 718 GWh (9%) and 51 GWh (1%), through the interconnections to France, Portugal and Morocco, respectively.

Planned exports have amounted to 9,414 GWh, which is 16% less than that of the previous year. Main reductions have been noticed in exports through the interconnections to France (764 GWh) and Morocco (836 GWh), which have decrease 58% and 47%, respectively, compared to last year. But planned exports through the interconnection to Portugal have shown a slight increase (7,543 GWh on 2005, versus 7,460 GWh, in 2004).

Operations-related markets

Red Eléctrica duties, as the system operator, enclose the management of the operations markets, which are aimed to match the scheduled generation arising from the daily and intra-daily markets to meet properly the system's quality and reliability requirements. These markets supply the procedures required to solve technical restrictions, the allocation of auxiliary services and management of deviations.

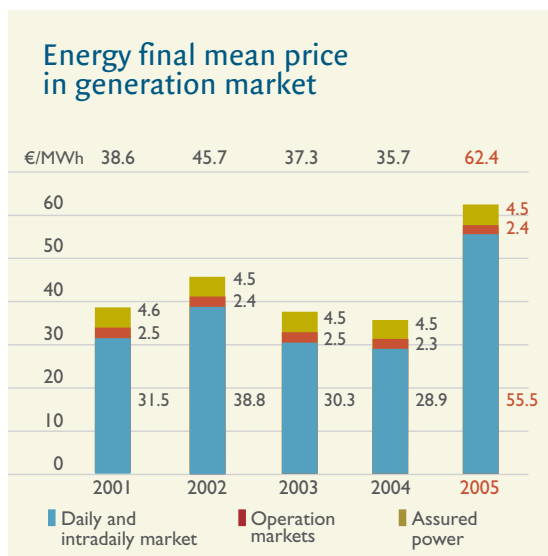
Electricity handled by all the mentioned markets amounted to 11,494 GWh, which is 5% of the total energy purchased from the generation market and 20.5% less than that recorded in 2004.

The decrease in scheduled energy related to solved technical restrictions, when compared to the basic operations schedule that stands at 3,093 GWh, or 48% less than the previous year, and that of scheduled energy for real time restrictions that drops 16% from 2004, clearly stand out.

Management of auxiliary services for secondary and tertiary regulation and scheduled energy for emergencies amounts to a total 7,050 GWh, or 4.7% over that of the previous year. From that total, 1,984 GWh are for secondary and 4,211 GWh for tertiary regulation. The mean power of the assigned regulation range was 1,208 MW at an average price of 30.61 €/MWh.

Demand matching is also ensured by Red Eléctrica through management of deviations to keep generation and consumption from being out of balance. During 2005, 1,350 GWh have been managed this way, a process that implied euros 27.8 million of total cost for the system.

The effect of those markets managed by Red Eléctrica on the energy final price that stood at 62.41 €/MWh, in 2005, was 2.38 €/MWh.



Off-the-Peninsula Electricity Systems

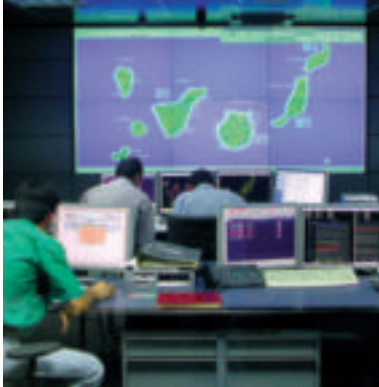
Since the 1st of July 2004, as established by the Royal Decree 1747/2003, Red Eléctrica has been appointed operator of the electricity systems in the Canary and Balearic Islands, Ceuta and Melilla. But these functions are not binding on the agents of the system until the regulations for the Royal Decree implementation are approved.

As established in the Electricity Industry Act of 1997, the access to those systems by other generating and trading utilities will be allowed by Red Eléctrica involvement, for it will prompt free competition with the attendant improvement of the off-the-Peninsula electricity systems economic efficiency.

In 2005, different actions that consolidate Red Eléctrica as the system operator in the mentioned locations have been completed.

- ▶ Operations are carried out through the control centres set up in the Balearic and Canary Islands. Those centres have been awarded the triple certificate that covers

“The financial efficiency of the off-the Peninsula systems will be enhanced by Red Eléctrica engagement as it will allow for new agents access and promote competition”



quality, the environment, and health and safety on the job, according to ISO 9001, ISO 14001 and OSHAS 18001.

- ▶ The Balearic and Canary Islands systems have been enclosed in the review of the transmission grid planning for 2005-20011.
- ▶ The elements that make up the electricity transmission grid in the Balearic and Canary Islands have been defined by the respective Autonomous Governments.
- ▶ Feasibility studies for future interconnection of the Balearic Islands electricity system to that of the Peninsula have been carried out.
- ▶ Meeting venues where the operations of agents active in the off-the-Peninsula and Islands systems will be described and studied have been set up.

Red Electrica’s basic operations in the off-the-Peninsula systems

Based on the operating model of those systems, the following actions are carried out by Red Eléctrica:

- ▶ Recibe de los productores la información necesaria para ejecutar el programa de generación (disponibilidad de grupos, reservas de combustible, etc), así como las previsiones de demanda de los distribuidores, comercializadores y consumidores.
- ▶ Based on that information and its own demand forecasts:
 - ▶ The hourly operation of generation units required to meet the demand is scheduled based on the variable generation costs of generation units.
 - ▶ The system’s technical restrictions are studied and duly managed. Then, the final generation schedule is drafted.
- ▶ Later on, the electricity to be generated by each agent as well as the production costs are published. This allows implementing the financial settlements that accrue to the respective system's agents.
- ▶ Utility schedules, too, the transmission grid development, management of access to the grid, and the proper continued operation of the generation-transmission system.



transmission grid management

Grid planning

Throughout 2005, Red Eléctrica, in its capacity as the system operator and transmission grid manager, has cooperated with the Ministry of Industry, Tourism and Trade to review the transmission grid planning described in *“Planning of the Electricity and Gas Industries. Transmission Grids Development 2002-2011”*.

The reviewed plan for the 2005-2011 period, where the views of all the duly entitled electricity system agents are shown, describes a rather large construction schedule of new transmission facilities that is aimed to achieve two purposes: ensure the electricity supply quality and reliability, and provide the capacity required for transmission of the planned future generation output.

Same as for the Peninsula system, Red Eléctrica has cooperated in the proposal to review the planned transmission grid for the Balearic and Canary Islands electricity systems. In these systems, the following scheduled actions for the grid development must be highlighted:

- ▶ The electricity link between Mallorca and Ibiza (which implies the interconnection of all the Balearic Islands electricity systems).
- ▶ The DC link between Mallorca and the Peninsula, and the
- ▶ 220 KV grids expansion in the Gran Canaria and Tenerife islands.

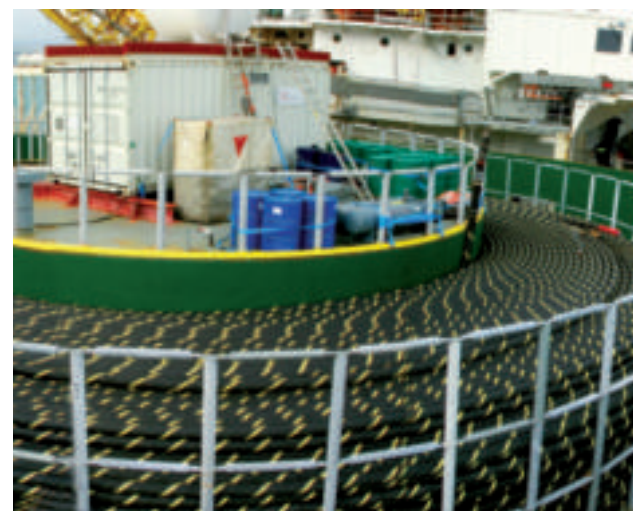
Projected electricity demand and how it will be met

Every year, both long and medium term electricity demand projections and how they will be met are drafted by Red Eléctrica.

The report on the Peninsula electricity demand projections for the 2005-2016 period shows the Peninsula annual electricity demand estimates, the hourly peak power demands, both during summer and winter; and the expected demand broken down by Autonomous Communities during the two first years of the projected horizon. Besides the mentioned information, the minimum hourly mean power demand (valley) and the monotonous load curve are also enclosed.



“A significant construction schedule for new facilities is described in the 2005-2011 development plan aimed to ensure the electricity supply reliability”



On the one hand, the new generation equipment required by the system are evaluated by the report that shows projections for electricity demand to be met in the Peninsula based on the 2005-2015 horizon. A number of assumptions related to demand growth, generation equipment evolution, both under ordinary or special operating conditions, and the units availability are used to perform the mentioned analysis. The planned inroads achieved by renewable energies, as shown in the 2005-2010 plan for renewable energies promotion, have been taken also into account by the already mentioned report.

On the other hand, Red Eléctrica, as operator of the Islands and off-the-Peninsula electricity systems, has drafted both demand projections and peak power demand values during 2005 and an estimate of the generation equipment required by those systems.

Studies for strengthening transnational interconnections

Portugal interconnection

Studies carried out jointly with Red Eléctrica Nacional (REN) have been completed by Red Eléctrica to define a new 400 kV interconnection line between both Countries laid along the Douro River zone. Based on the mentioned studies, the new line must be built between the existing Aldeadávila substation, in Spain, and the new Douro International Substation, in Portugal. Both technical and environmental issues have been taken into account by the performed studies.

France interconnection

The studies carried out by Red Eléctrica and Réseau de Transport d'Electricité (RTE) are going forward to define a transnational corridor for the new interconnection line in the Eastern section of the Pyrenees. The line will link up the Bascanó substation (Spain) to the Baixas (France) one.

This line will not only increase the interconnection capacity that ensures the reliability and quality of the electricity supply in the Girona area, but provides, also, support for the future Barcelona to Perpignan high-speed railway line.

Morocco interconnection

The works have continued, in 2005, to strengthen the interconnection with Morocco by laying a second submarine cable in the Straight of Gibraltar. Commissioning of this facility is planned for the spring of 2006.



Access and connection to the grid

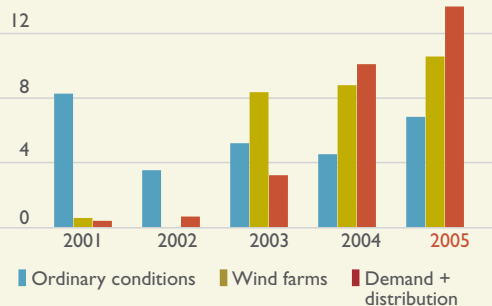
During 2005, Red Eléctrica has continued to manage both access and connection to the transmission grids. It receives, studies and answers, too, the different agents requests, which plan the addition of new facilities to the National Electricity System.

The current requests for access to the transmission grid that have been answered by Red Eléctrica, during the 2001 to 2005 period, are shown in the graph broken down by the type of facility for which connection to the grid is requested:

- ▶ Generation under ordinary operating conditions, mainly, by combined cycle plants using natural gas.
- ▶ Wind farms output.
- ▶ Demand, mainly to support the distribution grid, and power supplied directly to consumers and, more specially, to high speed railway lines.

Request to access the transmission grid

MW in thousand
16



“Access of third parties to the grid is ensured by Red Eléctrica on an equal footing by all agents”.

Transmission grid development

The Utility's size has changed significantly due to the transmission assets purchased from other utilities during the last few years. The purchase, in 2005, by Red Eléctrica of the remaining 75% of Redalta's assets, the utility that owned Iberdrola's high voltage facilities, besides the Viesgo assets purchase, are 2005 crowning events, since, now, Red Eléctrica owns virtually the complete high voltage transmission grid. In barely four years, the Utility has almost increased three-fold its transmission assets.

Transmission grid owned by Red Eléctrica.

	2001	2002	2003	2004	2005*
Circuit in kilometres	19,240	27,001	27,550	27,836	33,096
400 kV	14,838	15,782	16,308	16,548	16,808
220 kV and less	4,402	11,219	11,243	11,288	16,288
Number of busbar connections	719	1,740	1,813	1,935	2,746
400 kV	523	638	683	740	881
220 kV and less	196	1,102	1,130	1,195	1,865
Transforming capacity (MVA)	20,276	27,516	32,166	36,153	55,222

*Redalta and Viesgo transmission assets are enclosed

As part of the grid expansion and development plans, 38 new kilometres of high voltage line and 104 busbar connections at substations as well as 7 new transformers that contribute 3,600 MVA capacity have been commissioned during 2005. The facilities commissioned are listed below.

Substation	Busbar	
	400 kV	220 kV
Alcocero de Mola		4
Aljarafe		4
Almaraz		1
Alvarado		1
Aragón	2	
Can Barba	4	
Caparacena	3	2
Cartuja		1
Castejón	3	
Cervelló		3
Chantada		4
Espluga	7	
Fuenlabrada		8
Fuentes de la Alcarria	1	
Guadame	1	2
Guillena	1	1
Lora	5	
Magallón		2
Nueva Escombreras	9	
Olivares		3
Olmedilla	2	
Polígono		3
Puerto de la Cruz	1	
Puigpelat		3
Rubio		3
Sentmenat	1	
Serna	1	
Subirats		3
Torres del Segre		2
Trillo	1	
Vall d'Uxo		6
Villafranca del Penedés		3
Villanueva del Rey		2
Blindada móvil		1
	42	62

Lines 400 kV	km of circuits
E/S La Espluga - L/Ascó - Begues	2.9
E/S La Lora - L/Barcina - Herrera	1.6
E/S Olmedo - L/Mudarra - Lastras	0.6
	5.1

Lines 200 kV	km of circuits
E/S Rubió - Pierola - Pobla	0.4
E/S Chantada L/Belesar - Castrelo	4.6
E/S Jundiz L/Mercedes - Puentelarrá	0.2
E/S Vall d'Uxó L/La Plana - Sagunto	0.8
E/S Pinto L/Aceca - Villaverde	0.5
E/S Villafranca del Penedés L/Constantí - Viladecans	0.2
E/S Polígono L/Los Ramos -Tajo I	8.7
E/S Aljarafe L/Quintos - Santiponce	0.9
E/S Olivares L/Atarfe - Guadame	16.4
E/S Riera L/Sentmenat - Sant Fost	0.5
E/S Torres del Segre	0.1
	33.3

Capacity increase	MVA
369 km de líneas de 400 kV	2,235
88 km de líneas de 220 kV	1,147

Transformers	MVA
El Cereal	600
Torremendo 1	450
Torremendo 2	450
Benejama	450
Rocamora	450
Trives	600
Santa Coloma	600
	3,600



Facilities construction

Northern Region

Engineering and construction works in the Northern alignment corridor are continuing to increase the transmission capacity and will favour electricity exports from Asturias, Cantabria, Basque Country and Navarre.

Aragon and Catalonia

A significant development of the transmission grid is underway in this area to supply the Lérida-Barcelona-French Border high speed railway line and make available new electricity interconnections between Spain and France that will also carry wind farms output set up along the alignment.

Central Zone

Engineering and construction works of electricity transmission lines that link up Galicia, Castile and León and Madrid Autonomous Communities are in progress. Works to strengthen the Madrid ring line and supply power to the high-speed railway line are underway, too. The works to develop the Transmanchego lines corridor are also continued.

Galicia

The engineering works for the lines alignment to export energy to Asturias and the Central Zone of the Peninsula are going forward.

Extremadura

The preliminary engineering works to strengthen the Extremadura-Andalucía transmission lines alignment are in progress.

Andalucía

Besides the overall strengthening of the transmission grid, the works required for power supply to the Córdoba-Málaga high-speed railway line is continuing.

Eastern Seaboard

Engineering works for facilities that will carry the wind farms output and works to strengthen the electricity supply to Murcia and the coastal area in general are in progress. The preliminary engineering studies for the future Peninsula-Balearic Islands interconnection are continued.



Targets of Red Eléctrica investments plan:

- ▶ Supply sufficient capacity and flexibility to the system for assured electricity supply.
- ▶ Carry the electricity generated by combined cycle plants and wind farms.
- ▶ Support the high-speed railway lines network expansion.
- ▶ Strengthen international interconnections.

“Red Eléctrica has invested, in 2005, Euros 420 million to expand and improve the transmission grid. This is 73% larger than the previous year investment”

Lines construction in progress

31-12-2005

400 kV	Circuits in Kilometres
Pamplona-Magallón Lines	120
North Eastern Lines	150
North Western Lines	60
International connections	25
Wind farms connections	85
Eastern Zone lines	80
Murcia Power supply lines	196
West-Centre lines	150
Asturias-Galicia Lines	50
Power supply to Catalonia and for high-speed railway lines expansion	10
Conexión ciclos combinados	140
Aumento de capacidad	350
Total 1,416	

220 kV	
Pamplona ring line	15
Capacity increase	160
Total 175	



Substations construction in progress

31-12-2005

400 kV	Busbar connections			
	Transmission	Access	Transformer	React./Condensers
Pamplona-Magallón Lines	5		1 x 400/220 kV, 600 MVA	
North Eastern Lines	3		1 x 400/220 kV, 600 MVA	
International connections	8			
Wind farms connections	12	2		1 x 150 MVAr 2 x 100 MVAr
West-Centre lines	6	3	2 x 400/220 kV, 600 MVA	
Eastern Zone lines	14	3	2 x 400/220 kV, 450 MVA 1 x 400/220 kV, 600 MVA	
Asturias-Galicia Lines	4	3	1 x 400/220 kV, 600 MVA	
Murcia Power supply lines	17	6	2 x 400/220 kV, 600 MVA	
Power supply to Catalonia and for high-speed railway lines expansion	10	2	1 x 400/220 kV, 600 MVA	
Combined cycle connection	13	4	1 x 400/220 kV, 600 MVA	
Other	6	5	1 x 400/220 kV, 450 MVA	2 x 150 MVAr
Total 98		28		
220 kV				
Other substations	17	9		2 x 100 MVAr
Total 17		9		

Facilities maintenance

Lines maintenance

All the scheduled lines maintenance inspections have been carried out in 2005. DVD recording equipment was used mainly for the inspections and helicopters for transport. All the lines purchased from other utilities have been also thermo graphed to appraise the overall condition of these facilities.

A large number of live-wire maintenance works have been completed by Red Eléctrica to improve both the grid availability and service quality. In this connection, the works implemented to lay out fiber-optic cable, clean and replace isolators, and fit in birds-guards must be highlighted.

On the other hand, rust proofing was applied to many metallic structures to protect some 98,000 m². Significant works have been carried out also to trim trees and clear the lines right-of-ways. The mentioned works extended over 12,000,000 m² of land surface.

Substations maintenance

As part of the power transformers and reactances maintenance plan, 441 oil tests and 22 insulation values (power factor) have been measured and the windings condition in 22 power units has been checked.

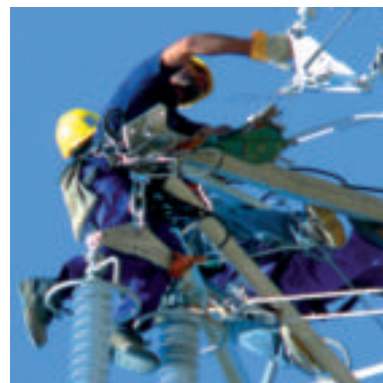
Concerning instruments transformers, the use of technical methods to measure partial loss of load in 93 current transformers, metered values to check the accuracy of 184 voltage transformers, oil tests of 120 current transformers, and thermo-grams of all instrument transformers that have been fitted in were completed as required by the maintenance plan.

As for high voltage circuit-breakers maintenance, remote troubleshooting has been again applied, maintenance actions optimised while maximum spacing of maintenance cycles has been applied to reduce downtime that keeps equipment out of service. This year, 662 values have been measured to appraise the condition of 130 circuit-breakers.

Maintenance of protection systems has been implemented as planned. Metering equipment fitted at interconnections has been checked as established in the Metering Points Regulations. All the protection systems fitted in the transmission grid have operated correctly. Generally speaking, the efficiency rate of the protections applied to remove faults and distur-



“Red Eléctrica continued leadership is based on its electric facilities operating efficiency and service quality”.



bances from the transmission grid has reached 98.93%.The remote control equipment availability stands at 99.99%.

Red Eléctrica transmission grid performance

The excellent quality of the services rendered by the transmission grid equipment and systems is especially dependent on the strict enforcement of quality criteria during maintenance works performance, the use of predictive procedures and live-wire work implementation.

The transmission grid performance has been again this year highly satisfactory:

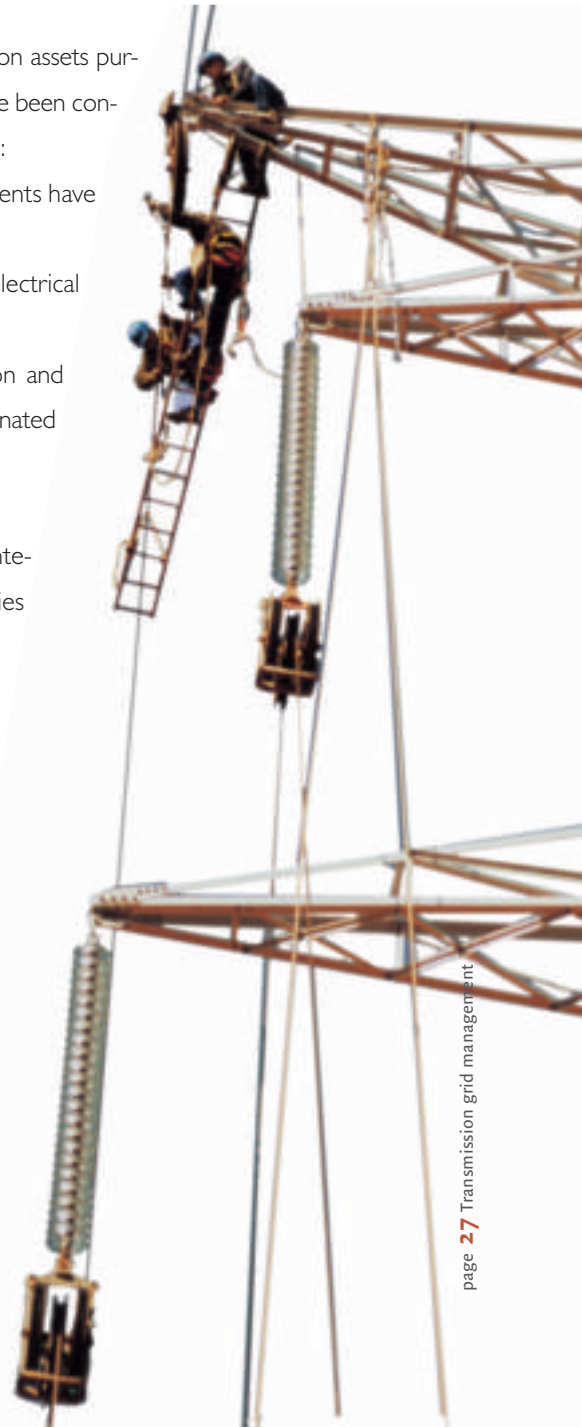
- ▶ The grid availability rate stands at 98.28% (the reference value is 97%).
- ▶ Energy that was not supplied to the system, due to incidents in the grid, stands at 506 MWh.
- ▶ Mean interruption time was 1,078 minutes (reference value is 15 minutes).

Assets Integration Project (AIP)

During 2005, actions aimed to integrate the transmission assets purchased from other utilities during the last few years have been continued. Besides other, the following must be highlighted:

- ▶ Legal, technical and proprietary supporting documents have been received and filed.
- ▶ New structures have been built in different electrical substations.
- ▶ The procedures required for the facilities operation and maintenance has been established through a coordinated effort with the utilities.

