

**Consolidated**  
annual  
accounts  
**2011**

On the road  
to sustainable  
energy

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# Independent Audit Report



*"This version of our report is a free translation from the original, which was prepared in Spanish. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation."*

## REPORT OF THE AUDITORS ON THE CONSOLIDATED ANNUAL ACCOUNTS

To the shareholders of Red Eléctrica Corporación, S.A.

We have audited the consolidated annual accounts of Red Eléctrica Corporación, S.A. (the parent company) and subsidiaries (the Group) consisting of the consolidated balance sheet at 31 December 2011, the consolidated income statement, the consolidated statement of other comprehensive income, the consolidated statement of changes in equity, the consolidated cash flow statement and related notes to the consolidated annual accounts for the year then ended. As is explained in Note 2.a of the accompanying notes to the annual accounts, the Company's directors are responsible for the preparation of these consolidated annual accounts in accordance with International Financial Reporting Standards as endorsed by the European Union and other provisions of the financial reporting framework applicable to the Group. Our responsibility is to express an opinion on the consolidated annual accounts taken as a whole, based on the work carried out in accordance with legislation governing the audit practice in Spain, which requires the examination, on a test basis, of evidence supporting the consolidated annual accounts and an evaluation of whether their overall presentation, the accounting principles and criteria applied and the estimates made are in accordance with the applicable financial reporting framework.

In our opinion, the accompanying consolidated annual accounts for 2011 present fairly, in all material respects, the consolidated financial position of Red Eléctrica Corporación, S.A. and subsidiaries at 31 December 2011 and the consolidated results of its operations and consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as endorsed by the European Union, and other provisions of the applicable financial reporting framework.

The accompanying consolidated Directors' Report for 2011 contains the explanations that the Parent Company's Directors consider appropriate regarding the Group's situation, the development of its business and other matters and does not form an integral part of the consolidated annual accounts. We have verified that the accounting information contained in the consolidated Directors' Report is in agreement with that of the consolidated annual accounts for 2011. Our work as auditors is limited to checking the consolidated Directors' Report in accordance with the scope mentioned in this paragraph and it does not include a review of information other than that obtained from the accounting records of Red Eléctrica Corporación, S.A. and subsidiaries.

PricewaterhouseCoopers Auditores, S.L.

Original in Spanish signed by Francisco J. Martínez Pérez  
Partner - Auditor

28 February 2012

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Consolidated balance  
**sheet**

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# Red Eléctrica Group Consolidated balance sheet

at 31 December 2011 and 2010

(thousand euro)

<b>Assets</b>	<b>31/12/2011</b>	<b>31/12/2010</b>
Intangible assets (Note 5)	4,830	2,943
Property, plant and equipment (Note 6)	8,068,413	7,607,912
Investment properties (Note 7)	2,695	2,126
Investments carried under the equity method (Note 8)	4,663	5,757
Non-current financial assets (Note 17)	91,904	78,969
Deferred tax assets (Note 21)	127,144	61,384
Other non-current assets (Note 9)	33,200	49,482
<b>Non-current assets</b>	<b>8,332,849</b>	<b>7,808,573</b>
Non-current assets held for sale	-	601
Inventories (Note 10)	44,378	43,788
Trade and other receivables (Note 11)	368,070	412,464
Receivables for sales and services rendered	22,775	30,680
Other receivables	343,832	370,716
Current tax assets	1,463	11,068
Other current financial assets (Note 17)	837	186
Cash and cash equivalents	19,343	18,286
<b>Current assets</b>	<b>432,628</b>	<b>475,325</b>
<b>Total assets</b>	<b>8,765,477</b>	<b>8,283,898</b>

# Red Eléctrica Group Consolidated balance sheet

at 31 December 2011 and 2010

(thousand euro)

Liabilities	31/12/2011	31/12/2010
<b>Equity</b>	<b>1,820,185</b>	<b>1,629,666</b>
Share capital	270,540	270,540
Reserves	1,208,913	1,071,446
Treasury shares (-)	(28,684)	(23,297)
Profit for the year attributed to the parent company	460,348	390,150
Interim dividend (-)	(90,932)	(79,173)
<b>Adjustments due to changes in value</b>	<b>(8,312)</b>	<b>(6,837)</b>
Hedging operations	(2,717)	(312)
Other adjustments due to changes in value	644	-
Exchange differences	(6,239)	(6,525)
<b>Equity attributed to the parent company</b>	<b>1,811,873</b>	<b>1,622,829</b>
<b>Minority shareholdings</b>	<b>1,674</b>	<b>1,725</b>
<b>Total equity</b> (Note 12)	<b>1,813,547</b>	<b>1,624,554</b>
Subsidies and other (Note 13)	400,894	368,761
Non-current provisions (Note 14)	67,426	75,752
Non-current financial liabilities (Note 17)	3,831,476	3,727,980
Bank borrowings and debentures or other marketable securities	3,776,873	3,695,289
Other non-current financial liabilities	54,603	32,691
Deferred tax assets (Note 21)	607,616	338,426
Other non-current liabilities (Note 15)	77,540	81,601
<b>Non-current liabilities</b>	<b>4,984,952</b>	<b>4,592,520</b>
Current provisions	1,948	1,864
Current financial liabilities (Note 17)	1,693,612	1,839,677
Bank borrowings and debentures or other marketable securities	971,283	1,070,927
Other current liabilities	722,329	768,750
Trade and other payables (Note 19)	271,418	225,283
Trade payables	251,915	209,101
Other payables	18,982	16,142
Current income tax liabilities	521	40
<b>Current liabilities</b>	<b>1,966,978</b>	<b>2,066,824</b>
<b>Total liabilities</b>	<b>8,765,477</b>	<b>8,283,898</b>

(Notes 1 to 33 form an integral part of the consolidated financial statements).



# Red Eléctrica Group Consolidated Income Statement

2011 and 2010

(thousand euro)

Consolidated income statement	2011	2010
Net revenue (Note 22-a)	1,637,336	1,397,252
Work performed on the Company's own assets	18,077	18,044
Raw materials and consumables (Note 22-c)	(42,649)	(45,022)
Other operating revenues (Note 22-b)	10,043	15,256
Personnel costs (Note 22-d)	(128,846)	(112,709)
Other operating expenses (Note 22-c)	(278,741)	(270,922)
Asset depreciation/amortisation (Notes 5, 6 and 7)	(382,681)	(305,064)
Non-financial asset and other subsidies attributed (Note 13)	11,407	10,364
Impairment and profit/loss on fixed asset disposals (Note 6)	(139)	(18,658)
<b>Operating profit</b>	<b>843,807</b>	<b>688,541</b>
Financial income	6,699	5,027
Financial expense (Note 22-f)	(155,301)	(104,341)
Exchange differences	19	101
Impairment and gain/loss on disposals of financial instruments	(12,474)	(29,883)
<b>Financial income/expense</b>	<b>(161,057)</b>	<b>(129,096)</b>
Results of companies carried under the equity method (Note 8)	925	1,003
<b>Profit before taxes</b>	<b>683,675</b>	<b>560,448</b>
Corporate income tax (Note 21)	(223,421)	(170,300)
<b>Consolidated profit or loss for the year</b>	<b>460,254</b>	<b>390,148</b>
<b>A) Consolidated profit or loss for the period attributed to parent company</b>	<b>460,348</b>	<b>390,150</b>
<b>B) Profit or loss for the year attributed to non-controlling interests</b>	<b>(94)</b>	<b>(2)</b>
<b>Earnings per share in euro</b>		
Basic earnings per share in euro (Note 31)	3.42	2.90
Diluted earnings per share in euro (Note 31)	3.42	2.90

(Notes 1 to 33 form an integral part of the consolidated financial statements).