These actions are aimed to ensure that maintenance of all the facilities purchased from other utilities can be taken over during 2006.



international business

International investments of the Red Eléctrica Group in transmission infrastructures are channelled through Red Eléctrica Internacional that renders both consulting and technical assistance to clients abroad. The last mentioned Company is also expected to ensure the optimal use of Red Eléctrica's experience and resources for management of electricity systems and grids abroad and finding new business opportunities.

Investments in transmission infrastructures

Red Eléctrica International investment operations are implemented through both its Peruvian subsidiary, Red Eléctrica del Sur (REDESUR), where it holds a 30% stake and acts as the strategic operator; and the Bolivian subsidiary, Transportadora de Electricidad (TDE), where it holds a 99.94% interest.

During 2005, **the Peruvian utility, REDESUR**, has remained the service quality leader compared to other transmission utilities in Peru, since an outages-free electricity supply was achieved. This shows the high efficiency standards reached by the Utility in its facilities operation and maintenance.

In its dealings with business agents, REDESUR has actively engaged with the Peruvian Government, Regulatory Agencies and other transmission utilities in the design of a regulatory framework that favours the transmission grid development and contributes to the economic development of Peru.

The excellent management results that have been achieved allowed payment of dividends amounting to US\$ 0.8 million. This shows the utility wants to achieve value added for the shareholders.

In line with its socially accountable commitment to the surrounding context, REDESUR continues to be highly engaged in social activities as shown by the efforts to improve school conditions in worst-off zones, the cooperation agreements signed with universities and the environment protection through the sustainable development of its facilities.

In its turn, **the Bolivian utility, TDE**, has worked hard to become the reference electricity transmission utility in Bolivia. Since 2004, the utility is implementing a rather large plan for new facilities construction that have been commissioned this year.

Additionally, in 2005, TDE has been authorized to start the Carrasco-Cochabamba transmission line construction and to implement the SCADA control system renewal.



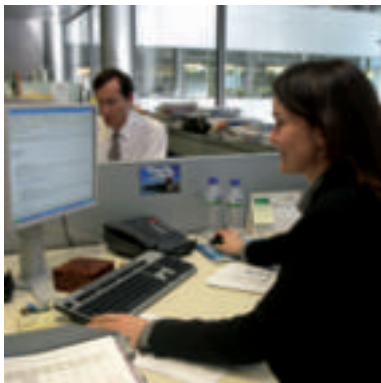
“Dividends have been paid to TDE and REDESUR, shareholders since the subsidiaries have achieved excellent financial results”

Both projects are of strategic significance for the Country since, the first one, implements the necessary strengthening of the transmission grid, while the second ensures the Bolivian Electricity System control and operation.

The utility has paid out, in 2005, dividends that amount to US \$ 2.67 million, since it aims to offer maximum yield for shareholders.

As regards the rendered service quality, the utility has again achieved the high availability ratios the grid has shown during the last few years. In 2005, the transmission grid availability has reached 99.80%.

As for the social accountability commitment, the utility has carried out different actions in the educational field. Besides other, the efforts intended to teach in rural areas, how electricity should be used, visits by students to the utility own Electricity Interactive Centre and the mutual cooperation agreement signed with the Bolivian Catholic University must be highlighted.



Technical consulting and assistance

Red Eléctrica Internacional is increasingly active in foreign markets through its engagement in different international consulting projects, which are related to the Utility own operations, such as: management of electricity transmission grids and electricity systems operation. The following technical and business consulting projects have been completed in 2005:

- ▶ **Serbia and Montenegro.** Purchase of adequate software and hardware for electricity planning, control and coordination of the Balkans area with other European countries.
- ▶ **Italy.** Supply of equipment and training for live wire work performed using helicopters.
- ▶ **Morocco.** Design of towers for 60 kV single and double circuit lines.
- ▶ **Libya.** Study of stable operation during minor disturbances of the electricity systems in Libya, Egypt, Jordan, Siria and Lebanon.
- ▶ **Libya.** Study of critical timing to remove faults in the transmission system, philosophy review and system protections adjustments.
- ▶ **Algeria.** Training of operators for the GRT-Sonelgaz Transport utility.
- ▶ **Peru.** Study of the current regulations model to draw up and submit changes that could be required to ensure reliability and quality of the long-term electricity supply in this country.



our people

The priority concerns of Red Eléctrica in the area of human resources strategy are targeted in setting up an organisation model aimed to enhance in-house efficiency, promote investments in training programmes that contribute to professional development and the transfer of know-how, as well as carrying out in-house communication efforts that foster the employee's commitment to the business project.

A shared corporate project

Red Eléctrica is fully aware that its success is due to the qualified payroll and its high potential for development. Employees targeted on the corporate strategies implementation and achieving its targets.

In this connection, the personnel management plans are based on the continuous improvement of employee's performance through the potential promotion and transfer of know-how, which, in turn, contributes to their work being properly acknowledged. The actions to farm out functions, the promotion of teamwork and the professional development of the Group employees are the basic guidelines of the Utility's Human Resources Policy.

The employees involvement in the Corporate Project is achieved through the implemented plans: 85% of the payroll claims they are proud to be employed in Red Eléctrica and the personnel turnover is one of the lowest in recent years (1.14%).

Payroll continues to grow and close to 28% of Red Eléctrica employees have joined the Utility during the last five years. This growth is mainly due to the purchase of transmission assets and the new duties that have been taken over in the off-the-Peninsula electricity systems.

In 2005, Red Eléctrica payroll totalled 1,254 employees and 1,401 in the Group as a whole. The net growth amounted to 109 newly hired employees.

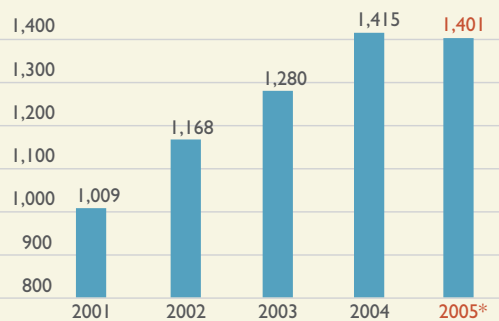
Organisation targeted on excellence

Red Eléctrica's organization model is aimed to optimise the available resources, simplify structures and take advantage of all possible synergies within the Group to improve both business returns and efficiency, free of any negative effects on the quality all the business processes have achieved.



Group payroll trend

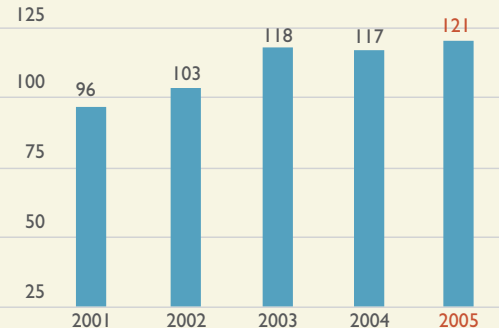
number of employees



*Shows the Albura sale effects

Nett profit per employee*

euros in thousand



*Based on Red Eléctrica payroll

In order to achieve higher organization efficiency levels, during 2005:

- ▶ The territorial structure of operations and maintenance has been revamped. This implied, sometimes, an increased employees turnover in those units, and
- ▶ Some organisation units have been readjusted. Payroll has been reduced in supporting areas, while efforts were increased at the business end.

Red Eléctrica bets on hiring professionals that fit the personnel profile of a modern, dynamic and resourceful Utility. With that in mind, the Utility looks for multivalent young people with initiative, who like teamwork and share the Corporate Project's philosophy. An attractive professional career is open to those that meet the requirements.

On the other hand, through agreements with Engineering Schools and Universities, a large number of trainees and graduates in subsidized jobs have joined the payroll.



“Red Eléctrica success is based on its highly qualified payroll that has high potential for development and is actively involved in the Corporate Project”



The new employees are assigned to a programme for their integration in the corporate culture. Two classes have already graduated through this initiative that starts by the welcome opening meeting and runs for 36 months. During this time, the new professionals attend meetings on specific subjects and other to learn about the Corporate Project, for actual implementation in their daily work.

The scheduled activities reached last year some 7,500 hours, which enclose meetings to inform about the different organization units in the Utility and courses to enhance communication skills.

Professional careers

One of the basic aims of the Human Resources Management Policy applied by Red Eléctrica is the promotion of talent through professional development.

The training plan, which is updated every year; based on the needs found by a survey of the Utility's different business processes provides language, quality and other technical training courses. In 2005, a total of 82,506 training hours were delivered, or almost 68 hours per employee in the average.

The professional development of employees is materialized also through specific programs fitted to

each employee profile. Programmes addressed to the executive team or the technical staff with a management profile and employees in management-support positions are delivered, which are aimed specifically to their needs.

Through these training and professional development programmes, 7 employees have been promoted to executive positions in 2005.

School for Operation of the electricity system

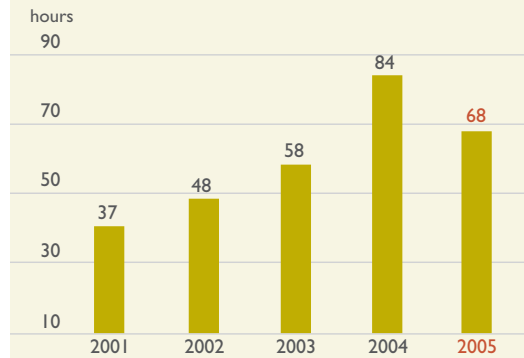
Red Eléctrica is fully aware that know-how transfer to employees is a basic need for the payroll development and continuous updating of specialized knowledge in our business. For this reason, the School for Operation of the electricity system was established in 2004. The School provides a training syllabus that fits the requirements of new operators and to update the skills of those more experienced.

The School for Operation has available the latest technological breakthroughs and operates a training simulator; for complex events simulation, as it replicates on real time the power electricity and energy management systems.

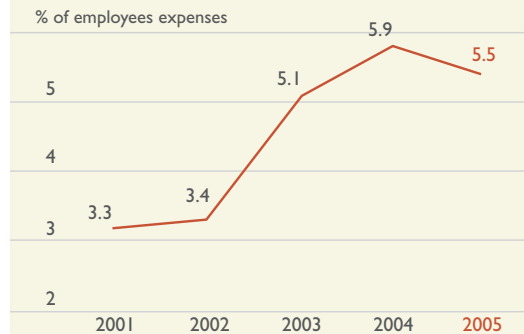
Lecture room courses, laboratory practices, visits to facilities, workshops, training periods on the simulator and virtual training are combined in this educational process.

The first specialists class for electric systems operation graduated in 2005. The course is delivered jointly with the Higher Technical School of Engineering (ICAI) of the Comillas Pontifical University. This is the first training course of this type available in Spain.

Training hours per employee



Investment in training





“Red Electrica’s School for Operation is the only one that provides specialized training and skills updating of electricity system operators”

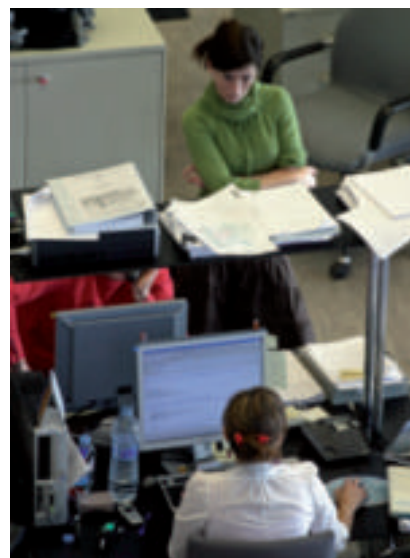
Promotion of in-house communication

Promotion of in-house communication is one of the main guidelines in the Utility Strategic Plan. This is ambitious in-house communication plan for prompting employees’ involvement to share in the Corporate Project that was completed in 2005. The events for the Utility’s 20th Anniversary celebration have been emphasised by the mentioned Plan.

The launching of work groups in eight of the organisation units (in-house communication observatories), which are intended to ensure tracking of the in-house communication plan implementation in the work site, is one of the more outstanding actions that have been implemented.

Other communication actions have been carried out, too, that explain the Utility’s strategic guidelines through meetings between the Management Committee and technical experts from different areas (the so-called Grid Breakfasts), which are aimed to promote employees commitment to the Corporate Project.

The actions implemented in bottom-up, downwards and horizontal communication areas reach in total 15,743 hours per employee and over 13,000 hours have been devoted to attend corporate events. This implies an almost three-fold increase in the number of employees attending those activities.





corporate excellence

The management model based on excellence developed by Red Eléctrica has meant, on the one hand, its worldwide consolidation as a reference Utility for grids and electricity systems efficient management and, on the other, an enhanced corporate standing and image.

Red Eléctrica is increasingly regarded as a modern, competitive, environmentally concerned utility, bent on meeting the needs of each and every stakeholders groups.

excellence in management

The Príncipe Felipe Award to Entrepreneurial Excellence, in its Industrial Quality version, won by Red Eléctrica is a fitting reward to the efforts devoted for over five years to ensure Excellence in Management. This is the tenth edition of the more prestigious award granted in Spain to Entrepreneurial Excellence and acknowledges the Utility's efforts to improve its competitive edge and strengthen relations with stakeholders groups.

Again, this year, Red Eléctrica has been awarded, for the second year in a row, **the Golden Seal Rating (+ 500 points)** that the Excellence in Management Club grants on behalf of the European Foundation for Quality Management (EFQM), as its representative in Spain. The EFQM Model is applied by Red Eléctrica for corporate management since 1999

Concerning management systems implementation, the Utility has been granted, too, the joint triple certificate for quality, environment and health and safety on the job, as required by the ISO 9001, ISO 14001 and OHSAS 18001 specifications. The certificate is related to the off-the-Peninsula electricity systems operation that Red Eléctrica carries out since the 1st of July 2004. The Utility's qualification and capacity to manage the new electricity systems operations are evidenced by the mentioned certificate.

The decision to have in place a corporate accountability system aimed to sustainable development, added to the actions intended to meet stakeholders groups demands, the respect of employees interests and their integration, as well as the value added that benefits the context where the Utility interacts must be highlighted as some of the guidelines that support the Excellence in Corporate Management model.

This commitment to strengthen the Corporate Project in tune with an ethical management that takes into account society at large, the environment and population has led to the Utility inclusion for the first time in the **Dow Jones STOXX Sustainability Indexes (DJSI)**. It implies to be enclosed in the 20% of the European utilities best ranked from the corporate accountability standpoint.

In 2005, Red Eléctrica has been granted, too, for its overall operations **the Social Accountability Certificate (SA8000)**, an international standard for social accountability that ensures a corporate commitment to human rights respect and an ethical approach to



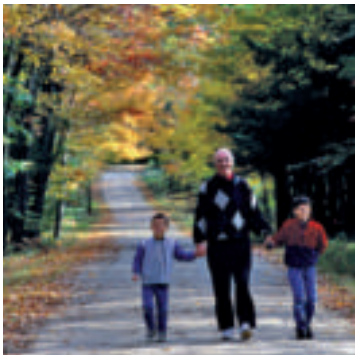
employees' demands. The Utility is one of the first Spanish companies and the only one in the energy industry that has been awarded this certificate.

On the other hand, the system to manage relations with stakeholders has been redesigned by Red Eléctrica. Based on a survey of the organisation processes and operations, as well as how they interact in the context:

- ▶ The Utility's stakeholders groups have been identified.
- ▶ The best fitted method to identify needs, expectations and requirements has been defined, and
- ▶ The frequency for data measuring and to design improvement plans has been established.

During the survey, data about the following stakeholders groups: shareholders and investors, social agents, communication media and suppliers were compiled.

committed to the environment



The challenge of making compatible the sustainable development of its electricity infrastructures with an environment friendly protective policy is duly met by Red Eléctrica. Each and every project is implemented to meet the more strict environmental requirements, while the widest possible social acceptance is sought for their integration in the community.

Environmental Actions

Besides the environmental impact surveys implemented for all new facilities projects and regardless of whether they are or not required to submit an environmental impact statement, a large number of environment-friendly actions are implemented by Red Eléctrica to avoid or reduce its own facilities interaction with the surrounding context, as the principles of its environmental policy demand.

While environmental impact surveys are implemented, enquiries are submitted to the respective environmental agencies and the option for each project is mutually agreed that ensures the least possible impact. This procedure has secured positive environmental impact statements granted by the Ministry of the Environment, during 2005, to set up 9 facilities. Also, the respective summary reports have been submitted to evaluate the environmental impacts issuing from 15 additional projects.

Environmental surveys of different construction, renewal or improvement works, which are in progress for different facilities have been implemented, and the required preventive and corrective steps applied, while areas for hazardous wastes storage and actions to ensure proper handling of those issuing from the mentioned works have been carried out.

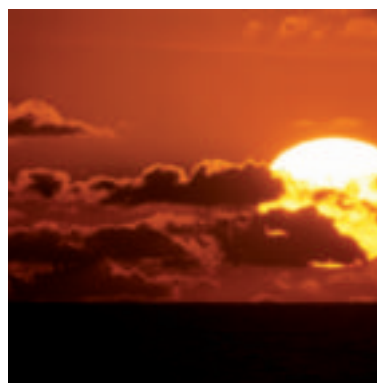
Environmental studies and research projects

Red Eléctrica is actively and continuously engaged in different research projects targeted on birds' protection. Besides other, the following must be highlighted:

- ▶ Study about the electricity transmission lines interaction with steppe birds and possible ways to manage these birds habitat. The Higher Scientific Research Council (CSIC) cooperation and assistance supplied by the Doñana Biological Station and the Natural Sciences Museum of Madrid researches was available for the study.
- ▶ Study about the effective performance and working life of spiral birds-guards fitted in electricity transmission lines. The study is currently implemented in cooperation with the Doñana Biological Station (CSIC). During 2005, a follow up was carried out on 12 kilometres of lines fitted with the new model of birds-guards spirals.
- ▶ Project implemented in cooperation with the Wildlife Section of the Territorial Service in the Environment Department of the Castille and León Autonomous Government. The project is intended to protect the common peregrine falcon (*Falco peregrinus*) in Valladolid Province.
- ▶ A study has been also completed on electric substations where kestrels gather. The study was performed through a cooperation agreement signed with the Doñana Biological Station (CSIC). An unknown situation was disclosed by this study. The hundreds of kestrels (*Falco naumanni*) found in electricity transmission substations located in Navarre and Aragon. A triptych that describes this bird has been drafted to publish the mentioned research findings.

Concerning emissions control, the following research studies are in progress:

- ▶ Project to study currents induced in the human body by industrial frequency electromagnetic fields. The study is carried out in cooperation with both UNESA and the "Salvador Velayos" Applied Magnetism Institute (part of the Madrid Complutense University and the Higher Research Council). The project is scheduled to last two and a half years and intended to develop a model for computing the currents induced in the human body by industrial frequency electromagnetic fields and carry out actual tests.





“The prevention or reduction of negative interactions between electricity facilities and birds wildlife is an environmental priority for Red Eléctrica”



- ▶ Project to develop a software application and implementation protocol to carry out studies on lighting pollution.
- ▶ Study of a tool to determine noise issuing from electrical facilities. The main initial sources have been determined during this year and a work methodology to study the acoustic impact has been established.

Prevention and reduction of environmental effects

The environmental survey of virtually all the substations purchased from other utilities was completed during 2005. The survey was intended to find out their environmental condition and state the actions (both preventive or corrective steps) required to refit them. A social-environmental inventory of the purchased lines has been also implemented where all the natural environments listed in the Natura Network and urban areas the transmission lines run across have been recorded.

Concerning actions for birds wildlife protection, the planned fitting of birds-guards in transmission lines has been continued as provided for in the cooperation agreements signed with different Government Agencies.

- ▶ Aragón Autonomous Government. Through this agreement, Red Eléctrica is committed to fit birds-guards in all the electricity transmission lines running through the Aragón Autonomous Community, if a hazard for birds wildlife is implied.
- ▶ Agreement in effect with the Industry and Environment Department of the Murcia Autonomous Government. This agreement is intended to protect and restore the *Hieraaetus fasciatus* – eagles population. This Life-Nature project is enclosed in the “Almenara – Murcia – *Hieraaetus fasciatus* preservation” plan.
- ▶ Agriculture and Environment Department of the Extremadura Autonomous Government. Those transmission lines stretches, which imply greater hazards for birds, have been studied and birds-guards spirals fitted in.

Besides the actions provided in the mentioned agreements, those line spans, are possibly hazardous, have been fitted with birds-guards spirals in Andalucía, Extremadura and Murcia. The effectiveness of systems used to discourage nesting by white storks (*Ciconia ciconia*) on electricity transmission lines towers located in Castille-La Mancha, Castille and León, Extremadura, Galicia and Madrid has been followed up and fitting in

new discouraging devices was deemed necessary since the storks population shows a significant increase.

Concerning actions to prevent facilities pollution, 100% of the expansion reservoirs in power equipment have been inspected and preventive steps that should be implemented next year have been proposed.

Finally, the plan for measuring electrical and magnetic fields as well as noise levels that was started the previous year has been continued in 2005. Operations this year were intended to appraise the workmen exposure level. The electric and magnetic field levels measured are quite lower than the threshold values stated in the European Directive that regulates workmen exposure to electromagnetic fields in their usual work locations, such as compound bays, huts and offices. As for audible noises, the limit values established in the respective legislation were not exceeded.

Actions to release environmental information

During 2005, the Utility has attended both national and international meetings of different committees and work groups made up by technical staff and experts. Besides other, the following can be highlighted: The CIGRÉ Study Committee on “Environmental performance of electricity systems” and AENOR Subcommittee on “Environmental management systems”, as well as the work groups listed below:

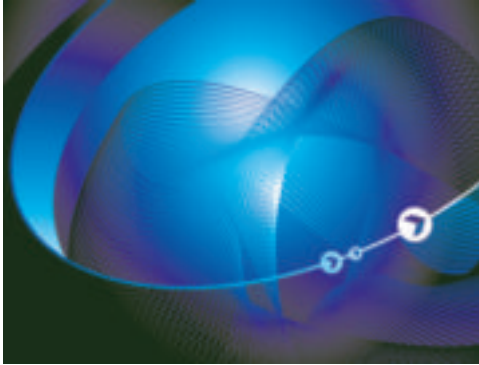
- ▶ “Environmental costs appraisal” of AENOR
- ▶ “Electromagnetic fields” of UNESA
- ▶ “Environment and society” of EURELECTRIC
- ▶ “Utilities practices in sustainable development” and “Sustainable development performance indicators” of CIGRE.
- ▶ “Noise Act Regulations” of the Environment Ministry.

Rather extensive efforts to release information through published works and manuals have been implemented. The following can be highlighted:

- ▶ “Red Eléctrica and birds wildlife: 15 years of applied research”. This book shows the extensive research carried out by the Utility during these years.
- ▶ The triptych “Kestrels in electrical substations” drafted in cooperation with the Higher Scientific Research Council.
- ▶ The “Environmental Annual Report for 2004”, approved by AENOR



technological innovation



During 2005, R+D+i operations carried out by Red Eléctrica have progressed significantly that can be summarised by the following key points:

- ▶ Projects intended for easier integration of renewable energies have been fostered. Work lines have been targeted on winds prediction improvement, analysis of stability phenomena and the transmission grid dynamic performance.
- ▶ Involvement in research and development projects financed by European funds under the 6th Framework Programme has increased. During 2005, two contracts for integrated projects have been signed with the European Commission (FENIX and WIND ON THE GRID) as well as a coordination action (RELIANCE).
- ▶ A significant increase of investments in R+D+i projects that reach almost Euros 3 million has been achieved.