# Red Eléctrica Group

## Consolidated statement of comprehensive results

2011 and 2010

(thousand euro)

Consolidated statement of comprehensive results	2011	2010
<b>Consolidated profit or loss for the year</b>	<b>460,254</b>	<b>390,148</b>
<b>Revenues and expenses attributed directly to equity</b>	<b>(15,929)</b>	<b>(8,775)</b>
- Measurement of financial instruments	(12,549)	(11,214)
a) Available-for-sale financial assets (Note 17)	(12,549)	(11,214)
- Cash-flow hedges (Note 18)	(3,874)	(1,627)
- Conversion differences (Note 12)	555	741
- Actuarial Gains and Losses and other adjustments	587	(950)
- Revenues and expenses attributed directly to equity	(808)	514
- Tax effect	160	3,761
<b>Transfers to the income statement</b>	<b>14,349</b>	<b>21,071</b>
- Measurement of financial instruments (Note 17)	12,549	29,935
- Cash-flow hedges (Note 18)	438	166
- Conversion differences	(75)	-
- Companies carried under the equity method	-	-
- Revenues and expenses attributed directly to equity	-	-
- Tax effect	1,437	(9,030)
<b>Total comprehensive results for the year</b>	<b>458,674</b>	<b>402,444</b>
<b>A) Consolidated overall results for the year attributed to parent company</b>	<b>458,725</b>	<b>402,533</b>
<b>B) Comprehensive results attributed to non-controlling interests</b>	<b>(51)</b>	<b>(89)</b>

(Notes 1 to 33 form an integral part of the consolidated financial statements).







# Red Eléctrica Group

## Consolidated cash flow statement

2011 and 2010

(thousand euro)

CONSOLIDATED CASH FLOW STATEMENT	2011	2010
<b>Cash flows from operating activities</b>	<b>1,205,946</b>	<b>824,678</b>
<b>Profit before taxes</b>	<b>683,675</b>	<b>560,448</b>
<b>Adjustments to results</b>	<b>522,571</b>	<b>459,757</b>
Asset depreciation/amortisation	382,681	305,064
Other adjustments to results (net)	139,890	154,693
Shareholdings consolidated using the equity method (results)	(925)	(1,003)
Results on disposal/impairment of non-current assets and financial instruments	12,613	48,593
Accrual of financial income	(6,699)	(5,027)
Accrual of financial expense	155,301	104,341
Transfer to provision/excess provision for liabilities and charges	(6,314)	22,209
Attribution of subsidies and other	(14,086)	(14,420)
<b>Changes in current assets</b>	<b>121,012</b>	<b>(51,408)</b>
<b>Other cash flows from operating activities</b>	<b>(121,312)</b>	<b>(144,119)</b>
Payment of interest	(122,967)	(100,207)
Collection of dividends	5,395	5,237
Collection of interest	2,213	568
Corporate income tax payments received/(made)	(3,892)	(48,953)
Other income/(expenses) from operating activities	(2,061)	(764)
<b>Cash flows from investing activities</b>	<b>(889,167)</b>	<b>(2,249,299)</b>
<b>Payments for investments</b>	<b>(933,297)</b>	<b>(2,308,614)</b>
Property, plant and equipment, intangible assets and investment properties	(932,476)	(2,306,745)
Other financial assets	(821)	(1,869)
<b>Collections from divestments</b>	<b>590</b>	<b>1,471</b>
Other financial assets	590	1,471
<b>Other cash flows from investment activities</b>	<b>43,540</b>	<b>57,844</b>
Other income from investing activities	43,540	57,844
<b>Cash flows from financing activities</b>	<b>(316,381)</b>	<b>1,428,303</b>
<b>Payments received/(made) for equity instruments</b>	<b>(4,627)</b>	<b>(9,927)</b>
Acquisition	(167,035)	(134,623)
Disposal	162,408	124,696
<b>Payments received/(made) for financial liability instruments</b>	<b>(58,962)</b>	<b>1,637,007</b>
Issue and draw downs	1,401,564	3,418,068
Repayment and amortisation	(1,460,526)	(1,781,061)
<b>Payments of dividends and remuneration for other equity instruments</b>	<b>(252,792)</b>	<b>(198,777)</b>
<b>Effect of exchange rate variations on cash or cash equivalents</b>	<b>659</b>	<b>536</b>
<b>Net increase/(decrease) in cash and cash equivalents</b>	<b>1,057</b>	<b>4,218</b>
<b>Cash and cash equivalents at the beginning of the period</b>	<b>18,286</b>	<b>14,068</b>
<b>Cash and cash equivalents at the end of the period</b>	<b>19,343</b>	<b>18,286</b>

(Notes 1 to 33 form an integral part of the consolidated financial statements)





**2**  
Consolidated  
**report 2011**

# 1. Activities of Group Companies

Red Eléctrica Corporación, S.A. (hereinafter the Parent Company or the Company) and its subsidiaries comprise the Red Eléctrica Group (hereinafter the Group or Red Eléctrica Group). The Group's primary activity consists of the transmission of electricity, the operation of the system and the management of the electricity transmission grid in Spain. These regulated activities are carried out by Red Eléctrica de España S.A.U. (hereinafter REE).

Schedule I provides details of the Parent Company's activities and domicile and its subsidiaries, as well as the Parent Company's direct or indirect stakes in dependent companies.

## 2. Basis of presentation of the Consolidated Annual Accounts

### a) General information

The consolidated financial statements have been prepared by the Directors of the Parent Company to present fairly the consolidated equity and the consolidated financial position at 31 December 2011, the consolidated results of operations, and changes in consolidated equity and consolidated cash flows of the Group for the year then ended.

The historic cost approach has been applied when preparing these Consolidated Financial Statements, adjusted by the available-for-sale financial assets and financial assets and liabilities (including derivatives) at fair value through changes in profit and loss and the taking into consideration of the recognition criteria for business combinations.

The consolidated financial statements are expressed in thousands of euro and have been prepared in accordance with International Financial Reporting Standards adopted by the European Union (IFRS-EU), in accordance with EC Regulation 1606/2002 of the European Parliament and Council and the interpretations (IFRIC) endorsed by the European Union.

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

These consolidated financial statements, prepared by the Directors of the Company at the Board meeting held on 27 February 2012, have been prepared on the basis of the individual accounting records of the Company and other companies which comprise the Red Eléctrica Group (Schedule I). The companies prepare their financial statements in accordance with the accounting principles in effect in the country where they operate. Therefore the consolidated financial statements include certain adjustments and reclassifications made to bring the accounting principles followed by the Group companies in preparing their financial statements

into line with EU- IFRS. Similarly, the accounting policies of the consolidated companies are changed when it is necessary to ensure consistency with the accounting policies adopted by the Company.

The consolidated financial statements for 2010 were approved by the General Shareholders' Meeting of 13 April 2011. The Consolidated Financial Statements for 2011 are pending approval by shareholders at the Annual General Meeting. Nonetheless, the Company's Board of Directors considers that those consolidated financial statements will be approved without changes.

### **b) New EU-IFRS and IFRIC interpretations**

The adoption of the new standards or amendments to existing standards and interpretations (IFRS 1, IFRS 3, IFRS 7, IAS 1, IAS 24, IAS 27, IAS 32, IAS 34, IFRIC 14, IFRIC 13, IFRIC 19) approved and published and which enter into force for years commencing in 2011 did not have any significant impact on these Consolidated Annual Accounts.

With respect to the new accounting standards, changes to existing standards and interpretations (IAS 1, IAS 12, IAS 19, IAS 27, IAS 28, IAS 32, IFRS 1, IFRS 7, IFRS 9, IFRS 10, IFRS 11, IFRS 12 and IFRS 13 and IFRIC 20) to be applied to the years commencing 1 January 2012, the Group does not expect them to have significant effects on the Consolidated Annual Accounts. In 2011 the Group chose not to apply any of these standards early.

### **c) Accounting estimates and assumptions**

The preparation of the consolidated financial statements under IFRS requires Group management to make judgements, estimates and assumptions that affect the application of standards and the reported amounts of assets and liabilities, income and expenses. Estimates and judgements are continually evaluated and are based on past experience and other factors, including expectations relating to future events that are considered to be reasonable under current circumstances. Actual results may differ from these estimates.

The consolidated financial statements for 2011 include the estimates of management of the Group and consolidated companies on the value of assets, liabilities, income, expenses and commitments recognised, which were subsequently ratified by the Board of Directors.

These estimates mainly comprise:

- ◆ Estimated recovery of assets. The calculation of impairment of assets is based on discounted cash flows according to the financial projections used by the Group. The discount rate used is the weighted average cost of capital, taking into account the country risk premium.
- ◆ Estimates of the useful lives of property, plant and equipment.
- ◆ The assumptions used in actuarial calculations
- ◆ As a general rule, liabilities are accounted for when an obligation is likely to give rise to an indemnity or payment. The Group assesses and estimates the necessary amounts to be paid in the future, including additional amounts relating to income taxes, contractual obligations, the settlement of

outstanding litigations or other liabilities. Those estimates are subject to interpretations of current events and circumstances, projections of future events and estimates of the financial effects of those events.