More significant projects completed in 2005

Power flows directing

A project enclosed in the European Commission Programme for Electricity Trans-European Grids has been implemented. The programme was intended to study the performance of equipment able to direct power flows.

Results have been satisfactory and new research lines based on those findings are now open for further research on the FACTS (Flexible Alternating Current Transmission System) equipment.

SEPDES: Expert system for outages planning

Project aimed to automate the study of requests for carrying out works on the transmission grid, when outages are required, and how their impact on electricity supply can be determined. The first release of the developed software has been commissioned in 2005.

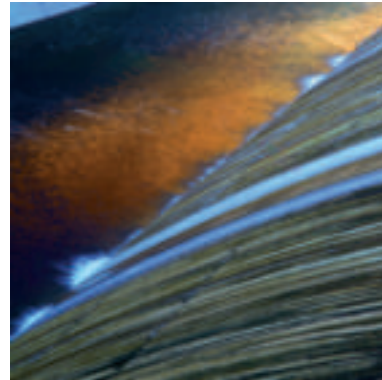
IELAS

A consortium of businesses and European universities under Red Eléctrica leadership have implemented during four years this project for development of a current instrument transformer based on magnetostrictivity (the property some materials display to change their dimensions when subject to magnetic fields). The project was completed and a prototype built and successfully tested in an Italian high voltage laboratory. A new research line for state-of-the-art technologies applied to electric values metering equipment is now available.

ESAF: Setting up Future Scenarios

This research project, carried out through cooperation with Comillas University is aimed to study an electricity system performance by setting up automatically short-term grid scenarios based on actual historical events. During 2005, forecasting the reactances position through decision trees and generation units set values using regression models have been implemented.

“Technological innovation is challenged by the efforts to optimise those infrastructures that support the electricity system”.



Most significant projects in progress

RELIANCE

This project is intended to identify the R + D common requirements of TSO (Transmission System Operator) in Europe and set up an operation flow sheet of tasks to be implemented. Work is currently implemented jointly with eight TSO and several businesses and European Research centres to such purpose.

FENIX

This project is aimed to promote distributed generation based on the development of a generation plants virtual platform. A DSO (Distributed System Operator) would be set up also for output management and relations with TSO. National Grid, EDF, Siemens, Areva and Gamesa are some of the partners involved in this Iberdrola-coordinated project.

WIND ON THE GRID

This project bets on large scale integration of wind generated electricity and is framed on the European Target for 2010, which envisions that 12% of the primary energy con-

sumption will be from renewable sources. Both technical and regulation procedures are proposed to optimise wind farms management.

MOTTIBA

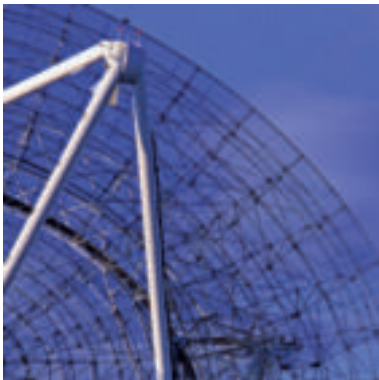
Artificial intelligence, neural and Bayesian networks, as well as supporting vector processors are applied by this project to optimise the topology design of telecommunication networks.

Real time transmission capacity

The transmission grids operation close to their physical limits is increasingly necessary. The real time study of critical weather parameters involved in transmission capacity determination is allowed by this project.

HYSTERESIS: Research on demand voltage trends

This project is aimed to find out how voltage is related to energy demand. This information is significant for the system operation and highly relevant in conditions close to a voltage collapse.



Facilities database

Red Eléctrica is the first electricity transmission utility worldwide that keeps the data about all the facilities georeferenced through satellite. This project enclosed in the development of a large database where technical, topological, graphic and mapping information is held, improves the assets management capacity and increases the National Electricity System reliability.

Aerial photography of the high voltage transmission line rights-of-way and transformer compounds locations are available in the new facilities database that can output referenced maps using satellite imagery. This information that shows more accurately the facilities location offers, besides other improvements, increased efficiency of the facilities maintenance as well as larger capacity for future planning and the electricity system development.

On the other hand, detailed information checks of the facilities, both geographical and of the documents associated to projects, is made easier when the database is integrated in the assets management systems of the Utility.



economic- financial management

The Utility's growth potential and value generation have been ratified again this year by the bigger financial results and cash flow. Both values have increased over those reported the previous year by 19.6% and 22.5%, respectively.

The funds generated combined with the Utility's sound financial position allow paying shareholders an attractive dividend and fund a large investments plan, while an efficient capital structure is kept throughout.

consolidated results of 2005

The outstanding financial events, in 2005, are described next:

- ▶ Since the 15th of February 2005, Inalta accounts, the utility that controls the assets owned formerly by Iberdrola, are enclosed in Red Eléctrica Group financial statements. The inclusion was carried out on the 30th of June 2005, once the remaining 75% held, still, by Redalta, the utility that owned 100% of Inalta's shares, was purchased.
- ▶ The complete (100%) share capital of Red Eléctrica Telecomunicaciones (Albura) was sold, the past 30th of June, to T-Online Internacional.
- ▶ On the 1st of January 2005, the purchase of Viesgo transmission assets and the agreement to purchase-sell Unión Fenosa's transmission assets have been completed.

Turnover has reached Euros 860.2 million, which implies a 16.4% growth over 2004. The increase is due basically to:

- ▶ The remuneration associated to Inalta's transmission assets, earned during 10 and a half months, which amounts to Euros 107.6 millions.
- ▶ The increased income from transmission operations that is due to the facilities commissioned by Red Eléctrica during 2004, and that from the purchased Viesgo and Unión Fenosa assets.
- ▶ Income from engineering and construction works implemented for third parties, although the amount is smaller than that of the previous year.

"Growth of the business arising from the Utility's main operations and the synergies issuing from the purchased assets integration have led to excellent financial results".



Consolidated results (IFRS)

Euros in thousand	2005	2004	05/04 %
Turnover	860,163	738,830	16.4
(EBITDA) Gross operating profit)	591,129	496,369	19.1
(EBIT) Nett operating profit)	332,164	307,229	8.1
Profit before taxes from continued operations	262,044	240,453	9.0
Annual profit from continued operations	176,704	159,276	10.9
Profit contributed by the controlling company	162,422	135,806	19.6

The **consolidated operating expenses** have reached Euros 274.6 million, compared to Euros 246.4 million, in 2004. This implies an 11.4% increase. In the consolidated operating expenses, the following stand out:

- ▶ Other operating expenses and supplies, which enclose costs associated to facilities maintenance, have reached Euros 196.5 million, and show a 10.3% increase over 2004.
- ▶ Employees costs amount to Euros 78.1 million and show a 14.5% increase over the same period of 2004.

Increased efficiency of the procurement process has been required due to the significant investments in the transmission and the addition of new assets during the last few years. For the mentioned reasons, a suppliers area in the web site (where they are promptly informed about how they are qualified) plus quality-related agreements with suppliers have been signed to achieve better financial conditions, enhance service quality and increase mutual trust.

The Group's mean payroll has increased 10.8% and numbers 1,355 employees in 2005. The increase is due to the personnel added to the parent Utility following the purchased transmission assets integration and the need to render new operating services in the off-the-Peninsula systems. The Group's final payroll stands now at 1,401 employees.

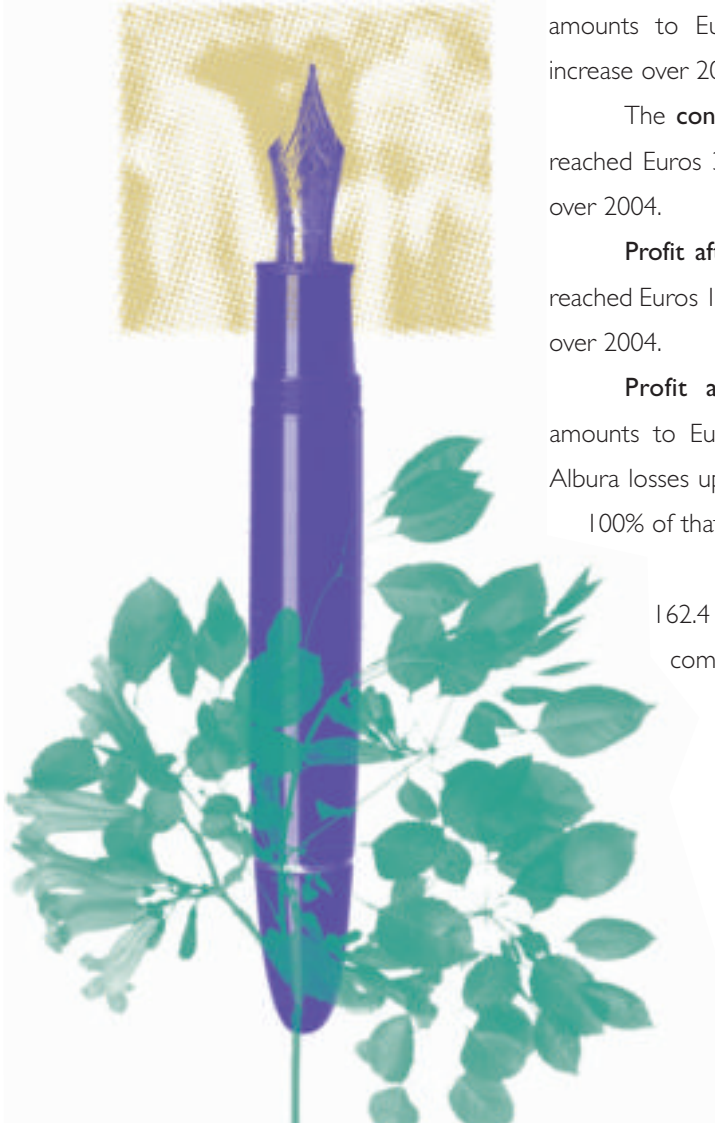
The **consolidated gross operating profit (EBITDA)** amounts to Euros 59.1 million, which imply a 19.1% increase over 2004.

The **consolidated net operating profit (EBIT)** has reached Euros 332.2 million, and shows an 8.1% increase over 2004.

Profit after taxes from continued operations has reached Euros 176.7 million, which implies a 10.9% increase over 2004.

Profit after taxes of interrupted operations amounts to Euros – 14.3 million. This amount includes Albura losses up to 30th of June and the loss arising when 100% of that utility's shares were sold.

Profit after taxes has reached Euros 162.4 million, which implies a 19.6% increase compared to Euros 135.8 million, in 2004.



Financing

Red Eléctrica financial operations during 2005 have been determined by the increased funding requirements due, mainly, to the Redalta purchase. To finance this purchase, the Utility not only had to raise more funds in the markets, but implied, also, an opportunity to rearrange the Group's financial structure.

A number of financial instruments were applied:

- ▶ Loans already available were used.
- ▶ Some medium and long-term banking facilities were rescheduled amounts and terms were increased and costs lowered, and
- ▶ Securities were issued in the long-term market.

Of the actions carried out, three must be highlighted:

- ▶ A new syndicated funding facility, through a credit line, was subscribed to replace the syndicated loan signed in 2003. The limit has been increased to Euros 900 million and maturity extended to 2012.
- ▶ The long-term loan signed with the Official Credit Institute, in 2004, amounting to Euros 200 million, has been rescheduled to improve some relevant conditions such as the maturity term extended to 2015;
- ▶ A bonds issue in the United States private placement market for a total US \$ 500 million, distributed in four tranches with maturities in 2015, 2020, 2025 and 2035. The foreign exchange risk has been completely deleted through hedging contracts that cover the complete amount and maturity terms.

The Utility has been able through these transactions to strengthen its financial structure, for a proper balance between bank debt and securities issues. Additionally, the investors' base has been enlarged and maturity terms extended.

It must be pointed out that the already mentioned Redalta purchase has not reduced the Group's solvency, as evidenced by the credit agencies, Standard & Poor's and Moody's. Both upheld, throughout 2005, the credit ratings they have assigned to Red Eléctrica: AA-/A+1 and A2, respectively.

“The debt rescheduling that increased the amounts and extended maturity terms coupled to the hedging against increased interest rates ensure a highly competitive long-term financial structure”



Red Eléctrica Group Balance Sheet – IFRS

Euros in thousand	2003	2004	2005	05/04 %
Non-current assets	3,124,338	3,099,843	4,247,996	37.0
Current assets	234,441	363,095	390,554	7.6
Total assets	3,358,779	3,462,938	4,638,550	33.9
Equity	824,431	876,205	962,853	9.9
Net financial debt	1,911,147	1,845,826	2,791,134	51.2
Other liabilities	623,201	740,907	884,563	19.4
Total liabilities	3,358,779	3,462,938	4,638,550	33.9
Leverage ratio	69.9 %	67.8 %	74.4 %	

Note: In 2004, non-current assets decreased since the telecommunication business was deemed to be ready for sale.

Red Eléctrica Group Investments

Consolidated investments, during 2005, have amounted to Euros 755.5 million. Of the mentioned investments, Euros 420.2 million were allocated to expansion and improvement of the transmission grid; Euros 247.3 million to purchase the 75% of Redalta (this implies the addition to the Group of Euros 1,020 million in tangible fixed assets); Euros 45.1 million allocated to the Viesgo transmission grid purchase, and Euros 42.9 million to other investments. In addition, Euros 124.6 million of assets that were sold to Unión Fenosa have been deleted from this heading.

The main projects being currently implemented in the Peninsula transmission grid are listed below:

- ▶ Works strengthen the transmission infrastructure in Andalusia and the Peninsula South-eastern zone.
- ▶ Development of the Northern transmission lines alignment to increase their transmission capacity.
- ▶ Strengthening the Peninsula Central, Northeastern and Northwestern zones.
- ▶ Development of infrastructures to support the high-speed railway lines expansion and,
- ▶ Increased transmission capacity of the Morocco interconnecting link across the Strait.

Investments

Euros in thousand	2001	2002	2003	2004	2005	05/04 %
Transmission grids purchased in Spain	-	815,929	535,177	-	45,098	-
Investments in transmission grids in Spain	129,885	203,396	215,347	243,368	420,182	72.7
Purchase of stakes in other companies	-	91,668	-	-	247,335	-
Investments in equipment and telecommunications network	105,164	39,677	10,751	-	-	-
Investment in Bolivia	-	-	1,956	7,256	7,199	-0.8
Other investments	9,784	8,040	17,038	23,946	35,725	49.2
Total	244,833	1,158,710	780,269	274,570	755,539	175.2

Note: In 2004, does not include the telecommunication investment was deemed ready to be sold



our shareholder

Red Eléctrica shares have shown an excellent outlook in 2005. At year's end, a 58.5% revaluation had been achieved over the previous year.

The shares performance has been far better than most of the reference stock exchange indexes. Based on dividends paid out, total return for shareholders reached 62.3%.

shareholders and stock exchange information

As of 31st December 2005, Red Eléctrica share capital of Euros 270,540,000 made up by 135,270,000 shares of 2 euros par value each was fully subscribed to and paid in. During 2005, both the number of outstanding shares or their par value did not experience any change.

Red Eléctrica share capital is listed in the four Spanish Stock Exchanges as well as in the Spanish electronic stock market. In the 1st of July 2005, Red Eléctrica returned to the selective Ibex-35, after being barred from that index during the six previous months. The weighted value, in the Ibex-35, as of the 31st December 2005, reached 0.86%.

The free-float shares of Red Eléctrica increased, during 2005, from 58.5% to 70.0%. This increase was due to:

- ▶ The 3% stake in Hidroeléctrica del Cantábrico sold on 1st of April 2005, when the Royal Decree Law 5/2005 was published, which limits to 1% the stake anyone that is active in the electricity industry is allowed to own in the Utility.
- ▶ The 8.5% stake that the Sociedad Estatal de Participaciones Industriales (SEPI) owned in the Utility was sold on the 29th of September 2005. This reduced SEPI's stake in Red Eléctrica capital to 20%.

Both transactions were carried out through block trades and targeted to domestic and foreign institutional investors.

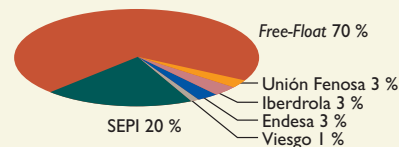
As of 31st December 2005, the free-float consisted of 94,689,000 shares. It is deemed that 18% are owned by minority stockholders, 25% by Spanish institutional investors and 57% by foreign institutional investors mainly from the United Kingdom, United States and Germany.

The number of treasury stock shares, as of 31st December 2005, amounted to 160,982 shares, equivalent to 0.17% of the total outstanding shares.



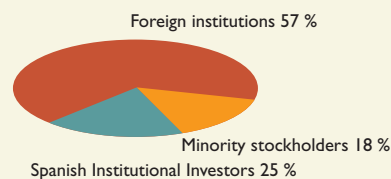
Shareholders structure

31st December 2005



Free-float structure

Estimated at the 31st December, 2005



Stock exchange development

In spite of the record oil prices and rates of interests that increased in the United States and the Eurozone, 2005 has been the third year in a row that earnings have been

reported by most stock exchanges worldwide. Good business profits and the markets high liquidity have supported the stock exchanges rise.

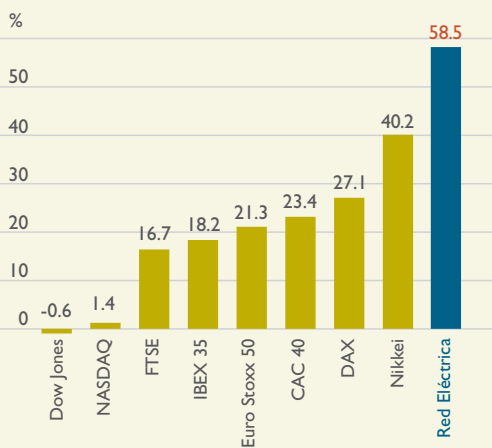
Both for Japanese and European stock exchanges, 2005 has been a year to remember, while the United States market have been affected by the steady interest rates increase. In Europe, the main stock exchanges achieved significant results and the same happened to the Nikkei that shows a 40.2% increase, while the Dow Jones decreased – 0.6%.

Red Eléctrica reached Euros 26.16 per share or a 58.5% revaluation at year's end, this exceeded by far that of the Ibex-35 that ended at 18.2%. Red Eléctrica strategy of exercising earlier the option to purchase Redalta's 75%, added to the good growth outlook of the Utility and paid dividend have been rewarded by the stock exchange investors attitude.

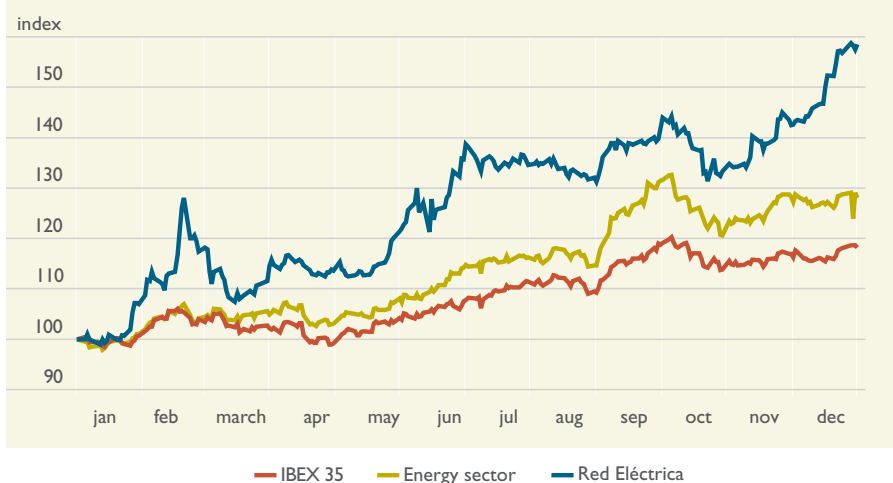
The number of traded shares amounted to 23.1 million, which is 2.44 times the free float shares amount, while stock exchange actual dealings amounted to Euros 4,870.2 million.

“Red Eléctrica shares performance in the stock exchange has been much better than that of Ibex-35 and most utilities”

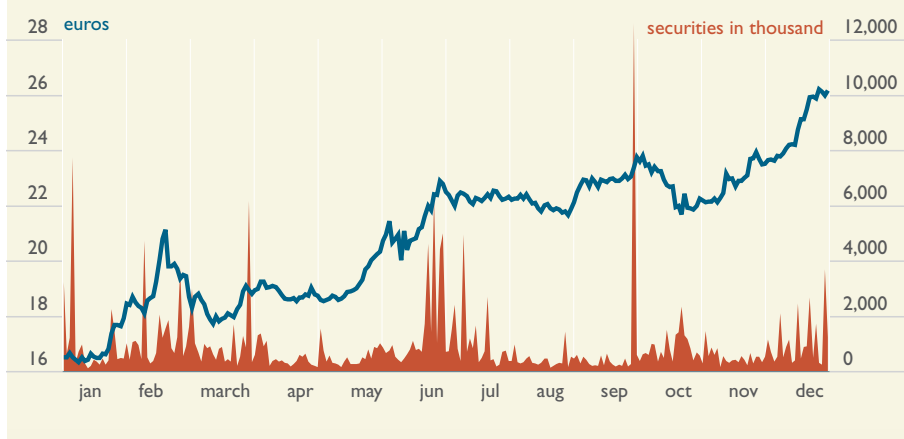
Stock exchange indexes. 2005



Red Eléctrica compared to IBEX35 - Energy Sector



Quoted prices and daily trading trends



Quoted prices monthly trend

	Exchange trading days	Monthly exchange turnover (€)				Monthly change %	Trading volumen	
		Max.	Min	Mean	Close		No. Shares	Cash payments (€)
January	20	17.95	15.95	16.78	17.93	-8.0	19,414,202	325,629,066
February	20	21.33	17.92	19.25	19.50	8.8	25,243,139	487,031,399
March	21	19.50	17.58	18.39	19.10	-2.1	18,743,131	344,918,162
April	21	19.39	18.45	18.88	18.75	-1.8	17,055,571	322,133,121
May	22	20.33	18.44	19.06	20.13	7.4	9,841,372	187,588,810
Jun	22	22.94	19.91	21.64	22.89	13.7	31,141,682	672,308,573
July	21	23.00	21.55	22.35	22.20	-3.0	27,118,737	606,780,497
August	23	22.47	21.41	22.01	21.87	-1.5	9,823,582	216,253,745
September	22	23.75	21.84	23.19	23.75	8.6	19,896,883	457,624,278
October	21	23.95	21.50	22.50	22.25	-6.3	18,486,804	416,017,466
November	22	23.93	21.85	22.74	23.52	5.7	11,188,835	254,513,867
December	21	26.40	23.47	25.03	26.16	11.2	23,160,606	579,391,149
Year's total	256	26.40	15.95	21.09	26.16	58.5	231,114,544	4,870,190,134

Shareholders remuneration

“Shareholders remuneration through dividends has increased 19% and shows the Utility decision to offer shareholders an increasingly attractive remuneration”.

Red Eléctrica is committed to achieve maximum value for its shareholders. With this in mind, it offers, on the one hand, an attractive return through the paid dividends and, on the other, contributes to the shares revaluation through an efficient business management.

In 2005, direct remuneration to shareholders through dividends increased 19% over the previous year. The gross dividend proposal submitted to the General Meeting of Shareholders to be paid against 2005 profits amounts to

Euros 0.7304 per share. An interim gross dividend of Euros 0.2708 per share was paid on the 2nd of January 2006, and Euros 0.4596 per share were pending distribution to complete the gross dividend paid for 2005.