To better understand the Consolidated Annual Accounts the various estimates and assumptions are detailed in each of the notes to the annual accounts

In addition, the Company has arranged insurance policies to cover possible third- party claims which may be filed in the ordinary course of its activities.

Although estimates were based on the best information available at 31 December 2011, 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.

#### d) Consolidation principles

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 and are excluded from consolidation at the time such control ceases.

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

##### ◆ Group companies

Subsidiaries are entities controlled by the Parent 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 50% of the voting rights. Control also exists when the Parent Company 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 the meetings of the Board of Directors and control of the entity is by that Board.

The financial statements of subsidiaries are fully consolidated.

The Group recognises any non-controlling stake in each business combination at the proportional part of the uncontrolled stake in the identifiable net assets of the investee.

##### ◆ Jointly controlled entities

Jointly controlled entities are considered to be those that the parent company manages together with other companies. Joint management is understood to be that for which there is a contractual agreement to share control of an economic activity, requiring strategic decisions in both financial and operational areas of the activity, and there is unanimous consent among the parties sharing control.

The financial statements of jointly controlled entities are consolidated using the proportional method.

The Group consolidated multi-group companies using the proportional method, incorporating assets, liabilities, revenues, expenses and cash flows on a line-by-line basis in accordance with the stake held in the jointly controlled company. The Group recognizes its share in the profits or loss deriving from the sale of Group assets to jointly controlled entities in its consolidated financial statements in the proportion corresponding to other participants. The Group does not recognize its share in the profits or loss of a jointly controlled entity deriving from the purchase by the Group of assets from the jointly controlled entity until the assets are sold to an independent third party. However, a loss on the transaction is immediately recognised if it reveals a reduction in the net realisable value of current assets or an impairment loss.

#### ◆ Associates

Associates are entities over which the Company has significant influence 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.

Investments in associates are accounted for by the equity method of accounting, that is, at the 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 identifiable net assets of the associate attributable to the Group on the acquisition date 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 the identifiable net assets of the associate held by the Group on the acquisition date (i.e. discount on acquisition) the difference is recognised directly in the income statement in the period of acquisition.

Information on consolidated subsidiaries and associates of the Company, the consolidation or valuation methods applied in the preparation of the accompanying consolidated financial statements and other information are included in Schedule 1.

The financial year end closing dates of the financial statements of the subsidiaries and associates used in the consolidation process coincide with those of the Parent Company.

The operations of the Company and subsidiaries have been consolidated in accordance with the following basic principles:

- ◆ The accounting principles and criteria used by the Group companies have been brought into line with those used by the Parent Company.
- ◆ The financial statements of foreign companies have been translated by applying the year-end exchange rate at the date of the balance sheet for assets and liabilities and the average exchange rate

for the period for income and expenses, and the historic exchange rate for capital and reserves.

- ◆ Exchange rate differences resulting from translation to euro are recognised in the consolidated balance sheet at the year end as a separate component of Equity named Conversion differences.
- ◆ All significant balances and transactions between fully consolidated companies have been eliminated in the consolidation.
- ◆ Margins on sales of capitalised goods and services between Group companies are eliminated when the relevant operations are carried out.

### e) Comparability of information

Group management presents comparative information relating to 2010 in the accompanying consolidated annual accounts. As is required by IFRS-EU, these consolidated financial statements for 2011 present, for the purposes of comparison, the figures relating to the previous year.

### f) Changes in the scope of consolidation

During 2011 there have been no changes in the scope of consolidation compared with last year.

On 17 May 2010 Red Eléctrica Corporación S.A. incorporated the wholly owned subsidiary REDCOR Reaseguros S.A., domiciled in Luxembourg and whose corporate purpose consists of designing and carrying out all the general and specific activities of a captive reinsurance company in all lines of business.

On 14 July 2010 Red Eléctrica Internacional S.A.U. (hereinafter REI) incorporated (75%) together with AC Capitales SAFI S.A., the company Transmisora Eléctrica del Sur, S.A. (hereinafter TESUR), domiciled in Lima (Peru), whose main activity is the transmission of electricity and the operation and maintenance of electricity transmission networks.

On 31 August 2010 Transportadora de Electricidad S.A. (hereinafter TDE) sold the 75% stake it held in the company Cybercia S.R.L. (hereinafter CYB) for 150 thousand USD, and at that time the company ceased to consolidate with the Group.



## 3. Industry Regulation

### Electricity sector in Spain

The electricity sector is regulated by Law 54/1997, of 27 November 1997, on the Electricity Sector, as partly amended by Law 17/2007, of 4 July 2007, by virtue of which REE was created.

According to Additional Provision Three of that law, all provisions concerning the system operator and transmission grid manager of the Electricity Sector Law are applicable to the Company.

The following should be noted with respect to these activities:

- ◆ The Law on the Electricity Sector recognises that electricity transmission is a natural monopoly due to the economies of scale provided by the single grid. The deregulation of transmission is arranged through generalised third-party access to the grid, which is available to the various parties to the electricity system and consumers in exchange for the payment of access tariffs. The compensation for this activity is set by law and fundamentally by Royal Decrees 2819/1998 and 325/2008.

In addition, in order to bring the sole transmission operator function into effect, the Law lays down that companies owning transmission facilities should transfer these facilities to the Company within a maximum of three years after the law takes effect. To comply with that legislation, in 2010 the Company concluded plant acquisition contracts with Endesa Distribución Eléctrica, S.L., Unión Fenosa Distribución S.A.U., and Hidrocantábrico Distribución Eléctrica, S.A.U.

- ◆ In the performance of its Spanish electricity system operator activities, the REE's main function is to ensure the continuity and security of electricity supply and the correct coordination of the production and transmission system, by carrying out its functions in coordination with the operators and players of the Mainland Electricity Energy Market under principles of transparency, objectivity and independence. The Company has also been assigned the functions of settlement, communication of payments and collections and the management of guarantees related to the guarantee of supply and the effective diversion of generation and consumption units. The Company is also responsible for the short-term energy exchanges that are intended to maintain supply quality and security conditions

Furthermore, REE has also been attributed the operation of the island and off-mainland electricity systems in the Balearic Islands, Canary Islands, Ceuta and Melilla.

- ◆ In its capacity as manager of the transmission grid, REE 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 consistent and coherent criteria. It is also responsible for the administration of power transmission between external systems using the Spanish grid, as well as withholding access to the grid when capacity is insufficient.

## International electricity sector

The Red Eléctrica Group, through REI, has investments in the electricity sector internationally, namely, in Bolivia and Peru.

Both of these countries have deregulated their electricity industry and use a regulation model supported by regulated tariffs for transmission.

## 4. Accounting Principles

The main accounting principles used in the preparation of these consolidated financial statements, applied uniformly to the years presented, are as follows:

### a) Property, plant and equipment

Property, plant and equipment mainly comprise electricity plants which are measured, as appropriate, at production or acquisition cost, less accumulated depreciation and any impairment losses. Cost includes, where applicable, the following items:

- ◆ Financial expense on external financing solely accrued during the construction period.
- ◆ Operating costs, directly related to the construction of property, plant and equipment in projects controlled or managed by Group companies.

It is the policy of Group companies to transfer work in progress to property, plant and equipment in operation once it is brought into service and provided that the assets are in condition for use.

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

Repair and maintenance costs of property, plant and equipment which do not increase productivity, do not improve 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, applying the following rates:

	Annual rate
Buildings	2% - 10%
Electricity plants	2.5% - 7.14%
Other plant, machinery, tooling, furnishing and other assets	4% - 25%

There have been no significant changes in the depreciation policy for assets compared with last year.

Most of the plant, machinery and equipment relates to electricity installations that are mainly depreciated at a rate of 2.5%.

The residual value and useful life of assets is examined and adjusted, if necessary, at the date of each balance sheet.

When an asset's carrying amount exceeds its estimated recoverable amount, the carrying amount is written down immediately to the recoverable amount.

## b) Intangible assets

Intangible assets are stated at acquisition cost and tested and adjusted on a regular basis for impairment. The assets included under this heading are as follows:

### ◆ Computer software

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

The costs relating to the maintenance of computer programs are recognized as an expense when incurred. Software is amortised on a straight-line basis over a period of between three and five years from the installation date of each program.