Dividend per share

	2001	2002	2003	2004	2005
Dividend per share (in euros)	0.4550	0.4800	0.5480	0.6138	0.7304
Interim	0.1800	0.1900	0.2120	0.2375	0.2708
Complementary	0.2750	0.2900	0.3360	0.3763	0.4596
Dividend computed on net profit (%)	67.8	67.7	65.0	65.3	67.8

Main stock exchange indicators

	2001	2002	2003	2004	2005
Total number of shares	135,270,000	135,270,000	135,270,000	135,270,000	135,270,000
Total number of outstanding shares	42,610,050	42,610,050	80,485,650	80,485,650	94,689,000
Share par value (euros)	2	2	2	2	2

Daily trading (securities)

Maximum	1,075,878	865,787	42,935,482	6,714,657	12,587,045
Minimum	53,511	42,618	110,021	104,761	115,238

Quoted price (euros)

Maximum	11.32	11.95	13.34	16.75	26.40
Minimum	9.00	7.91	9.54	12.75	15.95
Mean	10.16	10.18	11.29	14.32	21.09
Closing	10.45	9.64	13.00	16.50	26.16

Market capitalization at year's end (€)

	1,413,571,500	1,304,002,800	1,758,510,000	2,231,955,000	3,538,633,200
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Profit per share (BPA) (euros)

Net cash flow per share (CFPA) (euros)	1.44	1.66	2.37	2.58	3.18
Quoted price/ BPA (PER) (number of times)	15.52	13.06	15.19	16.34	21.79
Quoted price / CFPA (PCF) (number of times)	7.25	5.80	5.48	6.40	8.23
Quoted price / Book value per share (PVC) (number of times)	1.82	1.61	2.07	2.55	3.68

IFRS Data

Communication with shareholders and investors

Red Eléctrica dialogue with shareholders is open, fluent and stays close to their concerns. Communication is fully transparent and supplies them the available information at the same time it is released to the stock exchange or financial agents.

During 2005, the Utility management team has attended lectures and meetings held with institutional investors in the main financial markets of Spain, Europe and the United States. Meetings with institutional analysts and investors numbered 198, besides 15 road shows and 11 lectures delivered to institutional investors both on equity and fixed-yield securities.

On the other hand, as a way to promote communication channels addressed to the shareholders, and foster their attendance to General Meetings, Red Eléctrica has enhanced its web site (www.ree.es) as follows:

- ▶ Allowing electronic voting.
- ▶ Looking up documents and information related to General Meetings of Shareholders.
- ▶ Transmission on line of General Meetings of Shareholders.
- ▶ Transmission on line of lectures on the Utility profits and strategy.
- ▶ The notices service, "Grid Updated", that shows relevant news about the Utility at the same time they are released to the markets.

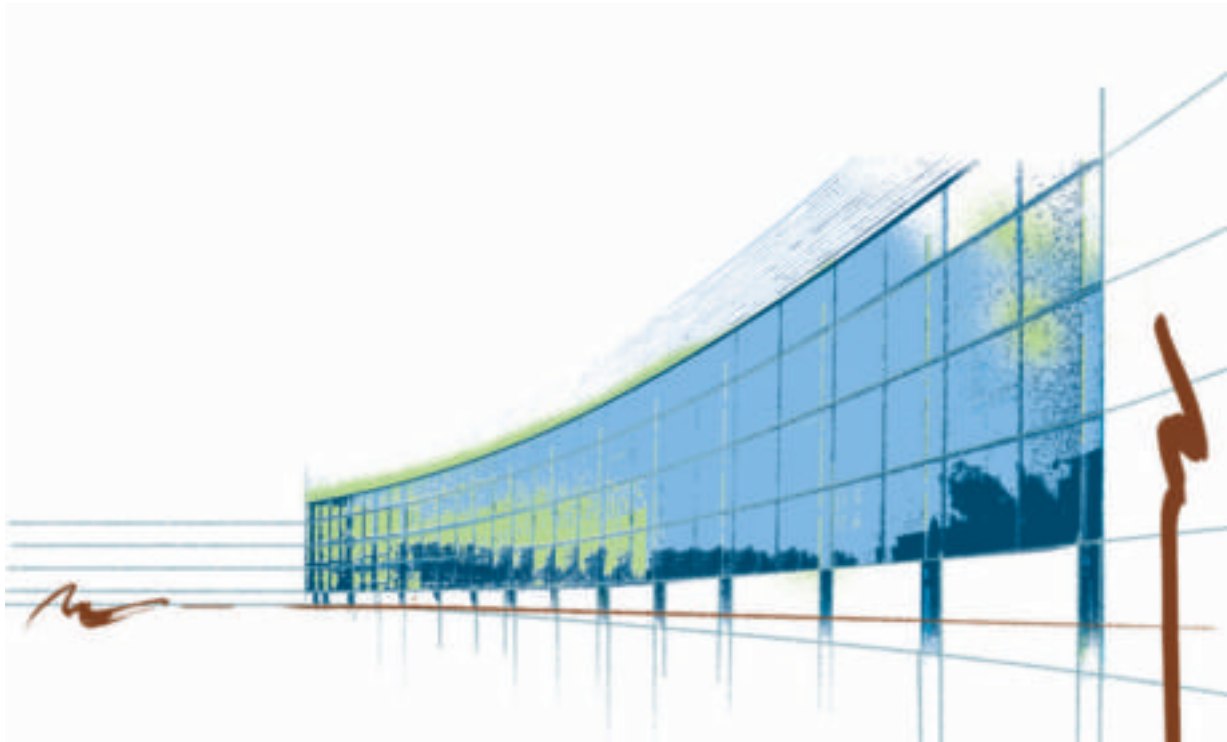
The main communication channels used by the Utility to inform and answer shareholders inquiries are the following:

Shareholders information office
Toll-free telephone: 900 100 182
Electronic mail: accionistas@ree.es

Web site: www.ree.es
("shareholders and investors" area)

Quarterly Shareholders Newsletter

Unit for investors attention
Electronic mail:
relacioninversores@ree.es





legal
documentation



KPMG Auditores S.L.
Edificio Torre Europa
Paseo de la Castellana, 95
28048 Madrid

Auditors' Report on the Consolidated Annual Accounts

(Free translation from the original in Spanish.
In the event of discrepancy, the Spanish-language version prevails)

To the Shareholders of
Red Eléctrica de España, S.A.

1. We have audited the consolidated annual accounts of Red Eléctrica de España, S.A. (hereinafter the Company) and subsidiaries (hereinafter the Red Eléctrica Group), which comprise the consolidated balance sheet at 31 December 2005, the consolidated statements of income, cash flows and changes in equity for the year then ended and the notes thereto, the preparation of which is the responsibility of the Company's board of directors. Our responsibility is to express an opinion on the consolidated annual accounts taken as a whole, based on our audit which was conducted in accordance with generally accepted auditing standards in Spain, which require examining, on a test basis, evidence supporting the amounts in the consolidated annual accounts and assessing the appropriateness of their presentation, of the accounting principles applied and of the estimates employed.
2. The accompanying consolidated annual accounts for 2005 are the Red Eléctrica Group's first annual accounts prepared in accordance with European Union-endorsed International Financial Reporting Standards (hereinafter EU-IFRS) which require comparative figures be included for the previous year. Therefore, and in accordance with prevailing Spanish legislation, the consolidated balance sheet at 31 December 2005, consolidated statements of income, cash flow and changes in equity for the year then ended and the notes thereto include comparative figures for 2004 which result from the application of EU-IFRS in force at 31 December 2005. Consequently, the figures for 2004 differ from those reported in the approved 2004 consolidated annual accounts prepared in accordance with accounting principles prevailing that year. The differences generated as a result of applying EU-IFRS to consolidated equity at 1 January and 31 December 2004 and to consolidated results for 2004 are detailed in note 33. We express our opinion solely on the consolidated annual accounts for 2005. On 14 March 2005 we issued our unqualified audit report on the consolidated annual accounts for 2004, which were prepared in accordance with accounting principles prevailing that year.
3. In our opinion, these consolidated annual accounts for 2005 present fairly, in all material respects, the consolidated equity and consolidated financial position of Red Eléctrica de España, S.A. and subsidiaries at 31 December 2005 and the consolidated results of its operations and the changes in consolidated equity and consolidated cash flows for the year then ended, and contain sufficient information necessary for their adequate interpretation and understanding, in accordance with EU-IFRS, which have been applied on a basis consistent with that used in the preparation of the figures and information for the preceding year which, as stated in the paragraph above, have been included in the 2005 consolidated annual accounts, exclusively for comparison purposes.
4. The accompanying consolidated directors' report for 2005 contains such explanations as the directors of the Company consider relevant to the situation of the Red Eléctrica Group, the evolution of its business and other matters, but is not an integral part of the consolidated annual accounts. We have verified that the accounting information contained therein is consistent with that disclosed in the consolidated annual accounts for 2005. Our work as auditors is limited to the verification of the consolidated directors' report within the scope described in this paragraph and does not include a review of information other than that obtained from the accounting records of Red Eléctrica de España, S.A. and subsidiaries.

KPMG AUDITORES, S.L.

Julián Martín Blasco

24 March 2006



consolidated annual accounts 2005

page **64** Financial highlights 2005

page **68** Notes to the Consolidated Financial Statements

page **107** Consolidated directors' report

page **114** Individual Financial Statements

page **118** Proposed Profits Distribution

Group Red Eléctrica

Consolidated balance sheets at 31 december 2005 and 2004 · In thousands of Euros

ASSETS	2005	2004
Property, plant and equipment (note 5)	4,174,430	3,022,049
Investment property (note 6)	3,666	1,216
Goodwill (note 7)	15,056	13,040
Intangible assets (note 8)	8,686	8,844
Non-current financial assets (note 17)	4,355	17,453
Investments accounted for using the equity method (note 9)	7,142	4,003
Deferred tax assets (note 21)	33,973	25,878
Other non-current assets	688	7,360
Total non-current assets	4,247,996	3,099,843
Inventories (note 10)	35,640	28,037
Trade and other receivables (note 11)	347,642	230,638
Current financial assets (note 17)	31	1,234
Income tax receivable (note 21)	1,481	930
Other current assets	5,791	19
Cash and cash equivalents	18,768	12,958
Assets classified as held for sale (note 20)	-	103,471
Total current assets	409,353	377,287
Total assets	4,657,349	3,477,130

EQUITY AND LIABILITIES	2005	2004
Share capital	270,540	270,540
Other reserves	264,546	264,546
Rest of reserves	427,693	341,064
Minority Interests	74	55
Net equity (note 12)	962,853	876,205
Bonds and other marketable securities (note 15)	1,252,696	849,565
Borrowings (note 15)	1,284,828	783,085
Deferred tax liabilities (note 21)	156,776	57,461
Provisions (note 13)	34,618	30,329
Other non-current liabilities (note 14)	311,669	256,076
Non-current liabilities	3,040,587	1,976,516
Bonds and other marketable securities (note 15)	16,894	58,020
Borrowings (note 15)	282,974	189,246
Trade and other payables (note 18)	117,177	100,786
Other current financial liabilities (note 17)	2,854	3,010
Provisions	1,505	1,000
Current tax liabilities (note 21)	31,026	25,172
Other current liabilities (note 19)	201,479	140,995
Liabilities classified as held for sale (note 20)	-	106,180
Current liabilities	653,909	624,409
Total equity and liabilities	4,657,349	3,477,130

Group Red Eléctrica

Consolidated income statements years 2005 and 2004 - In thousands of Euros

INCOME STATEMENT	2005	2004
Net sales (note 22-a)	860,163	738,830
Other operating income	5,520	3,915
Materials consumed (note 22-b)	(26,432)	(18,365)
Personnel expenses (note 22-c)	(78,080)	(68,188)
Other operating expenses (note 22-b)	(170,042)	(159,823)
Amortization and depreciation (notes 5, 6 and 8)	(258,965)	(189,140)
Net operating profit	332,164	307,229
Financial income	4,604	2,716
Financial expenses	(108,437)	(76,701)
Exchange differences	(243)	739
Net profit/(loss) on changes in fair value of financial instruments (note 17)	4,753	(67)
Net loss on impairment of assets	(312)	(874)
Share of profit of associates accounted for using the equity method (note 9)	556	703
Net profit on disposal of non-current assets (note 22-d)	23,510	199
Other income or expenses	5,449	6,509
Profit before tax on continued operations	262,044	240,453
Income tax expense (note 21)	(85,340)	(81,177)
Profit for the year on continued activities	176,704	159,276
Loss after tax on discontinued activities (note 20)	(14,271)	(23,463)
Profit for the year	162,433	135,813
Minority interests	(11)	(7)
Attributable to equity holders of the Parent	162,422	135,806
Basic earnings per share (Euros)	1.20	1.01
Diluted earnings per share (Euros)	1.20	1.01

Group Red Eléctrica

Consolidated statements of changes in equity · Years 2005 and 2004 · In thousands of euros

NET EQUITY	Share capital	Other reserves	Rest of reserves	Minority interests	Total equity
Balances at 1 January 2004	270,540	264,546	289,290	55	824,431
Distribution of 2003 profit:					
Additional dividends for 2003	-	-	(45,451)	-	(45,451)
Interim dividend for 2004	-	-	(32,093)	-	(32,093)
Movement in own share reserve	-	-	103	-	103
Conversion differences	-	-	(4,560)	(7)	(4,567)
Valuation of financial instruments	-	-	(2,743)	-	(2,743)
Profit for 2004	-	-	135,806	7	135,813
Other	-	-	712	-	712
Balances at 31 December 2004	270,540	264,546	341,064	55	876,205
Distribution of 2004 profit:					
Additional dividends for 2004	-	-	(50,838)	-	(50,838)
Interim dividend for 2005	-	-	(36,588)	-	(36,588)
Movement in own share reserve	-	-	(1,128)	-	(1,128)
Conversion differences	-	-	7,195	8	7,203
Valuation of financial instruments	-	-	3,305	-	3,305
Profit for 2005	-	-	162,422	11	162,433
Other	-	-	2,261	-	2,261
Balances at 31 December 2005	270,540	264,546	427,693	74	962,853

Group Red Eléctrica

Consolidated cash flow statements · Years 2005 and 2004 · In thousands of euros

CASH FLOW STATEMENTS	2005	2004
CASH FLOWS FROM OPERATING ACTIVITIES	289,032	356,816
Cash flows from operations	500,658	433,308
Profit before tax on continued activities	262,044	240,453
Amortisation and depreciation	258,965	189,140
Provisions/provision surplus	12,337	12,717
Capital grants and other deferred income transferred to profit/(loss)	(9,178)	(8,803)
Profit/loss on disposal of non-current assets	(23,510)	(199)
Income taxes paid	(71,017)	(82,654)
Changes in current working capital	(140,609)	6,162
Increases in inventories, receivables, current advances and other current assets	(152,699)	(25,185)
Reduction in trade payables, current advance collections and other current liabilities	12,090	31,347
CASH FLOWS FROM INVESTING ACTIVITIES	(502,422)	(221,523)
Acquisition and disposal of PPE and intangible assets	(293,949)	(243,691)
Acquisition and disposal of other investments	6,672	1,887
Acquisition and disposal of subsidiaries and joint interests	(243,815)	(8,853)
Capital grants and other advance collections	28,670	29,134
CASH FLOWS FROM FINANCING ACTIVITIES	217,797	(136,160)
Changes in equity	1,284	753
Short-term financial debt	1,422,078	69,100
Repayment of short-term financial debt	(564,473)	(216,064)
Long-term financial debt	1,276,630	273,764
Repayment of long-term financial debt	(1,834,791)	(189,641)
Dividends paid	(82,931)	(74,072)
NET CASH FLOW	4,407	(867)
Effect of exchange rate fluctuations on cash and cash equivalents	1,403	(1,005)
CHANGES IN CASH AND EQUIVALENTS DURING THE PERIOD	5,810	(1,872)
Cash and cash equivalents at the start of the year	12,958	14,830
Cash and cash equivalents at year end	18,768	12,958

Notes to the Consolidated Financial Statements

Year 2005

(1) ACTIVITIES OF GROUP COMPANIES

Red Eléctrica de España, S.A. (hereinafter the Parent company or the Company) was incorporated in 1985. The principal activities carried out by the Parent company are the transmission of electrical energy, operation of the system and management of the transmission grid, co-ordination of international exchanges of electrical power and administration of international energy agreements. The Red Eléctrica Group, through its Parent company, carries out additional activities such as the acquisition, holding and management of foreign securities, provision of consultancy services, engineering and construction work and electrical activities outside the Spanish electrical system through Red Eléctrica Internacional, S.A. and subsidiaries (Appendix I) and the holding and management of national securities and electricity transmission activities through Red de Alta Tensión S.A., solely-owned company (hereinafter Redalta) and Infraestructuras de Alta Tensión, S.A., solely-owned company (hereinafter Inalta) (Appendix I). At their annual general meeting the shareholders of the Parent company approved these consolidated financial statements and the merger by simple absorption of Redalta and Inalta by the Parent company after acquisition of the remaining 75% of share capital in these companies, resulting in a 100% shareholding in each.

In July 2003 the Parent company incorporated the Dutch company Red Eléctrica de España Finance, B.V., the activity of which consists of attracting funds, performing financial transactions and rendering services to Group companies (Appendix I).

In June 2005 the Parent sold 100% of its shares in Red Eléctrica Telecomunicaciones, S.A. (hereinafter albura), a company through which the Group carried out telecommunication activities. In 2004 these telecommunication activities became available-for-sale non-current assets and discontinued activities. Consequently, albura's assets and liabilities were differentiated in the 2004 consolidated balance sheet.

(2) BASIS OF PREPARATION OF THE CONSOLIDATED ANNUAL ACCOUNTS

a) General information

The accompanying consolidated annual accounts of the Group have been prepared by the board of directors of the Parent company to present fairly the consolidated equity, the consolidated financial position at 31 December 2005, the results of its operations and changes in consolidated equity and cash flows of the Group for the year there ended.

The consolidated annual accounts of the Group are expressed in thousands of Euros and have been prepared in accordance with International Financial Reporting Standards (IFRS) and its interpretations endorsed by the European Union (EU-IFRS).

All mandatory accounting principles which would have a significant effect on the preparation of these consolidated annual accounts have been applied.

These consolidated annual accounts, formulated by the directors of the Company at the board meeting held on 23 March 2006 have been prepared on the basis of the accounting records of the individual companies which comprise the Red Eléctrica Group (see note 1). The consolidated financial statements include certain adjustments and reclassifications made to bring the accounting and presentation principles followed by different Group companies into line with those of the Company.

The consolidated annual accounts for 2004 were approved by the shareholders at their annual general meeting held on 26 May 2005. The Group's consolidated financial statements for 2005 are pending approval at the shareholders' general meeting. Nevertheless, the directors of the Company consider that these consolidated financial statements will be approved by the shareholders without significant changes.

b) Accounting estimates and assumptions

The preparation of financial statements under IFRS requires management of the Group to make judgements, estimates and assumptions that affect the application of standards and the reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates.

The Group's consolidated financial statements for 2005 include Group management's estimates on the value of assets, liabilities, income, expenses and commitments recognised, which were subsequently ratified by the board of directors. These estimates mainly comprise:

- ▶ Estimates on the recovery of assets and goodwill. Calculation of impairment of assets and goodwill is based on reasonable estimates and consideration of the country risk premium. Substantial changes to a country's regulations on goodwill could alter Company estimates.
- ▶ Estimates on the useful lives of property, plant and equipment.
- ▶ Assumptions used in the actuarial calculations.
- ▶ The existence and estimated amounts of contingent liabilities or liabilities of an indeterminate amount.

Although estimates were based on the best information available at 31 December 2005, future events may require these estimates to be modified (increased or decreased) in subsequent years. Any change in accounting estimates would be recognised prospectively in the corresponding consolidated income statement, in accordance with IFRS.

c) Reconciliation of IFRS with Spanish GAAP

As a result of the different accounting principles equity at 31 December 2004 and profits for 2004 under Spanish GAAP exceed their respective calculations under IFRS by Euros 19,620 thousand and Euros 3,425 thousand. At 1 January 2004 equity is Euros 24,688 thousand higher under Spanish GAAP than under IFRS. Note 33 on the effects of the transition from Spanish GAAP to IFRS includes a reconciliation of the main items in the Group's consolidated balance sheets at 1 January 2004 and 31 December 2004 and the 2004 consolidated statement of profit and loss of Red Eléctrica Group prepared under Spanish GAAP with figures resulting from applying IFRS, which have been used as a basis for the preparation of these consolidated financial statements.

d) Basis of consolidation

Consolidation of the results generated by entities for which control was acquired during the year is carried out taking into consideration only those results relating to the period between the date of acquisition and the close of that year.

Details of the type of companies consolidated and the respective methods of consolidation are as follows:

▶ Subsidiaries

Subsidiaries are entities controlled by the Company. Control is the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. Control is presumed to exist when the Parent company owns, directly or indirectly through subsidiaries, more than half of the voting rights. Control also exists when the parent owns half or less of the voting rights of an entity where there is power over more than half of the voting rights by virtue of an agreement with other investors or where it has power to cast the majority of votes at meetings of the board of

directors or equivalent governing body and control of the entity is by that board or body.

The financial statements of subsidiaries are fully consolidated. Consequently, all significant balances and transactions between fully consolidated companies have been eliminated.

Since 1 January 2004 (the date of transition to IFRS by the Group), assets and liabilities and contingent liabilities of a subsidiary are calculated at fair value on the date of acquisition. The excess of cost of acquisition over the fair value of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of identifiable net assets of the subsidiary acquired (i.e. discount on acquisition), the difference is recognised directly in the consolidated income statement. Minority interest investments are established in proportion to the fair value of the identified assets and liabilities recognised. Consequently, any loss attributable to the minority which exceeds the carrying amount of the minority interest is recognised with a charge to the equity of the Parent company.

- ▶ Minority interests in Group equity are included under minority interests in the consolidated balance sheet
- ▶ Minority interests in consolidated results for the year are included under minority interests in the consolidated income statement.

The financial year and closing date of the financial statements of consolidated subsidiaries coincide with those of the Parent company.

▶ Associates

Associates are entities over which the Company has significant direct or indirect influence through subsidiaries but not control or joint control. Usually, significant influence in an investee (direct or indirect) is when a company holds an interest equal to or more than 20% of the voting rights.

The financial year and closing date of the financial statements of associates coincide with those of the Parent company.

Investments in associates are accounted for by the equity method of accounting (unless those held for sale), that is at the Group's percentage share in the equity of the associate once dividends received from the associate and other balances have been eliminated, less impairment of individual shareholdings (in the event of transactions with associates the corresponding profit and loss should be eliminated to the extent of the Group's interest in the associate).

Any excess of cost of acquisition over the fair value of the part of identifiable net assets of the associate attributable to the Group is considered as goodwill and recognised in the consolidated balance sheet under associates. If the cost of acquisition is less than the fair value of the part of the fair value of distinguishable net assets of the associate attributable to the Group (i.e. discount on acquisition) the difference is recognised directly in the consolidated income statement.

Relevant information on consolidated subsidiaries and associates, the method of consolidation or valuation applied in preparation of the accompanying consolidated financial statements information is included in Appendix I to these notes.

The financial statements for each Group company are expressed in the functional currency of the main economic environment in which the entity operates. The consolidated financial statements are presented in Euros, which is the functional currency of the Company.