### ◆ Development expenses

Development expenses directly attributable to the design and testing of new or improved software that can be identified and are unique and may be controlled by the company are recognised as intangible assets when it is likely that the project will be successful, taking into consideration its technical and commercial viability and the costs may be reliably estimated. The expenses that do not comply with these criteria are recognised as an expense at the time they are incurred. Development costs are capitalised and amortised on a straight-line basis over a period not exceeding five years from commencement of the project. The costs relating to the maintenance of computer programs are recognized as an expense when incurred.

### ◆ Intangible assets in progress

The administrative concessions are recognised as intangible assets in progress are valued at the payments that will be made until fulfilment.

## c) Investment property

Group companies measure investment property at acquisition cost. The market value of the Group's investment property is broken down in Note 7 to 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. Investment properties are amortised over 50 years.

#### d) Financial assets

The Group classifies financial assets, except those investments accounted for using the equity method, in the following three categories:

- ◆ **Loans and receivables:** are non-derivative financial assets with fixed or determinable payments which are not listed on an active market and with respect to which there is no intention to trade in the short term. They are classified as current assets except for assets maturing in more than 12 months of the balance sheet date which are classified as non-current assets.

Loans 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.

Receivables are initially recognised at fair value and subsequently at amortised cost using the effective interest rate method. Furthermore, current advances generally deriving from multi-year contracts or commitments are considered accounts receivable and taken to the income statement over the period during which such contracts or commitments are in effect.

At the year end the Company evaluates the possible existence of impairment losses. Impairment losses are calculated as the difference between the carrying value for the asset and the present value of future estimated cash flows discounted at the original effective interest rate for the financial instrument. The carrying value is reduced and the loss is recognised in the Consolidated Income Statement.

- ◆ **Available-for-sale financial assets:** these are investments which the Company intends to hold for an unspecified period of time and which may be sold, on the basis of specific liquidity needs or changes in interest rates. They are classified as non-current assets unless their liquidation is planned in less than one year and this is feasible. These financial assets are stated at fair value, which is understood to be their quoted price at the year end for those securities quoted on an active market. The gains or losses resulting from fluctuations in fair value at the year end are recognised directly in equity and accumulated to the time of settlement or adjustment of value owing to impairment, at which time they are taken to the income statement. The calculation of possible impairment is done using the method of discounting expected future cash flows. A significant or prolonged fall in the listed value of securities below their cost is also considered to be evidence that the asset is impaired.

Dividends from shareholdings in capital classed as available for sale are taken to the consolidated income statement at the time the Company becomes entitled to receive them.

- ◆ **Cash and cash equivalents:** cash and cash equivalents include cash on hand, demand deposits in credit institutions and other highly liquid short-term investments maturing within three months.

The fair value appraisals are classified using a fair value hierarchy that reflects the relevance of the variables used to obtain the valuations. This hierarchy consists of three levels:

- ◆ Level 1: Measurements based on the listed price of identical instruments on an active market.
- ◆ Level 2: Measurements based on variables that are observable with respect to assets and liabilities.
- ◆ Level 3: Measurements based on variables that are not based on observable market data.

### e) Inventories

Inventories of materials and replacement parts are measured at the lower of acquisition cost, which is determined using the lower of the average weighted price method and net realisable value. Group companies review the net realisable value of inventories at each year end, recognising value adjustments as an expense in the income statement when their cost exceeds market value 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 and is recognised as revenue in the income statement.

### f) Asset impairment

Group companies analyse the recoverability of assets at the year end each year and whenever some event or change in circumstances indicates that the carrying value may not be recoverable. If the recoverable amount of an asset is less than its carrying value, an impairment loss is recognised immediately in the income statement. The impairment loss is therefore the difference between the carrying value of an asset and its recoverable value. The recoverable amount is the fair value of an asset, less the higher of costs incurred for its sale or its value in use. The calculation of the recoverable value is based on expected cash flows. Impairment is calculated for individual assets if the recoverable value of the individual asset cannot be determined the recoverable value of the Cash Generating Unit (CGU) to which the asset pertains will be determined. Possible reversals are recognised in the income statement. Losses from impairment recognised in goodwill are not reversed in subsequent years.

### g) Share capital, treasury shares and dividends

Share capital consists of ordinary shares. The issue costs of new shares, net of taxes, are deducted from equity.

Treasury shares are measured at acquisition cost and are presented by reducing equity. Any gain or loss obtained on the purchase, sale, issue or redemption of treasury shares is recognised directly in Equity.

The interim dividend reduces equity for the year to which it relates, on the basis of the resolution of the Board of Directors. Complementary dividends are not charged to equity until approved by the shareholders at their Annual General Meeting.

## h) Subsidies

Outright capital grants received from government agencies to finance the acquisition of assets are recorded by the Group, once the relevant investments have been made and it is assured that the grant will be received.

The Group recognises subsidies under non-financial subsidies in the income statement for each year over the term in which depreciation of the related asset is charged.

## i) Non-current advances

Non-current advances generally 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.

## j) Provisions

### ◆ Employee benefits

#### - 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 remuneration. 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 in the current and prior years. The contributions are recognised as employee benefit expense when they are due.

#### - Other long-term employee benefits

Other long-term employee benefits include defined benefit plans providing benefits other than pension plans, such as medical insurance, to part of the active and retired employees of the parent company and REE. Expected costs of benefits are recognised over the term of employment of personnel and are recorded under Provisions. These commitments are measured annually by qualified independent actuaries. The changes in the actuarial assumptions are recognised, net of taxes, under equity as Reserves in the year in which they arise and the cost of past services are recognised in the income statement.

Long-term compensation programs are also included and measured on an annual basis. This heading also includes length of service awards at the Bolivian company TDE. These commitments are measured annually by qualified independent actuaries. Changes in the value of length of service awards at the Bolivian company TDE due to changes in the actuarial assumptions used are charged or credited to the income statement as soon as they arise.

### ◆ Other provisions

The Group makes provisions for the amount required to settle present contractual obligations, legal or implicit, deriving from past events provided that the Group expects that it will probably

have to settle them through the outflow of resources and the amount involved can be reliably estimated. Provision is made when the liability or commitment is incurred.

Provisions are valued at the present value of the cash outflows which are expected to be necessary to settle the obligation using a rate before taxes which reflects the current market assessment of the temporary interest rate and specific risks of the obligation. The increase in the provision due to the passage of time is recognized as an interest expense.

### **k) Borrowings**

Borrowings, obligations and similar items are recognised initially at fair value, net of the transaction costs incurred. In subsequent periods, these financing obligations are valued at amortised cost, using the effective interest rate method, except for those transactions for which hedging has been arranged.

Borrowings are classed as current liabilities unless they mature in more than 12 months from the balance sheet date, in which case they are recognised as non-current assets.

### **l) Foreign currency transactions**

Foreign currency transactions are translated into euro 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 consolidated income statement.

Fixed-income securities and credits and debits in foreign currency at 31 December are translated to euro at the closing exchange rate. Foreign exchange differences arising on translation are taken to exchange gains and losses in the consolidated income statement, as appropriate.

Operations in foreign currency which the Group has hedged using financial derivatives or other hedging instruments are stated according to the principles described in Derivative instruments and hedges.

### **m) Financial derivatives and hedging operations**

Financial derivatives are initially recognised at fair value at the contract date (acquisition cost) in the consolidated balance sheet and subsequently the gain or loss on measurement to fair value is accounted for. The method of recognising the resulting gain or loss depends on whether the derivative is designated as a hedging instrument, and if so, on the nature of the item being hedged.

The total fair value of derivatives is classified as non-current assets or liabilities if the time remaining to maturity of the hedged item is more than 12 months and as current assets or liabilities if the time remaining to maturity of the hedged item is less than 12 months.

A hedge is considered to be highly effective when the changes in fair value or in the cash flows for the hedged items are offset by the change in fair value or in the cash flows of the hedge instrument within a range of between 80% to 125%.

The Group classifies some derivatives as hedging the fair value of assets or liabilities recognised as a firm commitment (fair value hedge) or as hedges of highly foreseeable transactions (cash flow hedge) or as net investment hedges on foreign operations.

The Group documents the relation between the hedging instruments and the assets or liabilities hedged at inception, as well as the purpose of the risk management and the strategy to carry out hedging transactions. The Group also documents its evaluation, at the start as well as on a continuous basis, of whether or not the derivatives used in the hedging transactions are highly effective to offset changes in fair value or in the cash flows relating to the hedged items.

The fair value of the derivative instruments used for hedging purposes are shown in Note 18. Movements under equity are set out in Note 12.

- ◆ For cash flow hedges, the effective part of changes in fair value of the derivatives which are designated and classed as cash flow hedges is recognised in equity. The gain or loss on the non-effective part is recognised directly in the consolidated income statement.
- ◆ For fair value hedges, changes in the fair value of derivatives designated as hedges are recognised in the consolidated income statement. Similarly, changes in the fair value of the hedged item in relation to the risk hedged are also recognised in the consolidated income statement. Therefore hedge accounting accelerates the recognition of income and expense of the hedged item in order to offset the effect of the derivative on the income statement.
- ◆ Net investment hedges on foreign operations are recorded in a similar manner to cash flow hedges. Any gain or loss on the hedge related to the effective part of the hedge is recognised in equity. The gain or loss on the non-effective part is recognised directly in the consolidated income statement. Accumulated gains and losses in equity are included in the income statement when the foreign operation is sold.

When a hedging instrument matures or is sold or when the requirements for its accounting as a hedge are not met, the gain or loss accumulated to such time in equity continues to be recorded in equity and is recognised as and when changes in the cash flows from the hedged item are recognised in the consolidated income statement. When the forecast transaction is not expected to arise, the accumulated gain or loss in equity is recognised in the consolidated income statement.

The market price of different financial derivative instruments is calculated as follows:

- ◆ The fair value of derivatives quoted on official markets is measured at its closing quotation price.
- ◆ For derivatives not quoted on organised markets, the Company establishes fair value by using valuation techniques. These include the use of recent arm's length transactions, relating to other instruments that are substantially the same, discounted cash flow analysis at the market interest and exchange rates in force on the presentation date, and option pricing models refined to reflect the issuer's specific circumstances.

## n) Trade payables

Trade payables are initially recognised at fair value and subsequently measured at amortised cost using the effective interest rate method. Payables falling due in less than one year and do not bear



a contractual interest rate, that are expected to be paid in the short-term are measured at their nominal value.

### **o) Income and expense**

Ordinary revenues are recognised at the fair value of the compensation received or to be received. Income and expenses are recorded on an accruals basis, i.e. when the actual flow of goods or services takes place regardless of the time the monetary or financial flow deriving there from takes place.

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

Interest income is recognised using the effective interest rate method.

Income from dividends is recognised when the collection right is established.

### **p) Tax situation**

Income tax expense/(income) 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 a business combination.

Current tax is the estimated tax payable on 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 relating to economic events arising in the year are recorded as a reduction in the accrued income tax expense unless there are doubts as to their realisation.

Deferred tax and the corporate income tax expense are calculated and accounted for using the liability method, on timing differences between assets and liabilities for financial reporting purposes and the amounts used for tax purposes. This method comprises the determination of deferred tax assets and liabilities for differences between the carrying value of assets and liabilities at the amounts for tax purposes, using tax rates which are expected to come into effect when these tax assets are realised and tax liabilities are settled.

Deferred tax assets are recognised insofar as future tax profits will probably arise against which to offset the temporary differences.

Deferred income tax is recognised on temporary differences arising on investments in subsidiaries and associates, except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

### q) 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 the case of the consolidated financial statements of the Red Eléctrica group at 31 December 2011 and 2010, basic earnings per share agree with diluted earnings since there have been no operations during those years which may change this figure.

### r) Insurance

The Red Eléctrica Group has contracted various insurance policies to cover the risks to which companies are subject through their activities. These risks mainly comprise damages to the Group companies' electricity plants and potential claims for third party damages which could arise from the Group's activities. Insurance premium income and expenses are recognised in the consolidated income statement on an accruals basis. Income to be recovered from insurance companies deriving from claims is reflected in the consolidated income statement using the matching principle.

### s) Environment

Expenses deriving from business actions taken to protect and improve the environment are recorded as an expense in the year incurred. When they relate to acquisitions of property, plant and equity the purpose of which is to minimise the environmental impact and protect and improve the environment, they are recorded as an increase in the value of fixed assets.

### t) Non-current assets held for sale

Non-current assets are classified as assets held for sale when their value will be recovered mainly through their sale, provided that their sale is considered to be highly likely. These assets are measured at the lower of their carrying value and their fair value, less selling costs if the carrying value will be recovered mainly through a sales transaction instead of through continued use.

### u) Share-based payments

The Parent Company, REE and REI have implemented a share acquisition plan under which managers are able to receive shares from the Company as part of their ordinary annual remuneration. The valuation of such share-based remuneration is based on the closing price of the Company's shares at the time of delivery. The expense deriving from this plan is reflected under Personnel costs in the consolidated income statement. All shares delivered derive from the Parent company's treasury shares.

## 5. Intangible assets

Movements in 2011 and 2010 in intangible assets and accumulated amortisation are as follows:

### Red Eléctrica Group

#### Movements in Intangible Assets 2011 and 2010

(thousand euro)

	31 December 2009	Additions	Changes in scope	Changes in exchange rate	31 December 2010	Additions	Changes in exchange rate	Transfers	31 December 2011
<b>Cost</b>									
Development expenses and computer applications	14,628	2,276	(76)	115	16,943	309	59	-	17,311
Intangible assets in progress	-	-	-	-	-	2,560	12	330	2,902
<b>Total Cost</b>	<b>14,628</b>	<b>2,276</b>	<b>(76)</b>	<b>115</b>	<b>16,943</b>	<b>2,869</b>	<b>71</b>	<b>330</b>	<b>20,213</b>
<b>ACCUMULATED AMORTISATION</b>									
Development expenses and computer applications	(12,644)	(1,329)	74	(101)	(14,000)	(1,334)	(49)	-	(15,383)
<b>Total Accumulated amortisation</b>	<b>(12,644)</b>	<b>(1,329)</b>	<b>74</b>	<b>(101)</b>	<b>(14,000)</b>	<b>(1,334)</b>	<b>(49)</b>	<b>-</b>	<b>(15,383)</b>
<b>Carrying value</b>	<b>1,984</b>	<b>947</b>	<b>(2)</b>	<b>14</b>	<b>2,943</b>	<b>1,535</b>	<b>22</b>	<b>330</b>	<b>4,830</b>

Operating expenses directly related to intangible assets capitalised in 2011 amount to €1,215 thousand (€418 thousand 2010). Intangible assets in progress relates to the advancement of work carried out by TESUR on the Tintaya-Socabaya transmission line and the associated substations.

## 6. Property, plant and equipment

The movement in 2011 and 2010 in property, plant and equipment and the relevant accumulated depreciation and impairment is as follows:

### Red Eléctrica Group Breakdown of movements in property, plant and equipment 2011 and 2010 (thousand euro)

	31 December 2009	Additions	Changes in scope	Changes in exchange rate	Sales, disposals reductions and write-offs	Transfers	31 December 2010	Additions	Changes in exchange rate	Sales, disposals reductions and write-offs	Transfers	31 December 2011
<b>COST</b>												
Land and buildings	76,218	-	-	539	-	337	77,094	4	254	-	85	77,437
Electricity installations	7,358,110	1,440,777	-	13,449	(750)	591,399	9,402,985	-	6,080	(1,227)	1,338,645	10,746,483
Other plant, machinery tooling, furnishings and other assets	112,823	135	(19)	211	(130)	12,519	125,539	274	122	(466)	12,155	137,624
Electricity installations under construction	877,700	709,179	-	173	(54)	(526,343)	1,060,655	671,547	78	-	(960,166)	772,114
Prepayments and PPE under construction	236,644	156,463	-	-	(52)	(77,912)	315,143	169,564	122	(24)	(391,049)	93,756
<b>Total Cost</b>	<b>8,661,495</b>	<b>2,306,554</b>	<b>(19)</b>	<b>14,372</b>	<b>(986)</b>	<b>-</b>	<b>10,981,416</b>	<b>841,389</b>	<b>6,656</b>	<b>(1,717)</b>	<b>(330)</b>	<b>11,827,414</b>
<b>ACCUMULATED DEPRECIATION</b>												
Buildings	(15,321)	(1,312)	-	(184)	-	-	(16,817)	(1,286)	(92)	-	-	(18,195)
Electricity installations	(2,873,410)	(293,412)	-	(6,902)	559	-	(3,173,165)	(370,455)	(3,340)	929	-	(3,546,031)
Other plant, machinery tooling, furnishings and other assets	(84,013)	(8,979)	15	(144)	126	-	(92,995)	(9,574)	(85)	443	-	(102,211)
<b>Total Accumulated depreciation</b>	<b>(2,972,744)</b>	<b>(303,703)</b>	<b>15</b>	<b>(7,230)</b>	<b>685</b>	<b>-</b>	<b>(3,282,977)</b>	<b>(381,315)</b>	<b>(3,517)</b>	<b>1,372</b>	<b>-</b>	<b>(3,666,437)</b>
<b>Impairment</b>	<b>(68,563)</b>	<b>(18,625)</b>	<b>-</b>	<b>(3,339)</b>	<b>-</b>	<b>-</b>	<b>(90,527)</b>	<b>-</b>	<b>(2,037)</b>	<b>-</b>	<b>-</b>	<b>(92,564)</b>
<b>Carrying value</b>	<b>5,620,188</b>	<b>1,984,226</b>	<b>(4)</b>	<b>3,803</b>	<b>(301)</b>	<b>-</b>	<b>7,607,912</b>	<b>460,074</b>	<b>1,102</b>	<b>(345)</b>	<b>(330)</b>	<b>8,068,413</b>