Operations of Red Eléctrica and subsidiaries have been consolidated in accordance with the following basic principles:

- ▶ The accounting principles and criteria used by Group companies have been harmonised with those applied by the Parent company.
- ▶ The financial statements of foreign companies have been translated by applying the year end exchange rates at the date of the balance sheet for assets and liabilities and the average exchange rate for the period for income statement items.
- ▶ Exchange rate differences from translation to Euros are recognised at year end under conversion differences in the consolidated balance sheet.
- ▶ All significant balances and transactions between fully and proportionally consolidated companies have been eliminated in the consolidation process.
- ▶ Margins on sales of capitalised goods and services between Group companies are eliminated when the relevant operations are carried out.
- ▶ Positive differences between the cost of acquisition and the underlying net book value of the shareholdings acquired which cannot be allocated to the fair value of assets and liabilities acquired are considered as goodwill.

Changes in the consolidated Group

Changes in the consolidated Group in 2005 are due to the acquisitions of Redalta and Inalta and the sale of albura (note 1).

e) Business combinations

All business combinations are accounted for by applying the purchase method. This consists of identification of the acquirer (the entity which obtains control over the other entities which comprise the business combination), measurement of cost of the business combination and allocation, on the acquisition date, of the business combination's costs to the assets acquired and the liabilities and contingent liabilities assumed.

The cost of the business combination is measured as the aggregate of the fair values at the date of exchange, assets contributed, liabilities incurred or assumed and net equity instruments issued by the acquirer, in exchange for control over the acquiree; plus any costs directly attributable to the business combination.

The excess of the cost of the business combination over the acquirer's interest in the net fair value of the identifiable assets, liabilities and contingent liabilities is recognised as goodwill.

If the acquirer's interest in the net fair value of assets, liabilities and contingent liabilities exceeds the cost of the business combination, the difference remaining after reassessment is recognised by the acquirer in profit or loss.

(3) LEGISLATION

Electricity sector in Spain

The legal framework for the electricity sector is contained in the Electricity Act (Law 54 of 27 November 1997). This Act recognises that electricity transmission is a natural monopoly due to the economies of scale provided by a single grid. The deregulation of transmission is instrumented through generalised third-party access to the grid, which is made available to the various parties to the electricity system and consumers in exchange for the payment of access tariffs. Remuneration for this activity is established by the Spanish State and is determined based on the cost of investment, operation and maintenance of installations, as well as other expenses incurred on the activity.

The Parent company has been assigned the functions of System Operator and manager of the transmission grid through this Act, in addition to its transmission activity. Accordingly, the Parent company is required to guarantee the quality and safety of power supplies and to co-ordinate the production and transmission systems. In its capacity as manager of the trans-

mission grid, the Parent company is in charge of the development and extension of the high voltage network and must ensure that it is maintained and improved in accordance with uniform and coherent criteria. It is also responsible for the administration of power transmissions between external systems using the Spanish grid, as well as withholding access to the grid when capacity is insufficient.

Royal Decree-Law 5/2005 of 11 March, on urgent measures for boosting productivity and improving public contracting levels, modifies the Electricity Act governing the maximum permitted shareholding of the Parent company and the role of System Operator regarding settlement, payment and collection and management of guarantees relating to supply and the numerous deviations with regard to generation and consumption units.

The Electricity Act deregulates intra-EU and international electrical energy exchanges, which may be carried out freely by the agents defined in this legislation. In its capacity as System Operator, the Parent company is responsible for short-term exchanges to ensure the quality and safety of the electricity supply. The Parent company will also continue to manage agreements for the long-term exchange of power with other EU and international electricity systems.

In respect of shareholding limitations, Law 54/97 establishes that any company of private individual may invest in the System Operator (activity attributable to the Company), provided that their direct or indirect shareholding or voting rights in the Company does not exceed 3%. Royal Decree-Law 5/2005 of 11 March, on urgent measures for boosting productivity and improving public contracting levels, which modifies the Electricity Act, establishes that the maximum permissible shareholding in the System Operator for parties which carry out activities in the electricity sector, or entities or individuals that hold at least 5% of the share capital of these entities (either directly or indirectly) is 1%, which may not be syndicated for any purpose. Furthermore, the sum of investment of electricity sector entities, either direct or indirect, should not exceed 40%. Nevertheless, this shareholding limitation is not applicable to SEPI which is required to hold at least 10% of the Company's share capital. At 31 December 2005, SEPI holds a significant investment in the Parent company, amounting to 20% of share capital (28.5% at 31 December 2004).

International electricity sector

At international level, the Red Eléctrica Group has investments in the electricity sector in Bolivia and Peru.

Both these countries have deregulated their electricity industry and use a regulation model supported by existing tariffs for the transmission activity. The regulatory models applied in both these countries are based on transparency of legislation, long-term stability and predictability of future income.

(4) SIGNIFICANT ACCOUNTING PRINCIPLES

The main accounting principles used in preparation of these consolidated financial statements are as follows:

a) Property, plant and equipment

Property, plant and equipment mainly comprises electrical energy plants and machinery which are valued at cost of production or acquisition. Cost includes, where applicable, the following items:

- ▶ Finance costs on external financing incurred during the construction period.
- ▶ Operating costs directly related to the construction of property, plant and equipment in projects directly controlled or supervised by Group companies.

Group companies transfer work in progress to property, plant and equipment in operation, when the asset enters service.

Enlargement or improvement expenses which lead to an increase in productivity or capacity or lengthen the useful life of the assets, are stated as an increase in the carrying amount of the asset.

Repair and maintenance costs of property, plant and equipment, which do not improve its performance or lengthen its useful life, are recognised in the consolidated income statement when incurred.

Property, plant and equipment is depreciated on a straight line basis over its estimated useful life, which reflects the period in which the companies expect to use the asset.

	Annual rate
Buildings	2%-10%
Electrical energy plant and machinery	2.5%-7.14%
Other installations, machinery, fixtures and fittings and other property, plant and equipment	4%-25%

b) Investment property

Investment property is measured at cost of acquisition. The market value of the Group's investment property is broken down in note 6 of the accompanying consolidated financial statements.

Investment property is depreciated on a straight line basis over its estimated useful life, which reflects the period in which the companies expect to use the asset.

c) Goodwill

Goodwill comprises the positive difference between the cost of acquisition and the fair value of assets and liabilities of the acquired subsidiaries. Goodwill is expressed in the functional currency of company acquired (note 7).

Goodwill is not amortised systematically but is subject to annual impairment testing (note 4-e).

d) Intangible assets

Intangible assets are stated at cost of acquisition and tested and adjusted periodically for impairment. Details of intangible assets included in this section are as follows:

Software

Software licenses are capitalised based on their cost of acquisition and preparation for use.

Software maintenance costs are expensed as incurred.

Software is amortised on a straight line basis over a period of between three and five years from the installation date of each programme.

Research and development costs

Research and development costs are recognised as the expense is incurred. Costs incurred in development projects (relating to the design and testing of new or improved products) are capitalised where there is evidence of the project's technical success and economic feasibility and where expenditure attributable to the asset during development can be measured

reliably. Research and development costs with a finite useful life are amortised on a straight line basis over a period not exceeding five years from commencement of the project.

e) Impairment

The recoverable value of non-current assets is assessed by the Group at each balance sheet date to determine whether there is any indication of impairment. An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount.

Goodwill, indefinite-lived intangible assets and intangible assets not yet ready for use are tested for impairment annually irrespective of whether any indication of impairment exists.

f) Investments

The Group classifies and values investments, except those accounted for using the equity method and those held for sale, in the following four categories:

- ▶ Loans and receivables (Group companies): are initially recognised at fair value, including transaction costs incurred on inception, and subsequently measured at amortised cost. Amortised cost mainly comprises the amount extended less any repaid principal, plus accrued interest receivable.
- ▶ Held-to-maturity investments: are initially recognised at fair value, including direct costs incurred in the transaction, and subsequently measured at amortised cost.
- ▶ Financial assets held for trading: are carried at market price, with changes in this value recognised under financial income or financial expense in the consolidated income statement
- ▶ Available-for-sale financial assets: are recognised at market price. Changes in market price are recorded in equity until the investment is derecognised, with the profit or loss on disposal taken to the consolidated income statement.

The fair values of quoted investments are based on current bid prices. If the market for a financial asset is not active (and for unlisted securities), the Group establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analysis, and option price models refined to reflect the issuer's specific circumstances.

g) Inventories

Quickly-rotating materials and replacement parts are measured at the lower of market price and cost, which is determined using the average weighted price model.

Group companies review the net realisable value of inventories at each year end, recognising value adjustments where cost exceeds market or where doubts exist over their use. When the circumstances that previously caused inventories to be written down below cost no longer exist or when there is clear evidence of an increase in net realisable value because of changed economic circumstances, the amount of the write-down is reversed.

h) Other non-current liabilities

▶ Employee benefits

(i) Pension commitments

The Group has defined contribution plans establishing the pension amounts employees receive upon retirement, normally based on one or more factors such as age, length of service, or salary band. Under the defined contribution plan, the Group pays set contributions to an external entity and has no legal or implicit obligation to make further contributions if the fund lacks sufficient assets to satisfy payments to employees for services rendered during the current and prior years

(ii) Other long-term employee benefits

Other long-term employee benefits include benefits other than pensions, such as electricity, health care for current and retired Parent company employees and length-of-service bonuses for employees of the Bolivian company TDE. Expected costs of benefits are recognised over the term of employment of personnel using actuarial assumptions. Changes in the expected costs are taken to profit or loss when they occur. The total cost of past services is recognised immediately.

These commitments are valued by qualified independent actuaries on a yearly basis.

► Government grants and unearned income

Outright capital grants received from government agencies to finance acquisition of assets are recorded by the Group following compliance with investment requirements and assurance that the grant will be received.

The Group recognises grants under other gains in the income statement for each year over the term in which depreciation of the related assets is charged.

Unearned income received in connection with multi-year contracts or commitments are taken to net revenues or other gains on a straight-line basis over the term of the contracts or commitments.

i) Provisions

The Group makes provisions for the amount required to settle contracted or future obligations arising from past events which the Group expects to settle through an outflow of resources and which can be reasonably estimated. Provision is made when the liability or commitment is incurred.

j) Borrowings

Loans, obligations and similar commitments are initially recognised at the amount received, less costs incurred in the transaction, and subsequently measured at amortised cost using the effective interest rate method, except for hedged operations.

k) Foreign currency transactions

Foreign currency transactions are translated into Euros using the exchange rate prevailing at the date of the transaction. Differences between the value at which foreign currency balances were recorded and the exchange rate prevailing at the date of collection or payment are recognised in the income statement.

Fixed income securities and credits and debits in foreign currency at 31 December are translated to Euros at the closing exchange rate. Foreign exchange differences arising on translation are taken to exchange differences in the consolidated income statement.

Operations in foreign currency which the Group has hedged using financial derivatives or other hedging instruments are recognised as described under financial derivatives and hedging operations.

l) Financial derivatives and hedging operations

Financial derivatives are recognised initially at cost. Subsequent to initial recognition derivative financial instruments are stated at fair value. The gain or loss on remeasurement to fair value is recognised directly in profit or loss. Gains or losses from fluctuations in value of ineffective instruments are recognised in the consolidated income statement whereas recognition of derivatives designated as highly effective hedging instruments is as follows:

- Fair value hedge: the gain or loss from remeasuring the hedging instruments and the hedged item at market price are recognised under changes in value of financial instruments in the consolidated income statement.

- ▶ Cash flow hedges: the change in fair value of the effective hedging instrument is initially recognised in equity and subsequently in the income statement for the year or years in which the hedging operation is performed. The gain or loss corresponding to the ineffective portion of the derivative's change in fair value is recognised directly in the consolidated income statement.

When a hedging instrument ceases to be effective, the accumulated loss or gain under changes in value of financial instruments at that date is taken to the consolidated income statement. Changes in the fair value of a derivative subsequent to the date at which the hedge ceases to be effective, are recognised in the consolidated income statement.

The market price of different derivatives is calculated as follows:

- ▶ The fair value of derivatives quoted in official markets is measured at its closing quotation price.
- ▶ The Group values derivatives held for trading in official markets based on market conditions at year end. Specifically, the market value of interest rate swaps is calculated at the revalued market interest rate differential of the swap rate. Future exchange rate contracts are valued by discounting future cash flows calculated using the future exchange rates at year end.

m) Current and non-current borrowings

Borrowings are classified in accordance with their maturity dates at year end in the accompanying consolidated balance sheet. Borrowings are classified as current if maturing within twelve months and non-current if maturing more than twelve months from the balance sheet date.

n) Income and expenses

Income and expenses are recognised on an accrual basis, irrespective of collections and payments.

Where the Parent company acts as an agent in international exchange purchases and sales of energy are made on account of the system and the Company receives a margin for this intermediation activity, which is recorded under services rendered in the consolidated income statement.

o) Income tax

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax both current and deferred is recognised in the income statement and in determining net profit or loss for the year except if it relates to items recognised directly in equity or to a business combination.

Current tax is the estimated tax payable, on the taxable income for the year using tax rates prevailing at the balance sheet date and any adjustment to tax payable in respect of previous years.

Deductions and credits corresponding to the year are recorded as a deduction in the income tax expense, where these are expected to be applied.

Deferred tax is calculated using the liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The income tax expense is recognised using the balance sheet liability method. This method comprises the determination of deferred tax assets and liabilities for temporary differences between the carrying amount of assets and liabilities at the amounts for taxation purposes, using tax rates which are expected to come into effect when then these tax assets are realised and tax liabilities are settled.

The Red Eléctrica Group recognises deferred tax assets only to the extent that it is probable that future taxable profits will be available against which a tax asset can be realised.

p) Cash and cash equivalents

Cash and cash equivalents include cash in hand, demand deposits with banks and other short-term highly-liquid investments.

q) Dividends

Dividends on account are recorded as a reduction in equity for the year to which they correspond. Complementary dividends are not charged to equity until approval from the shareholders at their annual general meeting.

r) Earnings per share

Earnings per share are calculated on the net profit attributable to the Parent company and a weighted average number of ordinary shares outstanding during the year, excluding the average number of Parent company shares held in Group company portfolios.

s) Insurance

The Red Eléctrica Group has contracted various insurance policies to cover the risks to which its companies are subject through its activities. These risks mainly comprise damages to electrical energy plants and machinery and claims for damages from third parties which could arise from the Group's activities.

(5) PROPERTY, PLANT AND EQUIPMENT

Movements in property, plant and equipment and details of its corresponding accumulated depreciation and impairment during 2005 and 2004 are as follows:

Group Red Eléctrica

Details of Movement in Property, Plant and Equipment• at 31 December 2005 and 2004 expressed in thousands of Euros

	31 December 2003	Additions	Exchange rate fluctuations	Disposals, write-downs write-offs	Transfers
COST					
Land and buildings	44,523	-	(506)	(3,069)	65
Electrical energy plant and machinery	4,104,531	14,176	(11,675)	(926)	215,635
Other installations, machinery, fixtures and fittings and other PPE	148,438	8,518	(154)	(85,821)	(3,861)
Electrical energy plant under development	176,218	227,110	(80)	-	(207,602)
Advances and PPE under development	41,686	18,014	-	(2,629)	(4,237)
Total Cost	4,515,396	267,818	(12,415)	(92,445)	-
ACCUMULATED DEPRECIATION					
Buildings	(9,192)	(747)	168	191	-
Electrical energy plant and machinery	(1,423,890)	(180,352)	5,957	791	460
Other installations, machinery, fixtures and fittings and other PPE	(63,778)	(5,785)	114	20,222	(460)
Total accumulated depreciation	(1,496,860)	(186,884)	6,239	21,204	-
Impairment	(16,839)	-	27	16,808	-
Net total	3,001,697	80,934	(6,149)	(54,433)	-

The main investments in 2005 and 2004 have been made in the electricity transmission network in Spain. Also noteworthy in 2005 was the increase in electrical energy plants as a result of incorporation of Inalta's assets into the Group, which were fully consolidated on 15 February 2005. In 2005 electrical energy plant disposals amounted to Euros 126,079 thousand.

In 2005 companies have capitalised finance costs of Euros 3,427 thousand as an increase in property, plant and equipment (Euros 3,651 thousand at 31 December 2004).

Operating expenses directly related with construction of property, plant and equipment underway during 2005 amounted to Euros 9,805 thousand (Euros 8,753 thousand in 2004).

31 December 2004	Additions	Changes in consolidated group	Exchange rate fluctuations	Disposals, write-downs write-offs	Transfers	31 December 2005
41,013	21,017	-	1,005	(77)	1,041	63,999
4,321,741	91,301	1,101,849	22,960	(139,010)	237,252	5,636,093
67,120	3,312	-	256	(80)	19,612	90,220
195,646	374,950	-	936	(10)	(215,244)	356,278
52,834	10,751	-	187	-	(42,661)	21,111
4,678,354	501,331	1,101,849	25,344	(139,177)	-	6,167,701
(9,580)	(918)	-	(324)	77	-	(10,745)
(1,597,034)	(245,555)	(81,867)	(11,590)	12,960	-	(1,923,086)
(49,687)	(9,652)	-	(157)	61	-	(59,435)
(1,656,301)	(256,125)	(81,867)	(12,071)	13,098	-	(1,993,266)
(4)	-	-	(1)	-	-	(5)
3,022,049	245,206	1,019,982	13,272	(126,079)	-	4,174,430

Fully depreciated property, plant and equipment amounted to Euros 888,880 thousand at 31 December 2005.

In 2004 property, plant and equipment from the Company's telecommunications subsidiary was considered as held for sale non-current assets and discontinued activities and was consequently recorded as disposals of in 2004.

(6) INVESTMENT PROPERTY

Details of movements in the Group's investment property in 2005 and 2004 are as follows:

Group Red Eléctrica

Details of Movement in Investment Property • at 31 December 2005 and 2004 expressed in thousands of Euros

	31 December 2003	Additions	Exchange rate fluctuations	31 December 2004	Additions	Exchange rate fluctuations	31 December 2005
COST							
Investment property	1.606	-	(34)	1.572	2.519	69	4.160
Total Cost	1.606	-	(34)	1.572	2.519	69	4.160
ACCUMULATED DEPRECIATION							
Investment property	(331)	(35)	10	(356)	(118)	(20)	(494)
Total accumulated depreciation	(331)	(35)	10	(356)	(118)	(20)	(494)
Net total	1.275	(35)	(24)	1.216	2.401	49	3.666

Investment property has a market value of between Euros 6 million and Euros 9 million.

	31 December 2003	Additions	Exchange rate fluctuations
COST			
Research and development costs	20,970	497	-
Software	17,738	4,927	(75)
Transfer of use	31,999	-	-
Total Cost	70,707	5,424	(75)
ACCUMULATED AMORTISATION			
Research and development costs	(18,811)	(842)	-
Software	(9,117)	(1,379)	67
Total accumulated amortisation	(27,928)	(2,221)	67
Impairment	(6,657)	-	-
Net total	36,122	3,203	(8)

(7) GOODWILL

Goodwill in the consolidated balance sheet represents the difference between the cost of acquisition of the company TDE on 30 June 2002 by Red Eléctrica Internacional, S.A and the actual price paid in the operation, less accumulated amortisation until the date of transition to IFRS. Details of movement in goodwill in 2005 and 2004 are as follows:

Group Red Eléctrica

Details of Movement in Goodwill • at 31 December 2005 and 2004 • expressed in thousands of Euros

	31 December 2003	Exchange rate fluctuations	31 December 2004	Exchange rate fluctuations	31 December 2005
Goodwill	14,063	(1,023)	13,040	2,016	15,056
Total	14,063	(1,023)	13,040	2,016	15,056

The Group carried out impairment tests at 31 December 2005 and 2004, concluding that no impairment to the goodwill included in this caption was required.

(8) INTANGIBLE ASSETS

Movements in intangible assets and the corresponding accumulated amortisation and impairment in 2005 and 2004 are as follows:

Group Red Eléctrica

Details of Movement in Intangible Assets • at 31 December 2005 and 2004 expressed in thousands of Euros

Disposals, Write-downs and write-offs	31 December 2004	Additions	Changes to Consolidated Group	Exchange rate fluctuations	Disposals, Write-downs and write-offs	31 December 2005
(1,705)	19,762	418	-	-	-	20,180
(6,600)	15,990	2,078	38	203	(38)	18,271
(31,999)	-	-	-	-	-	-
(40,304)	35,752	2,496	38	203	(38)	38,451
1,519	(18,134)	(480)	-	-	-	(18,614)
1,655	(8,774)	(2,242)	(10)	(137)	12	(11,151)
3,174	(26,908)	(2,722)	(10)	(137)	12	(29,765)
6,657	-	-	-	-	-	-
(30,473)	8,844	(226)	28	66	(26)	8,686

In 2004 intangible assets from the Company's telecommunications subsidiary were considered as held-for-sale non-current assets and discontinued activities and consequently recorded as disposals in 2004.

Fully amortised intangible assets amounted to Euros 25,807 thousand at 31 December 2005.

(9) INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD

Details of investments in companies accounted for using the equity method in 2005 and 2004 are as follows:

Group Red Eléctrica

Details of Investments Accounted for by the Equity Method at 31 December 2005 and 2004 • expressed in thousands of Euros

	31 December 2003	Equity accounted method	Disposals
Equity accounted investments			
REDESUR, REDINSUR and TENEDORA DE ACCIONES DE REDESUR	6,056	558	-
Nap de las Américas-Madrid, S.A.	812	312	(1,124)
REDALTA and INALTA	(2,045)	(167)	-
	4,823	703	(1,124)

In 2005 Redalta and Inalta were fully consolidated instead of being accounted for using the equity method, after the Parent company acquired the remaining 75% of share capital in each company.

(10) INVENTORIES

Details of inventories at 31 December 2005 and 2004 are as follows:

	Thousands of Euros	
	2005	2004
Inventories	39,803	33,152
Impairment adjustments	(4,163)	(5,115)
	35,640	28,037

Conversion differences	Dividends	31 December 004	Equity accounted method	Dividends	Conversion differences	Transfer to fully consol.	31 December 2005
(139)	(260)	6,215	590	(694)	1,031	-	7,142
-	-	-	-	-	-	-	-
-	-	(2,212)	(34)	-	-	2,246	-
(139)	(260)	4,003	556	(694)	1,031	2,246	7,142

(11) CURRENT TRADE AND OTHER RECEIVABLES

Details at 31 December 2005 and 2004 are as follows:

	Thousands of Euros	
	2005	2004
Receivables	316,409	185,777
Non-current advances	31,157	8,206
Associates	76	36,655
	347,642	230,638

Receivables mainly comprise amounts pending invoicing and/or receivables in respect of the electrical energy transmission activity.

Current advances at 31 December 2005 mainly include Euros 19,877 thousand corresponding to restatements from the electrical energy import contract (note 27).

(12) EQUITY

a) Share capital

At 31 December 2005 and 2004 the share capital of the Parent company comprises 135,270,000 bearer shares of Euros 2 par value each. These shares have been fully subscribed and paid and have the same voting and profit sharing rights. The Parent company's shares have been listed on the four Spanish stock exchanges since 7 July 1999, after the public offer for their sale.

At 31 December 2005 Sociedad Estatal de Participaciones Industriales (SEPI) holds 20% of the share capital in the Parent after selling 8.5% of the share capital held in 2005 (note 3).

b) Other reserves

This caption comprises statutory reserves, including the Euros 247,022 thousand appropriated to the 1996 revaluation reserve on revaluation of value of property, plant and equipment by the Parent company.

c) Remaining reserves

▶ Retained earnings

This caption includes:

▶ Legal reserve

Companies in Spain are obliged to transfer 10% of each year's profits to a legal reserve until this reserve reaches an amount equal to 20% of share capital. This reserve is not distributable to shareholders and may only be used to offset losses if no other reserves are available. Under certain conditions it may be used to increase share capital. At 31 December 2005 and 2004 this reserve amounts to Euros 54,199 thousand.

▶ Voluntary reserves

This caption includes voluntary reserves of the Parent company, profit for the year, reserves in consolidated companies and first application reserves. All of these items are freely distributable. At 31 December 2005 and 2004 voluntary reserves amount to Euros 410,708 thousand and Euros 328,956 thousand, respectively.

▶ Own shares

At 31 December 2005 own shares held by the Parent company and subsidiaries (or by a third party acting on behalf of the Parent) comprise 0.12% of the share capital of the Parent company. This corresponds to 160,982 shares with a par value of Euros 322 thousand or an average acquisition price of Euros 23.75 per share. At 31 December 2004 the Parent company held 184,188 own shares comprising 0.14% of its share capital with a par value of Euros 368 thousand or an acquisition price of Euros 14.63 per share.

The Parent company has complied with the requirements of article 75.2 and the second additional provision of the Spanish Companies Act, which establishes that the par value of acquired shares listed on official secondary markets, together with those already held by the Parent company and its subsidiaries, must not exceed 5% of the share capital. The Company's subsidiaries do not hold own shares or shares in the Parent company.

These shares have been recognised as a decrease in equity of Euros -3,823 thousand and Euros -2,695 thousand at 31 December 2005 and 2004, respectively.

► **Cumulative translation differences**

This caption includes translation differences in respect of foreign subsidiaries (mainly the Bolivian company TDE), which at 31 December 2005 and 2004 amount to Euros 2,635 thousand and Euros -4,560 thousand, respectively.

► **Other valuation adjustments**

This caption includes variations resulting from derivative financial instruments. At 31 December 2005 and 2004 this balance totals Euros 562 thousand and Euros -2,743 thousand, respectively.

► **Interim dividends and distribution of Parent company dividends**

Interim dividends approved by the board of directors in 2005 and 2004 were netted from Group equity at 31 December 2005 and 2004, respectively.

On 24 November 2005 the board of directors of the Parent company agreed to pay a dividend on account of 2005 of Euros 0.2708 per share, which was paid on 2 January 2006 (Euros 0.2375 per share on account from the 2004 profits). At 31 December 2005 and 2004 total dividends paid amount to Euros 36,588 thousand and Euros 32,093 thousand, respectively (note 19).

The board of directors of the Parent company has also proposed to the shareholders at their annual general meeting the distribution of a complementary dividend of Euros 0.4596 per share, which would result in a total dividend for 2005 of Euros 0.7304 per share (Euros 0.6138 per share in 2004).

d) Minority interests

Minority interests recorded under equity on the accompanying consolidated balance sheet reflects the shareholding of minority interests held in the Bolivian companies TDE and Cybercia. At 31 December 2005 and 2004 these items amount to Euros 74 thousand and Euros 55 thousand, respectively.

(13) PROVISIONS

Details of provisions in 2005 and 2004 are as follows:

Group Red Eléctrica

Details of Movement in Provisions • At 31 December 2005 and 2004 • expressed in thousands of Euros

	31 December 2003	Additions	Applications	Reversals and conversion differences	31 December 2004	Additions	Applications	Reversals and conversion differences	31 December 2005
Provisions	28,295	3,891	(742)	(1,115)	30,329	5,178	(608)	(281)	34,618
Total Provisions	28,295	3,891	(742)	(1,115)	30,329	5,178	(608)	(281)	34,618

Provisions comprise annual allowances made by Group companies to cover the possibility of unfavourable rulings in respect of claims by third parties and the provision made, on the basis of actuarial studies, to cover the voluntary redundancy plan to adapt the personnel profile to the Parent company's new requirements. The collective redundancy plan 24/05 was approved by employee representatives and subsequently by the Spanish employment authorities on 13 July 2005. The vol-

untary redundancy plan is scheduled for completion on 31 December 2007 and involves a maximum of 103 employees. The main actuarial assumptions of the plan are as follows:

	Redundancy plan
Discount rate	3.50%
Cost of growth	2.50%
Survival table	PERM/F 2000

(14) OTHER NON-CURRENT LIABILITIES

Details of this caption in 2005 and 2004 are as follows:

	Thousands of Euros	
	2005	2004
Personnel obligations	30,831	23,596
Capital grants	84,116	85,381
Non-current advances	196,650	146,997
Other non-current liabilities	72	102
	311,669	256,076

Commitments with personnel reflect future obligations (medical insurance and electrical energy), which are based on actuarial studies and assumed by the Parent for its employees on their retirement, and a provision made for the company TDE to cover a long-term service bonus.

Movements in obligations with personnel in 2005 and 2004 were as follows:

Group Red Eléctrica

Details of Movement in Obligations with Personnel at 31 December 2005 and 2004 expressed in thousands of Euros

	31 December 2003	Additions	Applications	Reversals and conversion differences	31 December 2004	Additions	Applications	Reversals and conversion differences	31 December 2005
Obligations with personnel	15,124	10,445	(122)	(1,851)	23,596	7,235	(264)	264	30,831
Total obligations with personnel	15,124	10,445	(122)	(1,851)	23,596	7,235	(264)	264	30,831

Additions in 2005 are mainly a result of Royal Decree 1556/2005 which establishes electricity rates for 2006 after modification of the rates applied to current and retired employees. In 2004 this increase was the result of a review of actuarial assumptions. These additions are recognised under personnel expenses or finance costs, in accordance with their nature.

Details of the main actuarial assumptions regarding obligations with personnel of the Parent company, which amount to Euros 28,717 thousand at 31 December 2005, are as follows:

	Medical insurance	Electrical energy
Discount rate	4.35%	4.35%
Growth rate	3.50%	2.00%
Survival tables	PERM/F 2000	

Capital grants mainly include those received by the Parent company from the European Union for the construction of electrical energy plants.

Movements in capital grants in 2005 and 2004 were as follows:

Group Red Eléctrica Details of Movement in Capital Grants at 31 December 2005 and 2004 expressed in thousands of Euros

	31 December 2003	Additions	Applications	31 December 2004	Additions	Applications	31 December 2005
Capital grants	81,011	8,780	(4,410)	85,381	2,670	(3,935)	84,116
Total capital grants	81,011	8,780	(4,410)	85,381	2,670	(3,935)	84,116

Non-current advances mainly reflect the portion attributable to the Parent company of the compensation paid by EDF on the adaptation of electrical energy import contract which amounts to Euros 23,625 thousand at 31 December 2005 and 2004. This caption also includes income from the transfer of use of fibre optics contracts, mainly comprising the contract signed in 1997 between Netco Redes, S.A. (NETCO), Auna Telecomunicaciones, S.A. (previously Retevisión, S.A.) and the Parent amounting to Euros 69,385 thousand at 31 December 2005 (Euros 72,625 thousand at 31 December 2004), as well as income generated from the construction of electrical energy plants for Euros 93,826 thousand (Euros 50,597 thousand in 2004).

(15) BONDS AND OTHER MARKETABLE SECURITIES ISSUED AND BANK LOANS

Details of bonds and other marketable securities issued and bank loans at 31 December 2005 and 2004 are as follows:

	Thousands of Euros	
	31 December 2005	31 December 2004
Issues in Euros		
Long term	1,252,696	849,565
Current	75,591	105,276
	1,328,287	954,841
Bank loans in Euros		
Long term	1,213,557	716,921
Current	192,178	118,023
	1,405,735	834,944
Bank loans in other currencies		
Long term	71,271	66,164
Current	4,640	4,066
	75,911	70,230
TOTAL LONG-TERM DEBT	2,537,524	1,632,650
TOTAL CURRENT DEBT	272,409	227,365
	2,809,933	1,860,015

At 31 December 2005 accrued interest payable on these loans amounts to Euros 27,459 thousand (Euros 19,901 thousand in 2004).

At 31 December 2005 issues in Euros comprise Eurobonds of Euros 849,620 thousand issued by Red Eléctrica de España Finance, BV. in relation to the Eurobond framework programme (Euros 849,565 thousand in 2004) and Euros 403,076 thousand (US Dollars 500,000 thousand covered in Euros) obtained in 2005 from private placement issues in the United States (USPP) to cover financing requirements. At 31 December 2005 this balance also includes short-term promissory notes issued amounting to Euros 75,591 thousand (Euros 60,200 thousand in 2004).

At 31 December 2005 bank loans include a new syndicated loan, which at 31 December is drawn down in an amount of Euros 897,247 thousand (Euros 547,594 thousand in 2004 from the previous credit facility). The conditions of the previous credit facility were modified in 2005 with the credit limit increasing from Euros 700,000 thousand to Euros 900,000 thousand and maturity from 2009 to 2012, consequently reducing the margin of this operation. This caption also includes long-term loans and credit facilities totalling Euros 508,488 thousand (Euros 287,350 thousand in 2004).

Details of maturity of these issues and bank loans at 31 December 2005 are as follows:

	Thousands of Euros				
	2006	2007	2008	2009	2010 and thereafter
Issues in Euros	75,591	-	-	-	1,252,696
Bank loans in Euros	192,178	24,573	21,582	23,528	1,143,874
Bank loans in US Dollars	3,399	5,245	5,284	5,634	53,032
Bank loans in Swiss Francs	1,241	1,241	835	-	-
	272,409	31,059	27,701	29,162	2,449,602

The average interest rate in 2005 was 3.58%.

At 31 December 2005 Group companies have contracted credit facilities with a long-term credit limit available for draw down of Euros 110,000 thousand (Euros 380,000 thousand at 31 December 2004) and Euros 128,490 thousand in the short term (Euros 280,426 thousand at 31 December 2004).

At 31 December 2005 the Parent company has a Spanish Securities and Exchange Commission-registered programme to issue highly-liquid promissory notes up to a maximum of Euros 250,000 thousand (Euros 250,000 thousand at 31 December 2004).

(16) FINANCIAL RISK MANAGEMENT POLICY

The Group's financial risk management policy establishes principles and guidelines to ensure that the relevant risks which could affect the aims and activities of the Red Eléctrica Group are identified, analysed, evaluated, managed and controlled and that these processes are carried out systematically and adhering to uniform criteria.

A summary of the main guidelines which comprise this policy is as follows:

- ▶ Risk management should be fundamentally proactive and directed towards the middle and long term, taking into account possible scenarios in an ever-increasingly global environment.
- ▶ In general terms risks should be managed in accordance with coherent criteria distinguishing between the importance of the risk (probability/impact) and the investment and resources required to reduce it.
- ▶ The impact that these risks could have on the safety and quality of service of the electrical system activities should also be taken into consideration.

Financial risk management should be orientated towards the avoidance of undesired variations in the Group's base value and not towards the generation of extraordinary profits.

The Group's financial managers are responsible for managing financial risks, to ensure coherence with the Group's strategy and to coordinate the management of risk across the various Group companies, identifying the main financial risks and defining the key action to be taken, based on establishing different financial scenarios.

The methodology for identifying, measuring, monitoring and controlling risks as well as management indicators and measurement and control tools specific to each risk, is documented in the financial risk manual.

The financial risks to which the Group is exposed are as follows:

a) Market risks

Market risks reflect market variations such as prices, interest and exchange rates, credit facility conditions and other variables which could affect short, middle and long-term financial costs.

Management of these risks is carried out both on long-term liability operations, currency, maturity and interest rates and through the use of hedging instruments which allows the aforementioned financial structure to be modified.

a.1) Interest rate risks

Management of interest rate risks is mainly concentrated on maintaining a debt structure of approximately 70% fixed and protected risk, and 30% variable interest rates. The structure of debt ratio at 31 December 2005 is 68%-32%.

a.2) Exchange rate risks

Exchange rate risks basically comprise translation risks which the company is subject to on consolidation of its subsidiaries and/or assets located in countries where the functional currency is not the Euro, and to transaction risks derived from collection and payment of cash in currencies other than the Euro.

b) Credit risks

The characteristics of income from electrical energy transmission and electrical system operation activities and the solvency of the electrical system agents mean the level of risk is not relevant to the Group's principal activities.

Credit risk management for the Group's other activities is mainly carried out through the control instruments to reduce or delimit such risk.

c) Liquidity risks

Liquidity risks arise due to differences between amounts and the collection and payment dates of the different assets and liabilities of the Company.

Liquidity risks are managed by controlling the temporary financial debt structure, setting maximum net volume limits by maturity date for each defined period.

Group borrowings have an average maturity of approximately 9 years at 31 December 2005.

(17) DERIVATIVE FINANCIAL INSTRUMENTS

The Red Eléctrica Group contracts derivatives in compliance with its financial risk management policy. Details of the derivatives contracted by the Group at 31 December 2005 and 2004 are as follows:

Principal hedged	Type of hedge	Type of instrument	Amount of principal hedged	Maturity	Thousands of Euros euros	
					Fair value of hedge at 31 December 2005	Fair value of hedge at 31 December 2004
Interest and exchange rate hedge						
Bank loan in Euros	Cash flow	Interest rate swap	350,000	Until 2012	766	(2,587)
Bank loan in Euros	Cash flow	Collar	25,000	Until 2006	(53)	(228)
Bank loan in Euros	Fair value	Interest rate swap	3,005	Until 2008	140	210
Bank loan in Euros (*)	Cash flow	Collar	560,000	Until 2008	(2,673)	-
Issues in Euros	Cash flow	Cross currency swap	403,076	Until 2035	2,846	-

(*) This instrument from Inalta does not fully comply with hedging policies as the underlying asset has been refinanced.

At 31 December 2005 operations to hedge interest rate risks on borrowings of Euros 938,005 thousand (Euros 253,005 thousand at 31 December 2004) and exchange rate risks totalling US Dollars 500,000 thousand.

(18) TRADE AND OTHER PAYABLES

Details are as follows:

	Thousands of Euros	
	2005	2004
Suppliers	6,155	6,866
Creditors for services rendered	56,717	53,234
Non-current advances	22,489	23,866
Bills payable	31,816	16,820
	117,177	100,786

(19) OTHER CURRENT LIABILITIES

Details of this caption at 31 December 2005 and 2004 are as follows:

	Thousands of Euros	
	2005	2004
Other debts	10,044	10,927
Dividends payable (note 12)	36,588	32,093
Fixed asset suppliers	154,847	97,975
	201,479	140,995

(20) ASSETS AND LIABILITIES HELD FOR SALE

In 2004 assets and liabilities corresponding to the Group's telecommunications subsidiary albura were classified as held for sale. Subsequent to the sale of this company, the Company has no held-for-sale assets or liabilities in 2005.

The sale of albura in June 2005 has resulted in losses after tax of Euros 14,271 thousand from these activities in 2005 (Euros 23,463 thousand in 2004).

(21) TAXATION

The tax group of which Red Eléctrica de España, S.A. is the Parent company has filed consolidated tax returns since 2002. The tax payable is distributed among the companies forming the tax group based on the agreements established between the Group companies, adapted to the Resolutions of the Institute of Accountants and Auditors of 9 October 1997 and 15 March 2002.

Legislation applicable in their respective countries is applied to companies that do not form part of the tax group.

At 31 December 2005 the tax group includes the Parent company and Red Eléctrica Internacional (in 2004 Red Eléctrica Telecomunicaciones also formed part of the tax group).

A reconciliation of the statutory tax rate prevailing in Spain with the tax rate applied to the Group is as follows:

	Thousands of Euros	
	2005	2004
Consolidated accounting income before income tax	262,044	240,453
Permanent differences and consolidation adjustments	1,768	945
Consolidated taxable income	263,812	241,398
Tax at prevailing rate in each country	91,625	83,408
Deductions	(6,285)	(2,231)
Income tax payable	85,340	81,177

Balances payable to and receivable from public entities at 31 December are as follows:

	Thousands of Euros	
	2005	2004
Current receivable		
Tax authorities, recoverable VAT	441	528
Tax authorities, tax recoverable	1,040	402
Total current receivables	1,481	930
Current payables		
Tax authorities, VAT	1,286	3,853
Tax authorities, other payables	3,308	1,509
Tax authorities, income tax payable	26,432	19,810
Total current tax liabilities	31,026	25,172

Deferred tax assets and liabilities at 31 December 2005 and 2004 are as follows:

	Thousands of Euros	
	2005	2004
Deferred tax assets		
Retirement and personnel obligations	19,963	18,742
Grants	1,909	1,984
Loss carryforwards	4,622	-
Other	7,479	5,152
Total deferred tax assets	33,973	25,878
Deferred tax liabilities		
Accelerated amortisation and depreciation	52,391	50,072
Non-deductible assets (note 30)	97,347	-
Other	7,038	7,389
Total deferred tax liabilities	156,776	57,461

Deferred tax assets include loss carryforwards corresponding to Redalta which are estimated to be recovered.

Non-deductible deferred tax liabilities include those generated from the Redalta business combination.

Group companies also have all applicable taxes for the last four years open to inspection. Due to the different possible interpretations of tax legislation applicable to the transactions carried out by the Company, certain contingent tax liabilities could materialise as a result of this inspection. Nevertheless, the directors do not expect that these liabilities, should they materialise, would significantly affect the Group's consolidated financial statements.

(22) INCOME AND EXPENSES

a) Net sales

Details of net sales in the 2005 and 2004 consolidated income statements are as follows:

	Thousands of Euros	
	2005	2004
Provision of transmission services in Spain	781,923	625,296
Provision of transmission services in Bolivia	18,980	17,236
Provision of operating services	34,552	32,757
Other services and sales	24,708	63,541
	860,163	738,830

In Spain income from electricity transmission services rendered is fixed annually by Royal Decree.

System operation income set annually by the Royal Decree corresponds exclusively to Spain.

Other income from services rendered includes revenues generated from the diversification of the Group's activities, including transfer of the rights to use and maintenance of the telecommunications network and rendering telecommunications services, as well as consulting, engineering, construction and maintenance work performed for third parties.

b) Materials consumed and other operating expenses

Details of this caption in the 2005 and 2004 consolidated income statements are as follows:

	Thousands of Euros	
	2005	2004
Materials consumed	26,432	18,365
Other operating expenses	170,042	159,823
	196,474	178,188

Materials consumed and other operating expenses mainly comprise repair and maintenance expenses incurred in electrical energy plants (a portion of which are subcontracted to electrical energy companies) and information technology, advisory, leasing and other services.

c) Personnel expenses

Details of personnel expenses in the 2005 and 2004 consolidated income statements are as follows:

	Thousands of Euros	
	2005	2004
Wages and salaries	51,155	46,324
Social security	12,889	11,014
Pension fund contributions and similar obligations	942	862
Other welfare benefits	13,094	9,988
	78,080	68,188

Group companies have capitalised personnel expenses of Euros 7,797 thousand at 31 December 2005 and Euros 7,296 thousand at 31 December 2004.

The Group has adopted voluntary defined contribution pension plans. These pension plans have been inscribed in the Pension fund in accordance with prevailing legislation.

Current employees

The average headcount of the Group in 2005 and 2004, distributed by professional category, is as follows:

	Number of people	
	2005	2004
Management	31	29
Honours graduates	454	404
Graduates	459	407
Specialists and non-qualified technicians	411	383
	1,355	1,223

d) Net profit on disposal of non-current assets

The Euros 23,510 thousand profit corresponds mainly to the sale by the parent company of electrical energy technical installations.

(23) BALANCES AND TRANSACTIONS WITH ASSOCIATES AND RELATED PARTIES

All transactions with associates and related parties have been carried out at market prices.

Balances and transactions with associates

The main transactions carried out by fully and proportionally consolidated Group companies with equity accounted companies in 2005 and 2004 were as follows:

Group Red Eléctrica

Details of transactions with equity accounted companies

For the years ended 31 December 2005 and 2004 • expressed in thousands of Euros

	2005				2004			
	Balances		Transactions		Balances		Transactions	
	Debtors	Creditors	Expenses	Income	Debtors	Creditors	Expenses	Income
Red Eléctrica del Sur S.A. (REDESUR)	76	11	-	421	73	1	-	380
Red de Alta Tensión, S.A. (REDALTA) (*)	-	-	-	-	14,898	-	-	1,971
Infraestructuras de Alta Tensión, S.A. (INALTA) (*)	-	-	-	-	36,582	-	-	35,197
Total	76	11	-	421	51,553	1	-	37,548

(*) These became group companies in 2005 after acquisition of the remaining share capital.

Balances and transactions with related parties

In 2005 there have been no transactions and there are no balances with related parties.

(24) REMUNERATION OF MEMBERS OF THE BOARD OF DIRECTORS

In 2005 and 2004 members of the board of directors of the Parent company received total remuneration of Euros 2,269 thousand and Euros 2,321 thousand, respectively. The aforementioned amounts include estimated performance-linked bonuses and the salaries of directors who are also employees of the Group. A breakdown of remunerations in accordance with the information model introduced by the National Market Securities Commission, which was approved by Circular I of 17 March 2004 for the annual report of the corporate government is as follows:

► Remuneration from the Parent company:

	Thousands of Euros	
	2005	2004
Remuneration item:		
Fixed salary	360	417
Variable salary	1,095	1,106
Allowances	780	706
Total Remuneration	2,235	2,229

► Company directors' remuneration from directorship or senior management of other Group companies:

	Thousands of Euros	
	2005	2004
Remuneration item:		
Fixed remuneration	-	-
Variable salary	-	-
Allowances	34	92
Total Remuneration	34	92

Note: This remuneration corresponds to the telecommunications subsidiary albura, which was sold in 2005.

Total remuneration by type of director is as follows:

	Thousands of Euros			
	From Parent company		From Group	
	2005	2004	2005	2004
Type of director				
Executive	698	778	-	-
External: Major shareholder appointed	620	705	-	-
External: Independent	917	746	34	92
Total Remuneration	2,235	2,229	34	92

Total remuneration accrued by members of the board of directors of Red Eléctrica de España, S.A. in 2005, both from the Parent company and Group companies, by director, is as follows:

	Thousands of Euros				
	From the Parent company			From the Group	
	Fixed remuneration	Variable remuneration	Allowances	Allowances	Total
D. Luis M ^a Atienza Serna	360	256	82	-	698
D. Pedro Rivero Torre	-	85	107	13	205
D. Juan Gurbindo Gutiérrez ⁽¹⁾	-	85	82	-	167
D. Antonio Garamendi Lecanda	-	85	82	13	180
D. Manuel Alves Torres ⁽¹⁾	-	85	82	-	167
D. José Riva Francos	-	85	57	-	142
D. José Manuel Serra Peris	-	85	57	-	142
D. Rafael Suñol Trepas	-	85	57	-	142
Dña. María de los Ángeles Amador Millán ⁽³⁾	-	49	26	-	75
D. Francisco Javier Salas Collantes ⁽²⁾	-	43	37	-	80
D. Martín Gallego Málaga ⁽²⁾	-	43	26	-	69
D. Joaquim Clotet i Garriga ⁽²⁾	-	25	25	8	58
D. Elías Velasco García ⁽²⁾	-	42	30	-	72
D. José Ignacio Sánchez Galán ⁽²⁾	-	42	30	-	72
Total remuneration accrued	360	1,095	780	34	2,269

(1) Amounts received from Sociedad Estatal de Participaciones Industriales (SEPI)

(2) Left the board of directors in 2005

(3) Joined the board of directors of the Parent company in 2005

Executive directors' contracts contain guarantee or safeguard clauses in respect of dismissals or changes in control. These contracts have been approved by the Committee of Appointments and Remuneration and the board of directors of the Parent company.

These clauses follow usual market practice and include clauses regarding termination of employment and indemnities of up to one year, unless the applicable legislation requires a greater indemnity to be paid.

At 31 December 2005 and 2004 no loans, advances or guarantees to members of the board of directors of the Parent company are reflected in the consolidated balance sheet. Furthermore, there are no pension commitments with members of the board of directors at that date.

In 2005 the members of the board of directors of the Parent company have performed no extraordinary operations or transactions under conditions other than market, directly or through intermediaries, with the Parent company or Group companies.