The main additions in 2011 and 2010 relate to the electricity transmission grid in Spain. Additions during 2010 include the acquisition by REE, in accordance with Transitional Provision Nine of Law 17/2007 (4 July), of certain assets forming part of the transmission grid from Endesa Distribución Eléctrica, S.L. for €1,412,128 thousand, from Unión Fenosa Distribución, S.A.U. for €46,922 thousand and from Hidrocantábrico Distribución Eléctrica, S.A.U. for €57,804 thousand. The transfer affected both island energy transmission grids (Canary and Balearic Islands) and assets forming part of the transmission grid on mainland Spain.

In 2011 companies capitalised finance expenses of €24,169 thousand as an increase in property plant and equipment (€25,121 thousand in 2010). The average weighted rate used to capitalised financial expense was 3.3%.

Operating expenses directly related to construction in progress of property, plant and equipment capitalised in 2011 amount to €16,862 thousand (€17,626 thousand in 2010).

In 2011 no impairment losses were recorded (€18,625 thousand in 2010).

To calculate the value-in-use of the international business' CGUs the effective cash flow method was used and various scenarios were examined to which probabilities were assigned:

- a) The value-in-use in the base scenario calculated using the discounted cash flow method using a discount rate: 17.3% (16.3% in 2010) and growth in line with market development, taking into consideration flows up until 2024, which the end of the estimated projection period. The residual value has been calculated as the present value of the regulatory asset updated until the end of 2024.
- b) A scenario relating to the realisable value, using market methods. (supported by comparable transactions and measurements prepared by analysts.
- c) Market scenarios relating to the realisable value that reflect the current situation of the market and the CGUs.

The key assumptions included in the cash flows are the value of the regulatory asset, inflation, residual value and the exchange rate, and the latter is the most sensitive.

## 7. Investment property

Movements in 2011 and 2010 in investment property owned by the Group are described below:

### Red Eléctrica Group

#### Breakdown of movements in Investment properties 2011 and 2010

(thousand euro)

	31 December 2009	Additions	Disposals	31 December 2010	Additions	Disposals	Transfers	31 December 2011
<b>COST</b>								
Investment property	2,309	-	-	2,309	-	-	601	2,910
<b>Total Cost</b>	<b>2,309</b>	<b>-</b>	<b>-</b>	<b>2,309</b>	<b>-</b>	<b>-</b>	<b>601</b>	<b>2,910</b>
<b>ACCUMULATED DEPRECIATION</b>								
Investment property	(151)	(32)	-	(183)	(32)	-	-	(215)
<b>Total accumulated depreciation</b>	<b>(151)</b>	<b>(32)</b>	<b>-</b>	<b>(183)</b>	<b>(32)</b>	<b>-</b>	<b>-</b>	<b>(215)</b>
<b>Carrying value</b>	<b>2,158</b>	<b>(32)</b>	<b>-</b>	<b>2,126</b>	<b>(32)</b>	<b>-</b>	<b>601</b>	<b>2,695</b>

Investment property have a market value of approximately €3 million and do not generate any significant operating revenues or expenses.

## 8. Investments accounted for using the equity method

Movements in 2011 and 2010 in investments accounted for using the equity method are as follows:

### Red Eléctrica Group

#### Breakdown of movements in investments recognised using the equity method 2011 and 2010

(thousand euro)

	31 December 2009	Equity Method	Dividends	Exchange differences	Other	31 December 2010	Equity Method	Dividends	Exchange differences	Other	31 December 2011
<b>REDESUR</b>	5,046	1,003	(778)	(389)	(97)	5,757	925	(909)	538	1,648	4,663
	<b>5,046</b>	<b>1,003</b>	<b>(778)</b>	<b>(389)</b>	<b>(97)</b>	<b>5,757</b>	<b>925</b>	<b>(909)</b>	<b>538</b>	<b>1,648</b>	<b>4,663</b>



In 2011, the heading Other includes USD -1,856 thousand relating to a capital reduction.

The balances recorded by REDESUR for 2011 and 2010 for assets, liabilities, ordinary revenues and results for the year are as follows:

(thousand euro)	2011	2010
Assets	39,147	41,856
Liabilities	25,329	25,167
Ordinary revenues	10,211	10,514
Profit for year	2,742	2,971

## 9. Other non-current assets

Other non-current assets at 31 December 2011 includes €33,200 thousand (€49,482 thousand in 2010), mainly relating to the Technical Assistance Availability Contract with Endesa Distribución Eléctrica, S.L. concluded in 2010 for four years and a total amount of €66,000 thousand. Under this contract REE is entitled to request Endesa Distribución Eléctrica, S.L. to render technical assistance services relating to the assets acquired in 2010.

## 10. Inventories

Details of inventories at 31 December 2011 and 2010 in the accompanying consolidated balance sheet are as follows::

(thousand euro)	2011	2010
Inventories	59,221	55,900
Value adjustments	(14,843)	(12,112)
	<b>44,378</b>	<b>43,788</b>

## 11. Trade and other receivables

The breakdown at 31 December 2011 and 2010 of Trade and other receivables in the accompanying consolidated balance sheet is as follows:

(thousand euro)	2011	2010
Receivables for sales and services rendered	22,775	30,680
Other receivables	343,832	370,716
Current tax assets	1,463	11,068
	<b>368,070</b>	<b>412,464</b>

In 2011 and 2010 other receivables mainly comprise amounts pending invoicing and/or receivable in respect of electricity transmission and system operation activities. This heading also includes pre-payments to creditors, trade receivables and VAT amounts refundable to the Group. At 31 December 2010 the balance under Other receivables included €66 million in VAT refundable to the Group, mainly due to the input VAT paid on the acquisition of transmission assets. There is no significant differences between the fair value and carrying value of this heading at 31 December 2011 and 2010.

At 31 December 2010 current tax assets mainly consist of corporate income tax refundable as a result of the accelerated depreciation of certain Group assets in accordance with the provisions of Law 4/2008 (Note 21).

## 12. Equity

### Capital risk management

The Group's objectives in relation to capital management are to safeguard its capacity to continue as a going concern, secure a return for shareholders, maintain an optimal capital structure and reduce costs.

In order to maintain or adjust the capital structure, the Group could adjust the amount of the dividends payable to shareholders, reimburse capital to shareholders or issue new shares.

The Group monitors capital in accordance with the financial leverage ratio in line with general practice in the sector. This ratio is calculated as net financial debt divided between net assets (understood as the Group's equity plus net financial debt). The net financial debt is calculated as follows:

(thousand euro)	2011	2010
Long-term debts	3,776,873	3,695,291
Short-term debts	909,953	1,041,931
Exchange rate derivative	25,433	37,665
Cash and equivalents	(19,343)	(18,286)
<b>Net financial debt</b>	<b>4,692,916</b>	<b>4,756,601</b>
<b>Equity</b>	<b>1,813,547</b>	<b>1,624,554</b>
<b>Leveraging ratio</b>	<b>72.1 %</b>	<b>74.5 %</b>

At 31 December 2011 the financial covenants set out in the debt agreements are not significant. In addition, there is a low probability of non-compliance and, should that happen, the impact on the company's results would not be significant.