Details of the interests held by the members of the board of directors of the Parent company at 31 December 2005 in the share capital of companies with a similar or complementary activity to that of Red Eléctrica de España, S.A., as well as the posts they hold and functions they perform and, where applicable, the direct or indirect performance of identical, similar or complementary activities to that of the Parent company, are included in Appendix II, in accordance with the correspondence received from the directors of the Parent company.

(25) MANAGEMENT REMUNERATION

Personnel expenses (monetary remuneration, social security, pension schemes, etc.) of senior management of the Parent company amounted to Euros 1,013 thousand in 2005 (Euros 717 thousand in 2004) and are recognised under personnel expenses in the accompanying consolidated income statement.

A list of senior management of the Parent company in 2005 has been prepared exclusively for this document, independently of their legal relationship with the Company:

Name	Position
Carlos Collantes Pérez-Ardá	General Manager of Transmission
Esther M ^a Rituerto Martínez	General Manager of Administration and Finance
Alberto Carbajo Josa	General Manager of Operations
Ángel Landa López de Ocariz	Assistant General Manager

No loans or advances have been paid to senior management at 31 December 2005 and 2004.

Senior management contracts contain guarantee or safeguard clauses in respect of dismissals. These contracts have been approved by the Committee of Appointments and Remuneration and the board of directors of the Parent company.

Two senior managers are affected by these contracts. The clauses of the contracts follow usual market practice and include clauses regarding termination of employment and indemnities of up to one year, unless the applicable legislation requires a greater indemnity to be paid.

(26) SEGMENT REPORTING

The main activity of the Red Eléctrica Group is the transmission of electrical energy in Spain, which represents 91% of Group's consolidated net sales and over 97% of its total assets. Other activities, System Operation, other electrical activities in Spain and consultancy and electrical activities outside Spain comprise the remaining 9% of consolidated net sales and reflect less than 3% of the Parent company's assets. Consequently, as these segments do not reach the levels established by IFRS, no segment reporting breakdown has been prepared.

(27) GUARANTEES AND OTHER OBLIGATIONS WITH THIRD PARTIES AND OTHER CONTINGENT LIABILITIES

At 31 December 2005 the Group is party to certain long-term contracts and obligations, as follows:

- ▶ Contracts between EDF and the Parent company for the import and export of electrical energy until 2010. The power quotas established in these two contracts range from 550 to 300 MW.
- ▶ A contract entered into in 1997 between the Company, Netco Redes, S.A. (NETCO) and Auna Telecomunicaciones, S.A. (formerly Retevisión, S.A) for the transfer of use of the telecommunications network. Subsequent to the sale of Red Eléctrica Telecomunicaciones, S.A.U in 2005, the Parent reacquired the management and maintenance activity of these assets, which had previously been transferred to this company.
- ▶ A contract signed in June 2005 for the transfer of rights of use of fibre optics from the Parent company to albura Telecomunicaciones, S.A. (formerly Red Eléctrica Telecomunicaciones, S.A.U.) which expires in 2016.

(28) ENVIRONMENTAL ISSUES

During 2005 Group companies incurred ordinary expenses of Euros 5,891 thousand to protect and improve the environment (Euros 4,916 thousand in 2004). These expenses mainly relate to the introduction of preventative and corrective measures in the Parent's installations, the protection of bird life and vegetation, waste and pollution management and the organisational unit within the Parent responsible for such tasks, various environmental communication and training activities and environmental research and preparation of a electromagnetic field and noise measurement plan in the Company's installations.

In 2005 the Parent company also performed environmental impact and supervision studies in relation to its new electricity installations. Costs incurred on these studies amounted to approximately Euros 2,080 thousand (approximately Euros 1,704 thousand in 2004), which were added to the value of property, plant and equipment.

Group companies have no litigation or contingencies relating to environmental protection or improvements.

(29) OTHER INFORMATION

The auditor of the accounts of the Group companies is KPMG Auditores, S.L. Accrued remuneration related to the 2005 audit amounts to approximately Euros 102 thousand (Euros 82 thousand in 2004). Remunerations accrued by companies directly and indirectly related to the auditors for professional services other than the audit of the accounts, which do not affect the Group companies' strategy or general planning, amount to approximately Euros 79 thousand in 2005 (Euros 50 thousand in 2004).

(30) BUSINESS COMBINATIONS

On 15 February 2005 the Parent acquired 75% of the share capital in Redalta and Inalta. Consequently, both companies became fully consolidated. Since that date net sales contributed by these companies in 2005 amounted to Euros 107.6 million. If the acquisition had taken place on 1 January, net sales would have been Euros 122.8 million.

Details of the fair value of the main assets and liabilities contributed by these companies on the date of acquisition are as follows:

	Millions of Euros
Property, plant and equipment	1,020
Borrowings	-592
Other long-term debt	-40
Other assets and liabilities	-158
Cash in hand and at banks	17
	247

(31) SUBSEQUENT EVENTS

No significant events have occurred subsequent to formulation of these consolidated financial statements at 31 December 2005 in any of the Group companies.

(32) EARNINGS PER SHARE

Details of basic earnings per share in 2005 and 2004 are as follows:

	2005	2004
Net profit (thousands of Euros)	162,422	135,806
Number of shares (shares)	135,270,000	135,270,000
Average number of own shares in portfolio (shares)	272,626	267,399
Earnings per share (Euros)	1.20	1.01
Diluted earnings per share (Euros)	1.20	1.01

At 31 December 2005 and 2004 the Group has not performed any operations which would result in any difference arising between basic earnings per share and diluted earnings per share

(33) TRANSITION FROM SPANISH GAAP TO IFRS

First-time adoption of IFRS

The Company has taken into account IFRS I First time adoption of IFRS in the preparation of the accompanying consolidated financial statements. The Red Eléctrica Group has opted to apply the following exceptions to the retrospective application of IFRS included in IFRS I:

- ▶ The cost of property, plant and equipment includes revaluations carried out as permitted by pertinent legislation.
- ▶ Business combinations prior to the date of transition to IFRS have not been restated. Consequently, goodwill has been calculated in accordance with the previous criteria.
- ▶ Translation differences from prior years have been transferred to other reserves.

Group Red Eléctrica

Reconciliation of Equity (Spanish GAAP-IFRS) • at 1 January 2004 and 31 December 2004 expressed in thousands of Euros

	1 January 2004	31 December 2004 (*)
EQUITY SPANISH GAAP	849,099	895,825
ADJUSTMENTS SPANISH GAAP - IFRS		
A) Impairment of telecommunications business	(14,495)	(12,467)
B) Goodwill	(3,744)	(3,405)
C) Establishment costs	(2,663)	(1,530)
D) Own shares	(1,551)	(1,218)
E) Financial instruments	3,634	318
F) Exchange gains	(1,088)	(1,373)
G) Minority interests	55	55
H) Accelerated depreciation	(4,816)	-
EQUITY IFRS	824,431	876,205
(*) Includes details of effects of 2004 profits as follows:		

	31 December 2004 (*)
PROFIT UNDER SPANISH GAAP	132,381
ADJUSTMENTS SPANISH GAAP - IFRS	
A) Impairment of telecommunications business	2,028
B) Amortisation of goodwill	1,362
C) Establishment costs	1,133
D) Own shares	(753)
E) Financial instruments	(573)
F) Exchange gains	228
PROFIT IFRS	135,806

Main differences between Spanish GAAP and IFRS

The main differences between Spanish GAAP and IFRS applicable to the Red Eléctrica Group are as follows:

a) Impairment of telecommunications business

In accordance with Spanish GAAP, the Company was required to make the necessary adjustments to tangible and intangible assets which exceeded their market value at year end, providing that the asset's carrying amount was not recoverable through generation of sufficient income to cover costs and expenses, including amortisation and depreciation. Furthermore, the calculation of impairment under IFRS is far more rigorous than under Spanish GAAP.

IFRS also introduces the concept of cash generating unit in calculating this recoverable value. Company management considers the telecommunications network as a whole to be the cash generating unit and has consequently discounted cash

flows based on forecast income and expenses in the future and where the discount rates applied have been based on a combination of share capital costs, which includes a sector discount premium and estimated debt costs.

The difference in equity resulting from the impairment calculation through application of the two accounting principles, net of tax, amounts to Euros 14,495 thousand at 1 January 2004 and Euros 12,467 thousand at 31 December 2004. The difference in profits for 2004 is a result of the Euros 2,028 thousand variation from application of the two accounting principles.

b) Goodwill

The Red Eléctrica Group has opted to apply the exemption to retrospective application of business combinations as established in IFRS 1. Consequently, goodwill is recorded in accordance with the previous accounting principles. Nevertheless, the difference in equity arising from application of both accounting standards is because goodwill under IFRS is recognised in the original currency. Consequently goodwill is reduced by Euros 3,744 thousand at 1 January 2004 and Euros 4,767 thousand at 31 December 2004 under IFRS compared to under Spanish GAAP. The impact on equity in 2004 is offset by an amount of Euros 1,362 thousand because goodwill is not amortised under IFRS.

c) Establishment costs

Spanish GAAP allows establishment costs, incorporation and share capital increase costs to be capitalised. Under IFRS these costs do not comply with the definition for intangible assets and therefore must be treated as expenses in the year in which they are incurred. There is a difference in equity resulting from the application of the two accounting principles of Euros 2,663 thousand at 1 January 2004 and Euros 1,530 thousand at 31 December 2004. The Euros 1,133 thousand variation between the two years has impacted on the profits for 2004.

d) Own shares

Under Spanish GAAP, own shares are recognised as assets except for those acquired through the redemption of share capital. Own shares under IFRS are recognised at cost of acquisition at par value per share as a reduction in equity. Profit and loss on redemption of own shares is recorded directly as a credit or debit to equity without being recognised on the income statement, as required by Spanish GAAP. Equity under IFRS is Euros 1,551 thousand lower at 31 December 2003 and Euros 1,218 thousand lower at 31 December 2004. The difference between the two results is due to profit and loss on redemption of own shares being recognised directly in equity.

e) Financial instruments

The Group uses certain financial derivatives to reduce its exposure to interest rate and exchange rate fluctuations. Under Spanish GAAP, derivatives are stated at the lower of cost or market. IFRS establishes that all derivatives, including hedging and non-hedging instruments are recognised at fair value, which is the market price for unquoted instruments. At 1 January 2004 the Group has carried out an analysis and valuation of existing hedging instruments, and has recognised the resulting increase in financial assets and liabilities as a Euros 3,618 thousand reduction in equity. Other instruments are also recognised differently under IFRS with the different treatment of financial instruments at the date of transition to IFRS resulting in a reduction in equity of Euro 3,634 thousand at 1 January 2004. At 31 December 2004 the effect on equity amounted to Euros 318 thousand. The impact on 2004 profits amounted to Euros 573 thousand, mainly due to the different treatments of loan arrangement commissions, which under Spanish GAAP are taken to profit and loss whereas under IFRS are deferred over the life of the loan.

f) Exchange gains

Under IFRS, translation differences should be recognised as income in the year that they are generated, except for those arising from non-current liabilities which should be considered in the financial statements as components of net equity until disposal of the investment, at which point they are recognised as income. The tax effect of translation gains which are considered as translation differences to hedge the investment in TDE, should be discounted under IFRS. The impact

of these differences at 1 January 2004 has resulted in a reduction in equity of Euros 1,088 thousand and a Euros 1,373 thousand decrease in equity at 31 December 2004. The variation in the 2004 profit for this item through application of both accounting standards amounts to Euros 228 thousand.

g) **Minority interests**

Under prevailing Spanish GAAP, minority interests are not classified within equity, as they are under IFRS. At 1 January 2004 and 31 December 2004 Euros 55 thousand of minority interests has been reclassified under net equity.

h) **Accelerated depreciation**

Applying the dispositions contained in Royal Decree Law 2 of 1985, Red Eléctrica made a capital allowance prior to 1990. This reserve was reduced annually with a charge to extraordinary income for amortisation and depreciation corresponding to the related fixed assets. Under IFRS at 1 January 2004 this reserve was reduced by Euros 4,816 thousand. At 31 December 2004 the Parent applied the same criteria under IFRS as under Spanish GAAP and consequently no difference has arisen.

Group Red Eléctrica
Details of shareholdings at 31 December 2005 • expressed in thousands of Euros

Appendix I

Company - Registered offices - - Principal activity	Percentage Ownership of the Parent company		Net book value of Company holding the interest
	Direct	Indirect	
A) FULLY CONSOLIDATED COMPANIES			
Red Eléctrica Internacional, S.A.U.	100%	-	60,000
- Paseo Conde de los Gaitanes, 177. Alcobendas (Madrid)			
- International shareholdings. Provision of consultancy, engineering and construction services. Electrical activities outside the Spanish electrical system.			
Transportadora de Electricidad, S.A. (TDE)	-	99.94% (1)	88,783
- C/ Colombia, N° 00655, casilla, N° 640. Cochabamba (Bolivia)			
- Transmission of electrical energy.			
Cybercia, S.R.L.	-	67% (4)	31
- C/ Colombia, N° 00655, casilla, N° 640. Cochabamba (Bolivia)			
- General service and commercial activities.			
Red Eléctrica de España Finance, B.V.	100%	-	2,000
- Amsteldijk, 166. Amsterdam (Holanda)			
- Financing activities.			
Red de Alta Tensión, S.A.U. (REDALTA)	100%	-	189,387
- Paseo Conde de los Gaitanes, 177. Alcobendas (Madrid)			
- Holding, management and administration of Inalta shares.			
Infraestructuras de Alta Tensión, S.A.U. (INALTA)	-	100% (5)	59,718
- Paseo Conde de los Gaitanes, 177. Alcobendas (Madrid)			
- Electrical energy transmission.			
Red Eléctrica Andina, S.A.C. (REA)	-	100% (1)	3
- Juan de la Fuente, 453. Lima (Perú).			
- International shareholdings. Provision of consultancy, engineering and construction services. Electrical activities outside the Spanish electrical system.			
B) SOCIEDADES CONSOLIDADAS POR EL MÉTODO DE PARTICIPACIÓN			
Red Eléctrica del Sur, S.A. (REDESUR)	-	30% (2)	4,597
- Juan de la Fuente, 453. Lima (Perú).			
- Electrical energy transmission.			
Tenedora de Acciones de Redesur, S.A.	-	8.33% (1)	877
- Paseo Conde de los Gaitanes, 177. Alcobendas (Madrid)			
- Holding, management and administration of REDESUR shares.			
Red Internacional de Comunicaciones del Sur, S.A. (REDINSUR)	-	24.57% (3)	70
- Juan de la Fuente, 453. Lima (Perú).			
- Telecommunications			

(1) Shareholding through Red Eléctrica Internacional

(2) Shareholding through Red Eléctrica Internacional (25%) and shares held in

(3) Shareholding through Redesur

(4) Shareholding through TDE

(5) Shareholding through Redalta

This appendix forms an integral part of note I to the consolidated financial statements.

Information on Members of the Board of Directors of the Parent Company at 31 December 2005

Members of the Board of Directors	Direct or indirect interests held by Members of the Board of Directors of the Parent company in the share capital of companies with a similar or complementary activity to that of the Parent company	Positions held and functions performed by Members of the Board of Directors of the Parent company in companies outside the Red Eléctric Group with an identical, similar or complementary statutory activity to that of the Parent company
Mr. Luis M ^a Atienza Serna	-	-
Mr. Pedro Rivero Torre	-	Director of the Iberian Energy Market Operator – Polo Español, S.A.
Mr. Juan Gurbindo Gutiérrez	-	-
Mr. Antonio Garamendi Lecanda	-	-
Mr. Manuel Alves Torres	-	-
Mr. José Riva Francos	853 shares in Iberdrola, S.A.	-
Mr. José Manuel Serra Peris	3,232 shares in Endesa, S.A. 3,932 shares in Iberdrola, S.A. 3,254 shares in Gas Natural, S.A.	-
Mr. Rafael Suñol Trepas	-	-
Ms. María de los Ángeles Amador Millán	-	-
Mr. Francisco Javier Salas Collantes	-	-
Mr. Martín Gallego Málaga	1,215 shares in Endesa, S.A.	-

Consolidated directors' report

2005

BUSINESS PERFORMANCE. SIGNIFICANT EVENTS

In 2005 the RED ELÉCTRICA GROUP completed its mission to become the Spanish TSO (Transmission and Systems Operator) through the acquisition of the remaining 75% of share capital of REDALTA, a company which owned the former transmission assets of Iberdrola, and also through the purchase of transmission assets from Viesgo. Growth in this area, together with the divestment of its telecommunications activity after the sale of albura, has allowed the Group to concentrate its efforts on developing its principal TSO activity.

Electrical energy system service in 2005 was excellent with the company providing a guaranteed and environmentally sustainable service of the highest quality, which has contributed to an overall strengthening of the energy sector.

The ability of the Spanish transmission network to adapt to continual increases in demand as well as its high operational efficiency and availability levels has resulted in RED ELÉCTRICA, (the GROUP's Parent company) becoming a global reference in the sector. The business management model developed by the GROUP has not only achieved economic growth but has received explicit recognition on several different levels:

- ▶ The considerable increase in share price in line with evolution of the stock-market.
- ▶ The incorporation of RED ELÉCTRICA GROUP in the Dow Jones STOXX Sustainability corporate responsibility index in recognition of its ethical and social management model.
- ▶ Maintenance of the GROUP's strong credit rating (among the highest in the sector), subsequent to the debt refinancing process carried out.
- ▶ The Crown Prince Felipe Excellence in Business Award for Industrial Quality, which is a tribute to the twenty years of effort by RED ELÉCTRICA in developing a modern and competitive business model.

These achievements are testament to the strength and prestige of the Group, which has been attained through a coordinated human approach that is fully integrated into the business project.

Positive interaction between the different interested parties (shareholders and investors, social agents, the media, suppliers, etc.) and the electrical system agents has contributed immensely to the success of the RED ELÉCTRICA GROUP.

Electricity Transmission Activity in Spain

RED ELÉCTRICA GROUP, through RED ELÉCTRICA and INALTA, has continued to make considerable investment in the Spanish transmission grid to guarantee the system's required flexibility and reliability. This ambitious plan has seen record investment of Euros 420.2 million made in the Group's transmission grid (up 73% on 2004). Furthermore, Euros 45.1 million was earmarked for the acquisition of transmission assets from Viesgo Distribución and Euros 247.3 million was paid for the remaining 75% of share capital in REDALTA, which owned the transmission assets of Iberdrola through its subsidiary INALTA. As a result of these investments RED ELÉCTRICA GROUP owns practically the entire Spanish mainland's transmission grid.

In 2005 the network grew by 38 km of lines and 104 new substations. Transmission capacity was also increased on 457 km of the existing lines. Of the considerable number of RED ELÉCTRICA GROUP projects underway, the most noteworthy have had the following objectives:

- ▶ To improve the transmission infrastructure in Andalusia and South-east Spain to incorporate the latest technological advances into the network.
- ▶ To increase the interconnection capacity with the Moroccan transmission grid through the installation of a second submarine circuit cable across the Gibraltar straits.
- ▶ To reinforce the electricity ring around Madrid and the central, north-east and north-west Spanish mainland areas.
- ▶ To develop the Cantabrian axis thereby increasing transmission to the energy-isolated areas of Galicia and Asturias and allow excess power to supply areas with energy shortages.
- ▶ To develop the necessary infrastructures for new high speed trains.

Furthermore, RED ELÉCTRICA, in collaboration with Rede Eléctrica Nacional (REN), took further steps to develop a new 400 kV interconnection axis, near Duero, linking Spain and Portugal and a cross-border corridor between France and Spain, to the east of the Pyrenees, in conjunction with Réseau de Transport d'Électricité (RTE) in 2005.

Electricity System Operation in Spain

In its capacity as System operator, the Parent company RED ELÉCTRICA has collaborated with both electricity system agents and the Spanish Ministry of Industry, Tourism and Trade in a review of transmission grid planning contained in the document "Electricity and Gas Sector Planning: Transmission Grid Development 2002-2011" to guarantee the mid and long-term electricity supply and to meet the demand of future generations.

RED ELÉCTRICA has also forecast middle and long-term electricity demand as well as the electricity required to cover the demand between 2005-2015. These forecasts take into account the expected increase in energy generation from renewable sources considered in the Spanish government plan to promote these types of energy.

RED ELÉCTRICA has maintained its leading position in the Spanish market despite being faced with continual increases in demand on the Spanish mainland, reflected by historically high electricity demands being registered in both winter and summer for a number of years (which grew 4.8% on 2004). In terms of guaranteeing electricity supplies, the total availability through RED ELÉCTRICA's grid, including INALTA, was 98.28% whereas average supply cuts totalled only 1.078 minutes.

In its capacity as system operator, RED ELÉCTRICA manages operating markets, adapting the resulting production programmes to supply guarantee and quality requirements of the system. The effect of this activity on the final average energy price amounted to €2.38/MWh from a total of €62.41/MWh.

RED ELÉCTRICA has undertaken to provide the first training course of its kind in Spain for electricity system operation specialists in conjunction with the ICAI Higher Engineering Technical College, in order to guarantee the quality of electricity system operations in the future.

Other Electrical Activities in Spain

The electricity exchange programmes had an export balance for the second year running, which amounted to 1,339 GWh in 2005, due to the growth in export programmes to Portugal. Regarding the international electricity agreements entered into by RED ELÉCTRICA, the electricity supply contract with Electricité de France (EDF) had an average utilisation rate of 87% in 2005 - almost half the total volume of domestic import programmes.

International Electricity Activities

GRUPO RED ELÉCTRICA international activity is carried out through RED ELÉCTRICA INTERNACIONAL, which has investments in Latin America, Bolivia (through TDE) and Peru (through REDESUR) and consultancy work and technical assistance to third parties as part of the GROUP's international expansion plan.

Net sales relating to the international activity total Euros 22 million, while net profits amount to Euros 4 million.

TDE carried out construction work on new transmission infrastructures in Bolivia amounting to US Dollars 8.5 million. New plant and machinery totalling US Dollars 20.8 million also entered service in 2005.

Both REDESUR in Peru and TDE in Bolivia have performed work on their electrical systems from which operating and maintenance standards of the highest quality in their installations have been achieved. This has resulted in availability levels of over 99%.

In 2005 consultancy and technical assistance projects were completed in Serbia and Montenegro, Italy, Morocco, Libya, Algeria and Peru, with other projects still in progress in Bolivia, Libya, Romania, Hungary, Morocco, Ecuador and South-east Europe.

TDE and REDESUR have added value to the GROUP after distributing dividends of US Dollars 2.7 million and US Dollars 0.8 million, respectively.

CORPORATE RESPONSIBILITY

The commitment to ethical and responsible management of environment, of personnel and of the Company has resulted in RED ELÉCTRICA GROUP being listed in the Dow Jones STOXX Sustainability Indexes in 2005. This corporate responsibility model includes the following benchmarks:

Corporate Governance

The RED ELÉCTRICA GROUP has shown itself to be at the leading edge of corporate governance by introducing an electronic voting system and enhancing open and fluid dialogue with shareholders to provide them with all available information at the same time as other stock or financial market agents.

The 2004 annual report on corporate government was published in 2005 and included best company practice which far exceeded the established legal requirements on this matter.

Risk management

The GROUP has established a Risk Control System covering all activities, which is adapted to its risk profile. Risk Policy and Internal Risk Control and General Management Procedures are based on the enterprise risk management integrated framework outlined in the Committee of Sponsoring Organisations (COSO II) report.

The main risks identified in achieving the strategic objectives comprise the regulations to which the main business lines of the GROUP are subject, operations mainly relating to electrical system servicing activities, financial risks described in note 16 to the consolidated financial statements (including market, loan or counter party or liquidity risks) and environmental risks. In 2005 no relevant risk has materialised.

Environment

RED ELÉCTRICA GROUP has continued to meet the challenge of incorporating environmental protection into the efficient operation of its infrastructures. All projects are carried out under the strictest environmental criteria (eco-efficiency, environmental vigilance, conservation and waste and consumption management etc.) and integrated into the community with the greatest social consensus possible.

The RED ELÉCTRICA GROUP has carried out numerous environmental activities to avoid or reduce environmental impact in accordance with its environmental policy. In 2005 it carried out environmental impact studies for all new installation projects. RED ELÉCTRICA has also participated in a number of environmental studies and research projects and has collaborated with various public entities through environmental protection agreements, especially regarding the protection of birdlife.

Research, Development and Innovation (R+D+I)

As testament to its talent and technical awareness and as part of its research, development and innovation activities the RED ELÉCTRICA became the first transmission company in the world to have geographically referenced positioning by satellite for all of its installations. This system has improved asset management capacity consequently improving domestic electrical system reliability.

Of the projects undertaken in 2005, those relating to integration of renewable energy systems and development of energy distributed in the Spanish transmission grid are noteworthy. Work lines have focussed on wind-power options and analysing the stability and dynamic performance of the transmission grid.

GROUP companies participate in research and development projects financed through European funds within the VI framework Programme. In 2005 two integrated project contracts were signed with the European Union: FENIX, in respect of WIND ON THE GRID, to integrate wind-power into the network and RELIANCE, to identify and plan the R&D&I needs of European TSOs.

The Group has also disseminated an extensive amount of environmental information through publications and manuals and through the establishment of collaboration and experience exchange agreements in a number of international organisations such as CIGRÉ, AENOR and EURELECTRIC.

Quality and operating excellence

In 2005 the RED ELÉCTRICA GROUP received the Crown Prince Felipe Excellence in Business Award for Industrial Quality in recognition of its management qualities. It was also re-awarded the Gold Seal by the Excellency Club for Management, the representative in Spain of the European Foundation for Quality Management.

All internal processes of the different companies are subject to a continual review and verification process and are orientated towards continual improvement of quality management, which contributes to mitigating risks derived from our activities. An example of this in 2005 was the award of the triple integrated quality, environmental and health and safety certificate in accordance with the standards ISO9001, ISO14001 and OHSAS18001 to RED ELÉCTRICA as non-mainland based system operator, (Canaries, Balearic Islands, Ceuta and Melilla).

Personnel

RED ELÉCTRICA GROUP has made corporate employee integration a priority in 2005. The strategy adopted for this has been directed towards promoting the growth of talent and is reflected in ambitious training courses of over 80,000 hours, the Operations College opened, an integration in business culture programme for new employees and the strengthening of internal communication through knowledge forums in the organisation.

The award of the Social Accountability SA8000 certificate demonstrates the RED ELÉCTRICA commitment to an appropriate social management model which is totally integrated with labour rights and management of the company.

The RED ELÉCTRICA GROUP closed 2005 with a headcount of 1,401 people.

ECONOMIC RESULTS AND STOCK-MARKET EVOLUTION

The figures for 2005 were affected by the following:

- ▶ The incorporation of INALTA's accounts into the accounts of RED ELÉCTRICA GROUP, which was effective on 15 February 2005. INALTA controls assets which previously belonged to Iberdrola.
- ▶ The sale of 100% of the share capital of Red Eléctrica Telecomunicaciones, S.A.U. (albura) to T-Online Internacional, A.G. on 30 June 2005.
- ▶ The materialisation of the sale and purchase of transmission assets agreement with Unión Fenosa.
- ▶ The incorporation of transmission assets from Viesgo.

In 2005 net sales amounted to Euros 860.2 million, which reflects an increase of 16.4% on the previous year. This rise was mainly due to the inclusion of Euros 107.6 million attributable to the transmission assets of INALTA during ten and a half months of the year; growth in income from the transmission activity mainly as a result of RED ELÉCTRICA installations which entered service in 2004 and assets acquired in 2005. There was a drop in income from engineering and construction work carried out for third parties.

Consolidated operating expenses rose 11.4% in 2005, amounting to Euros 274.6 million compared to Euros 246.4 million in 2004. This increase was mainly due to extra maintenance costs incurred on INALTA assets, expenses incurred in integrating assets into the electrical energy companies and higher personnel expenses as a result of the new appointments in the Parent company. These expenses were offset by the lower costs incurred in engineering and construction work.

The GROUP's average headcount grew 10.8% and totalled 1,355 employees at 31 December 2005. This increase reflects personnel appointed in the Parent company to integrate the transmission assets acquired and to render new system operation services.

The number of personnel of the group at year end amounted to 1,401 employees compared to 1,286 employees at 31 December 2004.

Amortization and depreciation amounted to Euros 259.0 million, compared to Euros 189.1 million in the prior year. The rise in amortisation and depreciation was mainly due to the incorporation of transmission grid assets from Inalta, new installations which entered service during the year and changes in the useful life of assets in 2005. This increase was partially offset by certain installations reaching the end of their useful lives and the amortisation and depreciation which was written off as a result of assets sold to Unión Fenosa.

Consolidated net operating profits (EBIT) amounted to Euros 332.2 million, reflecting an 8.1% rise on 2004.

Consolidated losses on financial operations amounted to Euros 104.1 million compared to Euros 73.2 million in 2004. This increase was mainly due to financial expenses incurred on the acquisition of 75% of the share capital in REDALTA.

Profit on disposal of non-current fixed assets amounted to Euros 23.5 million, which mainly comprised assets sold to Unión Fenosa.

Profits before tax on continuing activities were up 9.0% on the prior year and totalled Euros 262.0 million.

Profit after tax on continuing operations amounted to Euros 176.7 million, which was a 10.9% rise on 2004. The tax rate was 32.6% compared to 33.8% in the prior year.

Losses after tax on discontinued activities amounted to Euros 14.3 million. This figure includes losses attributable to albura until 30 June and losses from the sale of 100% of the share capital in this company.

Profits after tax amounted to Euros 162.4 million compared to Euros 135.8 million in 2004, representing an increase of 19.6%.

Cash-flow was up 22.5 % to Euros 429.6 million in 2005 compared to Euros 350.6 million in 2004.

Consolidated investments amounted to Euros 755.5 million (including Euros 247.3 million reflecting the 75% of share capital in REDALTA) compared to Euros 274.6 million in the prior year.

As a result of these acquisitions, net financial debt increased Euros 945.3 million to Euros 2,791.1 million at 31 December 2005. Despite this increase, the credit rating agencies Moody's and Standard & Poor's maintained their credit ratings of A2 and AA, respectively, subsequent to an analysis of the 75% acquisition of share capital in REDALTA.

Stock-market evolution and shareholder returns

The market capitalisation of RED ELÉCTRICA at the 2005 close was Euros 3,539 million. The RED ELÉCTRICA share price rose considerably in 2005 and closed the year at Euros 26.16 per share, 58.5% up on the prior year. The Company was reintegrated into the IBEX-35 in June 2005 and saw its share price close the year well above the 18.2% average of this market.

Free-float share capital also increased in 2005 mainly as a result of the divestments of SEPI from 28.5% to 20% of share capital and the shareholder Hidroeléctrica del Cantábrico, which held 3% of share capital.

RED ELÉCTRICA also maintained its commitment to maximise value for its shareholders and offered high returns per dividend in 2005.

OWN SHARES

At the annual general meeting held on 26 May 2005, the shareholders authorised the board of directors to acquire RED ELÉCTRICA shares, as permitted by the Spanish Companies' Act.

In order to provide investors with adequate levels of liquidity the Company acquired 5,390,029 shares with a total par value of Euros 11 million and cash of Euros 110 million in 2005. Consequently, 5,413,235 shares with a total par value of Euros 11 million were redeemed, plus cash of Euros 109 million was generated.

At 31 December 2005 own shares held by RED ELÉCTRICA represent 0.12% of share capital and total 160,982 shares. These shares have a global par value of Euros 0.3 million and a market value of Euros 4 million.

RED ELÉCTRICA has complied with the requirements of article 75.2 and the second additional provision of the Spanish Companies Act, which establishes that the par value of acquired shares listed on official secondary markets, together with those already held by the GROUP must not exceed 5% of the share capital. The remaining GROUP companies hold no own shares or shares in RED ELÉCTRICA.

OUTLOOK

In the next few years the RED ELÉCTRICA GROUP will concentrate its efforts in RED ELÉCTRICA, focussing on the strategy to provide a quality service as Spanish TSO and maintain the leading position of our system in terms of reliability and guaranteed supply.

The RED ELÉCTRICA GROUP will make the necessary investments to meet the expected increases in demand for electricity in Spain, by developing an ambitious investment plan for the transmission grid which will focus mainly on wind power and combined cycles. It will also support the expansion of the high-speed train network, consolidate its international interconnections and reinforce the system's reliability. To promote the development of its new infrastructures, RED ELÉCTRICA will continue to play an active role within the Spanish electrical energy sector so that growth is appropriate and carried out in a clearly regulated environment. Future investments are also to be analysed using a strict creation of value for the shareholder criteria.

Operating margins should continue to rise through increased production efficiency resulting from the integration of the acquired assets and economies of scale as a result of the greater dimensions. Commitments to maintain an efficient capital structure in line with the best sector practice will also allow RED ELÉCTRICA GROUP to offer low-risk high returns to its shareholders.

Individual Financial Statements • Red Eléctrica de España, S.A.
Balance Sheet 2004 and 2005 at 31 December • In thousands of Euros

ASSETS	2005	2004
INTANGIBLE ASSETS	8.246	8.369
Research and development expenses	20.180	19.762
Software	16.662	14.675
Amortisation	(28.596)	(26.068)
TANGLIBLE ASSETS	3.067.235	2.935.695
Land and buildings	59.646	35.640
Plant and machinery	4.328.191	4.200.606
Other installations, equipment and furniture	87.887	65.478
Plant and machinery under construction	347.355	189.728
Advances and tangible assets under construction	20.625	51.619
Provisions	(29.261)	(27.399)
Depreciation of plant and machinery	(1.680.431)	(1.523.456)
Other depreciation	(66.777)	(56.521)
INVESTMENTS	755.376	170.326
Investments in group companies	267.518	212.000
Loans to group companies	480.375	-
Investments in associated companies	-	3.732
Loans to associated companies	-	14.867
Other loans	1.719	2.326
Long-term guarantee deposits	323	182
Logn-term balances recoverable from public entitie	21.572	20.474
Provisions	(16.131)	(83.255)
OWN SHARES	1.133	1.218
TOTAL FIXED ASSETS	3.831.990	3.115.608
DEFERRED EXPENSES	17.880	15.972
STOCKS	35.571	27.978
Raw materials and other supplies	39.735	33.093
Provisions	(4.164)	(5.115)
DEBTORS	277.808	225.418
Trade debtors	14.261	15.636
Group companies	5.405	293
Associated companies	70	36.644
Sundry debtors	254.505	170.265
Personnel	811	914
Public entities	2.814	1.748
Provisions	(58)	(82)
SHORT-TERM INVESTORS	253.607	1.224
Loans to group companies	247.830	-
Loans to associated companies	-	31
Other loans	5.541	1.193
Short-term guarantee and deposits	236	-
CASH AND BANKS	4.861	307
PREPAID EXPENSES	21.652	2.323
TOTAL CURRENT ASSETS	593.499	257.250
TOTAL ASSETS	4.443.369	3.388.830

SHAREHOLDERS' EQUITY AND LIABILITIES	2005	2004
SHARE CAPITAL	270.540	270.540
REVALUATION RESERVE	247.022	247.022
RESERVES	325.572	282.435
PROFIT FOR THE YEAR	145.800	127.235
INTERIM DIVIDEND	(36.588)	(32.093)
TOTAL SHAREHOLDERS' EQUITY	952.346	895.139
Capital grants	84.116	85.381
Exchange gains	233	288
Other deferred income	181.225	161.367
TOTAL DEFERRED INCOME	265.574	247.036
Provisions for the pensions and other liabilities	50.191	21.898
Provisions for taxes	327	398
Other provisions	12.816	29.925
TOTAL PROVISIONS FOR LIABILITIES AND CHARGES	63.334	52.221
BONDS	1.218.387	722.667
LOANS	1.261.862	850.000
OTHER CREDITORS	50.625	48.295
LONG-TERM CREDITORS	2.530.874	1.620.962
BONDS AND OTHER MARKETABLE SECURITIES	-	45.583
Non-convertible bonds	-	45.076
Interest payable	-	507
LOANS	279.907	186.360
Loans and other debt	269.419	179.473
Interest payable	10.488	6.887
SHORT-TERM DEBT WITH EQUITY ACCOUNTED AND ASSOCIATED COMPANIES	22.624	31.219
Equity accounted companies	22.624	31.219
TRADE CREDITORS	89.164	75.107
For purchases and services received	57.348	58.287
Bill payable	31.816	16.820
OTHER CREDITORS	217.319	211.574
Public entities	29.721	26.099
Other	186.283	184.336
Short-term guarantee deposits received	1.315	1.139
ACCRUALS	22.227	23.629
TOTAL CURRENT LIABILITIES	631.241	573.472
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES	4.443.369	3.388.830

Individual Financial Statements • Red Eléctrica de España, S.A.
Profit and loss accounts for the years ended at 31 December 2005 and 2004 • In thousands of Euros

DEBIT	2005	2004
EXPENSES		
MATERIALS CONSUMED	214.435	213.313
Purchases of energy and power	182.698	194.981
Maintenance and repair materials	31.737	18.332
PERSONNEL EXPENSES	75.118	67.276
Wages and salaries	57.152	50.404
Social security	12.462	10.645
Pensions and similar obligations	942	862
Other social charges	4.562	5.365
AMORTISATION AND DEPRECIATION	182.413	184.011
CHANGES IN TRADE PROVISIONS AND BAD DEBTS WRITTEN OFF	(959)	1.583
Change in provisions for stocks	(951)	1.767
Change in provision for bad debts	(8)	(184)
OTHER OPERATING EXPENSES	161.849	186.031
External services	154.682	175.115
Local taxes	3.361	2.122
Other operating expenses	1.134	1.514
Provision for liabilities and charges	2.672	7.280
TOTAL OPERATING EXPENSES	632.856	652.214
OPERATING PROFIT	313.802	302.404
FINANCIAL AND SIMILAR EXPENSES	89.736	75.421
On debt with group companies	46.397	40.917
On debt with third parties	43.339	34.504
EXCHANGE LOSSES	2	18
TOTAL FINANCIAL EXPENSES	89.738	75.439
PROFIT ON ORDINARY ACTIVITIES	244.776	229.332
CHANGES IN PROVISIONS FOR FIXED ASSETS	24.118	28.759
LOSSES ON TANGIBLE ASSETS	26.421	-
LOSSES ON OWN SHARE OPERATIONS	105	1
EXTRAORDINARY EXPENSES	8.633	726
PRIOR YEARS' EXPENSES AND LOSSES	167	234
TOTAL EXTRAORDINARY EXPENSES	59.444	29.720
PROFIT BEFORE INCOME TAX	222.163	207.695
INCOME TAX	76.246	80.342
TAXES OTHER THAN INCOME	117	118
PROFIT FOR THE YEAR	145.800	127.235

CREDIT	2005	2004
INCOME		
NET SALES	926.094	936.637
Services rendered (Transmission and system operation)	708.915	658.053
Sales of energy and power	188.403	201.335
Other service income	28.776	77.249
SELF-CONSTRUCTED ASSETS	14.714	13.858
OTHER OPERATING INCOME	5.850	4.123
Other income	5.047	2.858
Grants	258	222
Surplus provision for liabilities	545	1.043
TOTAL OPERATING INCOME	946.658	954.618
INVESTMENTS INCOME	519	-
Group companies	519	-
REVENUES FROM OTHER MARKETABLE SECURITIES AND NON-CURRENT LOANS	8.772	1.971
Group and associated companies	8.772	1.971
OTHER INTEREST AND SIMILAR INCOME	11.336	292
Group companies	7.746	-
Other interest	3.590	292
EXCHANGE GAINS	85	104
TOTAL FINANCIAL INCOME	20.712	2.367
NET FINANCIAL EXPENSES	69.026	73.072
PROFIT ON DISPOSAL OF TANGIBLE FIXD ASSETS	23.565	10
PROFIT ON OWN SHARE OPERATION	2.127	1.159
CAPITAL GRANTS TAKEN TO INCOME	3.935	4.410
EXTRAORDINARY INCOME	4.579	2.099
PRIOR YEARS' PROFIT AND INCOME	2.625	405
TOTAL EXTRAORDINARY INCOME	36.831	8.083
NET EXTRAORDINARY LOSS	22.613	21.637

Proposed Profits Distribution

Red Eléctrica de España, S.A.

Proposed distribution of profits

Year 2005

The year 2005 profit reached Euros 145,800,128.73. The distribution of this profit, as proposed by the Board of Directors to the Annual General Meeting of Shareholders, provides for a gross dividend of Euros 0.7304 per share payable to those entitled to a dividend. Accordingly, an interim dividend of Euros 0.2708 per share has already been paid out. The balance, after the said dividends have been paid, will be transferred to Voluntary Reserves.

	Amounts in euros
VOLUNTARY RESERVES	47,042,514.66
DIVIDEND	
INTERIM DIVIDEND	36,587,522.07
EXTRA DIVIDEND	62,170,092.00
(Computed on the total number of shares)	
Total	145,800,128.73

CERTIFICATE

Rafael García de Diego Barber, Secretary to the Board of Directors of Red Eléctrica de España, S.A., as established in Article 109 of the Trade and Companies Register Regulations

Certifies Hereby,

That the Annual Accounts and Directors Report of the consolidated Red Eléctrica Group, as well as the Balance Sheet, Profit and Loss Statement and Proposed Profit Distribution of Red Eléctrica de España, S.A., as stated in the present document, are a true and accurate copy of those which were inspected and approved during the meeting held by the Board of Directors of Red Eléctrica de España, S.A., on March 23rd, 2006. A copy of each of these documents, signed by all the Directors, as required by Article 171,2 of the Reviewed Companies Act, is available at the Board Secretary's Office.

And as evidence thereof, I hereby issue this certificate in Madrid, on the 27th of March of the year 2006.



Co-ordination:

Department of Communications and Institutional Relations of Red Eléctrica

Front cover picture:

"Intensidad": 7 colours engraving by the painter Rafael Rodríguez de Rivera carried out for Red Eléctrica de España. Original graphic art work edited by Nave del Arte. www.navedelarte.com

Picture in chapters initial page:

Original acrylic on paper by the painter Rafael Rodríguez de Rivera carried out for Red Eléctrica de España. Original graphic art work edited by Nave del Arte. www.navedelarte.com

Photographs:

Red Eléctrica photographic archives

Graphic design, image processing and layout:

zen comunicación visual · www.zen.es

Colour separation

Siglo Digital

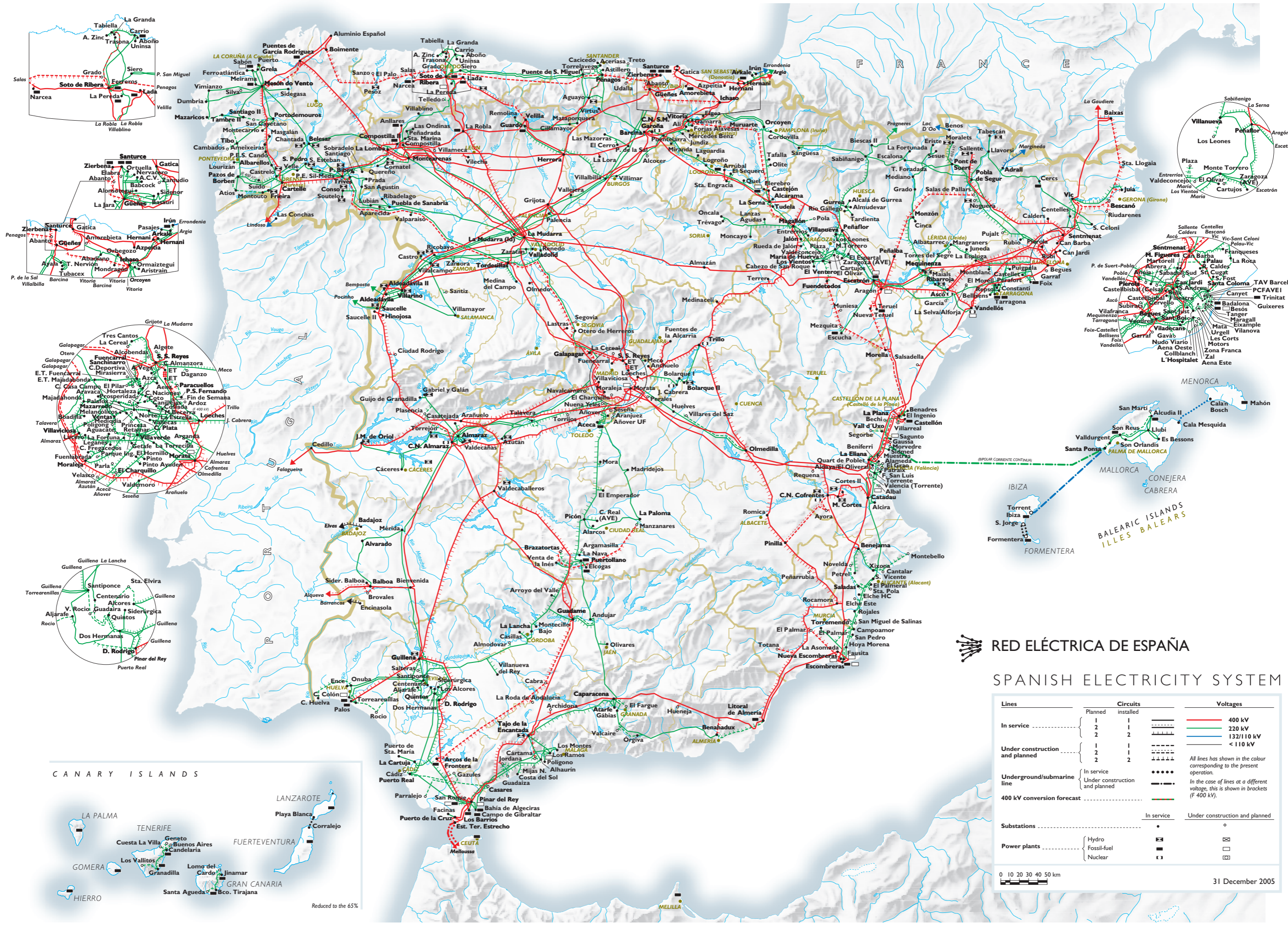
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RED ELÉCTRICA DE ESPAÑA
SPANISH ELECTRICITY SYSTEM

Lines	Circuits		Voltages
	Planned	Installed	
In service	1	1	400 kV
	2	2	220 kV
Under construction and planned	1	1	132/110 kV
	2	2	< 110 kV
Underground/submarine line	In service	•••••	All lines has shown in the colour corresponding to the present operation. In the case of lines at a different voltage, this is shown in brackets (F 400 kV).
	Under construction and planned	—•—•—	
400 kV conversion forecast		—•—•—	
Substations	In service	○	Under construction and planned
	Under construction and planned	◻	
Power plants	Hydro	☐	
	Fossil-fuel	■	
	Nuclear	☒	

0 10 20 30 40 50 km
 31 December 2005



Reduced to the 65%



RED ELÉCTRICA
DE ESPAÑA

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www.ree.es