At 31 December 2011 the credit rating granted by Moody's and Standard & Poor's has remained consistent in 2011 at A2 and AA-, respectively. After the end of 2011 and as a result of the recent two level cut in the rating for the Kingdom of Spain, Standard & Poor's lowered the rating from AA- to A+.

## Equity attributed to the parent company

### ◆ Equity

#### - Share capital

At 31 December 2011 and 2010 the share capital of the Parent Company comprises €135,270,000 fully subscribed and paid, in bearer shares, with a par value of €2 each which carry equal voting and dividend rights. The Parent Company's shares have been listed on the four Spanish stock exchanges.

In accordance with Law 17/2007 any natural or legal person may be a company shareholder, provided that the sum of direct or indirect stakes in the Company's capital does not exceed 5% and they do not give rise to voting rights exceeding 3%. These shares cannot be syndicated for any purpose. In the case of entities that carry out activities in the Electricity Sector and those natural or legal persons that hold a direct or indirect stake exceeding 5%, they cannot exercise voting rights exceeding 1% with respect to the company responsible for operating the system. These shareholding limitations with respect to the Parent Company are not applicable to Sociedad Estatal de Participaciones Industriales (SEPI) (Government Industrial Investment Company), which will, in any event, hold a shareholding of at least 10%. At 31 December 2011 and 2010 SEPI held 20% of the Company's share capital.

#### - Reserves

This heading includes:

##### - Legal reserve

Companies in Spain are obliged to transfer 10% of profits each year to the legal reserve until this reserve reaches an amount of at least 20% of share capital. This reserve is not distributable to shareholders and may only be used to offset losses in the event that no other reserves are available. Under certain conditions it may be used to increase share capital. At 31 December 2011 and 2010 it amounts to €54,199k.

##### - Other reserves

This heading includes the voluntary reserves of the Parent Company, reserves in consolidated companies and first application reserves. All of these items are freely available. At 31 December 2011 these reserves total €890,168 thousand (€752,701 thousand in 2010).

The heading also records the reserves required by law, which total €264,546 thousand and among them the Property, plant and equipment restatement reserve generated in 1996 by the parent company is notable at €247,022 thousand (This reserve may be used, without being subject to taxation, to offset losses, increase share capital or be transferred to freely available reserves after 10 years have elapsed, in accordance with the provisions of Royal Decree - Law 2607/1996).

- Treasury shares

At 31 December 2011 the Parent Company holds treasury shares representing 0.62% of the Parent Company's share capital and amounting to 834,774 shares, with an overall par value of €1,670 thousand and an average acquisition price of €34.36 per share (at 31 December 2010, 667,511 shares, which represented 0.49% of share capital, with an overall par value of €1,335 thousand and an average acquisition price of €34.90 per share).

Such shares are carried by reducing the Group's equity at 31 December 2011 by €28,684 thousand (€23,297 thousand in 2010).

The Parent Company has complied with the requirements of Article 509 of the Capital 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 10% of the share capital. The subsidiaries do not hold treasury shares or shares in the Parent Company.

- Profit for the year attributed to the parent company

Profits in 2011 totalled €460,348 thousand (€390,150 thousand at 31 December 2010).

- Interim dividends and proposed distribution of Parent Company dividends

Interim dividends approved by the Board of Directors in 2011 and 2010 are recorded as a decrease in Group equity at 31 December 2011 and 2010, respectively.

On 22 December 2011 the Board of Directors of the Parent Company agreed to pay an interim dividend against 2011 profits amounting to a gross amount of €0.6764 per share, which was payable as from 2 January 2012 (€0.5882 per share on account from 2010 profits). The interim dividend approved at 31 December 2011 totals €90,932 thousand (€79,173 thousand in 2010) (Note 17).

Dividends paid during 2011 and 2010 are as follows:

(thousand euro)	2011			2010		
	% of nominal	Euros per share	Amount (thousand euro)	% of nominal	Euros per share	Amount (thousand euro)
Ordinary shares	93.76%	1.8751	252,792	73.91%	1.4781	198,777
Total dividends paid	93.76%	1.8751	252,792	73.91%	1.4781	198,777
<b>Dividends charged against profits</b>	<b>93.76%</b>	<b>1.8751</b>	<b>252,792</b>	<b>73.91%</b>	<b>1.4781</b>	<b>198,777</b>

The Parent Company's Board of Directors has also proposed to the shareholders at their Annual General Meeting the distribution of a complementary dividend of €1.5360 per share, bringing the total dividend in 2011 to €2.2124 per share (€1.8751 per share in 2010).

#### ◆ Adjustments due to changes in value

##### - Hedging operations

This heading includes variations resulting from derivative financial instruments. At 31 December 2011 this heading reflects a negative balance of € -2,717 thousand (negative balance of € -312 thousand in 2010).

##### - Other adjustments due to changes in value

This heading includes €644 thousand in deferred tax assets deriving from deductions and credits (€0 in 2010).

##### - Exchange differences

This heading includes translation differences in respect of foreign subsidiaries (mainly the Bolivian company TDE) which at 31 December 2011 amount to €-6,239 thousand (€-6,525 thousand in 2010).

### Minority shareholdings

Minority interests recorded under equity in the accompanying consolidated balance sheet reflects the shareholding of minority shareholders in the companies TESUR and TDE. At 31 December 2011 this balance totals €1,674 thousand (€1,725 thousand in 2010).

## 13. Subsidies and other

Movements in subsidies in 2011 and 2010 were as follows:

### Red Eléctrica Group

#### Breakdown of movements in subsidies and other non-recurring advance payments received 2011 and 2010

(thousand euro)

	31 December 2009	Additions	Disposals and Applications	31 December 2010	Additions	Disposals and Applications	31 December 2011
Subsidies and other non-recurring advance payments received	321,177	57,966	(10,382)	368,761	43,540	(11,407)	400,894
	<b>321,177</b>	<b>57,966</b>	<b>(10,382)</b>	<b>368,761</b>	<b>43,540</b>	<b>(11,407)</b>	<b>400,894</b>

The heading Subsidies and other non-current advance payments received mainly includes the amounts received by REE to build electricity facilities and revenue deriving from the agreements relating to the building of electricity facilities. They are released to income for the year over the useful lives of the relevant facilities and are recorded under Non-financial asset subsidies and Other in the consolidated income statement.

In 2010 REE received a grant from the European Commission for the electricity connection project between Spain and France, which it is carrying out together with Réseau de Transport d'Électricité (RTE), through INELFE. The grant is for a maximum amount of €112.5 million, of which €33,750 thousand was received in 2010.

## 14. Non-current provisions

Movements in this heading in the consolidated balance sheet in 2011 and 2010 are as follows:

### Red Eléctrica Group Movements in Provisions 2011 and 2010

(thousand euro)

	31 December 2009	Additions	Applications	Transfers	Changes in scope	Reversals and differences on exchange	31 December 2010
Commitments with personnel	26,097	5,658	(548)	(248)	(56)	64	30,967
Other provisions	27,175	25,175	(85)	-	-	(7,480)	44,785
	<b>53,272</b>	<b>30,833</b>	<b>(633)</b>	<b>(248)</b>	<b>(56)</b>	<b>(7,416)</b>	<b>75,752</b>

	31 December 2010	Additions	Applications	Transfers	Changes in scope	Reversals and differences on exchange	31 December 2011
Commitments with personnel	30,967	3,054	(646)	-	-	32	33,407
Other provisions	44,785	13,535	(1,040)	-	-	(23,261)	34,019
	<b>75,752</b>	<b>16,589</b>	<b>(1,686)</b>	<b>-</b>	<b>-</b>	<b>(23,229)</b>	<b>67,426</b>

The heading Commitments with personnel mainly records future commitments, primarily consisting of medical insurance, assumed by REE with respect to its employees at the time of retirement, calculated based on independent actuarial studies and long-term compensation plans.

In 2011 and 2010 additions result mainly from the annual accrual and development of the actuarial assumptions used. These additions are recorded as Personnel expenses or Financial expense, based on their nature, and under Reserves when there are changes in actuarial assumptions in the case of the obligations deriving from medical insurance and the income statement in the case of obligations deriving from length of service or past service awards. Personnel expenses recognised in 2010 in the consolidated income statement total €1,214 thousand (€2,395 thousand in 2010), the amount of financial expenses recognised in 2010 in the income statement totals €1,273 thousand (€1,126 thousand in 2010) and the amount of Reserves recognised in 2011 totalled € -587 thousand net of taxes (€666 thousand in 2010). In addition, at 31 December 2011 and 2010, Personnel expenses totalling €1,074 thousand (€1,137 thousand in 2010) and Financial expenses €80 thousand (€48 thousand in 2010) relating to the accrual of long-term compensation for executives were recognised in the income statement.

The effect that a one percentage point change in the cost of medical insurance is as follows:

(thousand euro)	2011		2010	
	+1 %	-1 %	+1 %	-1 %
Cost of current year services	272	(195)	273	(195)
Interest expense on post-employment health costs-net	13	(8)	13	(8)
Accumulated obligations for post-employment benefits deriving from health insurance	5,633	(4,108)	5,356	(3,880)

These provisions are stated in accordance with actuarial studies using the following assumptions for 2011 and 2010:

	2011	2010
	Actuarial assumptions	Actuarial assumptions
Discount rate	4.50 %	4.56 %
Growth cost	4.00 %	4.00 %
Survival table	PERM/F 2000 New production	PERM/F 2000 New production

The heading Other provisions mainly records the amounts provided each year by Group companies to cover the possible unfavourable outcome of third-party claims.

In 2011 additions fundamentally consist of the €10 million provision to cover contingent tax risks for the international business relating to 2007-2011.

Reversals in 2011 are mainly due to obtaining favourable outcomes with respect to penalty proceedings initiated by various Regional Governments, for which provisions were recorded last year.

## 15. Other non-current liabilities

Other Non-current liabilities mainly includes revenues from the agreements concluded with several telecommunications operators for the assignment of the use of the telecommunications network, which end between 2016 and 2027 and total €53,793 thousand at 31 December 2011 (€57,850 thousand at 31 December 2010). This heading also includes non-current liabilities deriving from the compensation paid by Électricité de France (hereinafter EDF), by virtue of the agreement to adapt electricity supply contracts concluded on 8 January 1997, totalling €23,625 thousand at 31 December 2011 (€23,625 thousand at 31 December 2010), and since they are multi-year agreements they are subject to the condition that a facility be completed, which had not been completed at 31 December 2011.

## 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 consistently.

The main guidelines which comprise this policy may be summarised as follows:

- ◆ Risk management should be fundamentally proactive and also directed towards the middle and long-term, taking into account possible scenarios in an ever-increasing global environment.
- ◆ Risks should generally 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.
- ◆ Financial risk management should seek to avoid undesired variations in the Group's base value and not to generate extraordinary profits.

The Group's financial managers are responsible for managing financial risks to ensure consistency 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 actions to be taken, based on establishing different financial scenarios.

The methodology for identifying, measuring, monitoring and controlling risks as well as management indicators and measure 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:

### Market risk

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

Management of these risks is carried out both on liability operations, currency, maturity and interest rates and through the use of hedging instruments which allows the aforementioned financial structure to be modified. Particularly noteworthy market risks are:

#### ◆ Interest rate risks

Interest rate variations change the fair value of assets and liabilities which accrue interest at a fixed rate and the future flows of assets and liabilities linked to a variable interest rate. The management of interest rates mainly aims to maintain the structure of the debt ratio between the fixed and hedged rate and risks linked to variable interest rates at approximately 70%-30%. The structure at 31 December 2011 and 2010 is as follows:

(thousand euro)	2011		2010	
	Fixed rate	Variable rate	Fixed rate	Variable rate
Long-term issues	2,603,209	-	1,755,474	-
Long-term bank borrowings	887,826	311,271	1,260,973	798,375
Short-term issues	-	4,758	-	47,431
Short-term bank borrowings	201,997	703,198	-	912,634
<b>Total debt</b>	<b>3,693,032</b>	<b>1,019,227</b>	<b>3,016,447</b>	<b>1,758,440</b>
<b>Percentage</b>	<b>78%</b>	<b>22%</b>	<b>63%</b>	<b>37%</b>

The structure reflects a low risk profile with moderate exposure to interest rate variations. In addition, the impact of the rise in variable interest rates on borrowings is largely offset, provided the investment process continues, in the consolidated income statement by the increase in revenues deriving from the redistribution of the new points of service which is based on the base level of 10-year Spanish Treasury Bonds at that time.

The interest rate risk to which the Group is exposed at 31 December 2011 mainly affects equity for the year as a result of changes in the fair value of derivative financial instruments while profit for the year remains unchanged. Set out below is a sensitivity analysis of that risk:

Effect on consolidated equity (thousand euro)	Change in market interest rates			
	2011		2010	
	+0,10%	-0,10%	+0,10%	-0,10%
Interest rate hedges:				
- Cash flow hedges. Interest rate Swap	3,730	(3,759)	4,767	(4,807)
Interest rate and exchange rate hedges:				
- Cash flow hedge. Cross Currency Swap	(182)	185	282	(289)

The sensitivity of fair value has been estimated using a valuation technique based on discounted future cash flows at market interest rates prevailing at 31 December 2011 and 2010.

#### ◆ Exchange rate risks

Exchange risk management comprises 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 in other than the euro.

In order to eliminate the exchange risk in Private Placements in the United States (USPP), the Company has arranged cash flow hedges through cross currency swaps for the principal and interest covering the amount and entire duration of the same to October 2005 (Note 18).

In order to mitigate the translation risk of the assets located in countries whose functional currency is not the euro, the Group finances part of such investments in the functional currency. Therefore at 31 December 2011 any increase or decrease in the dollar/euro exchange rate of 10% with respect to the year end closing would have generated an increase or decrease in equity of approximately €1 million (€1 million at 31 December 2010).

## Credit risk

The characteristics of income from electricity transmission and electrical systems operation and the solvency of the electrical system agents mean that 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.

In any event, the credit risk is supported through policies containing requirements in relation to the credit standing of the counterparty and additional guarantees are called for, where necessary.

In addition, at the closing there is little exposure to credit risk relating to the fair value of the recognised derivatives.

At 31 December approximately 4% of balances are past due (3% in 2010) although the companies consider that there is no recoverability risk. The receivables are considered to be of high credit quality.

## Liquidity risk

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

Maintaining a significant volume of funds available during the year contributes positively to the strengthening of the Group's financial structure and contributes an additional guarantee of liquidity.

These risks are mainly managed by the controlling of the temporary financial debt structure, setting maximum net volume limits for each defined period. This process is also carried out at the level of several group companies, in accordance with the practices and limits established by the Group. The established limits vary based on geographic areas for the purpose of taking into account the liquidity of the market in which the Company operates. The liquidity management policy includes the realisation of cash flow projections in the main currencies in which it operates, taking into consideration the level of liquid assets that are necessary to attain those projections, the control of balance sheet liquidity indexes and their comparison with market requirements and the maintaining of the financing plans using debt.

Group borrowings have an average maturity of 5 years at 31 December 2011.

The Group's liquidity position for 2011 is based on its strong capacity to generate cash, supported by credit lines drawn down amounting to €1,195 thousand (€245 million in the short-term and €950 million in the long-term). REE has also been granted lines of credit pending formalisation totalling €425,000 thousand.

## Price risk

The Group is exposed to the price risk relating to its investments in capital instruments and classified as available-for-sale on the balance sheet. Available-for-sale investments that are listed mainly relate to the 5% stake the Company holds in REN. At 31 December 2011 the listed price of shares in REN had risen by 10%, thereby generating an increase in equity of approximately €4 million (€5 million in 2010) and a 10% decline in the value would have caused a drop in this value of approximately €4 million (€5 million in 2010).





## 17. Financial assets and liabilities

### Financial assets

The breakdown of the heading Financial assets, both current and non-current, of the Red Eléctrica Group at 31 December 2011 and 2010 is as follows:

(thousand euro)

	Current period			
	Financial assets available for sale	Loans and receivables <sup>(1)</sup>	Hedge derivatives	Total
Equity instruments	56,852	-	-	56,852
Derivatives	-	-	32,185	32,185
Other financial assets	-	2,867	-	2,867
<b>Long-term/non-current</b>	<b>56,852</b>	<b>2,867</b>	<b>32,185</b>	<b>91,904</b>
Derivatives	-	-	36	36
Other financial assets	-	801	-	801
<b>Short-term/current</b>	<b>-</b>	<b>801</b>	<b>36</b>	<b>837</b>
<b>Total</b>	<b>56,852</b>	<b>3,668</b>	<b>32,221</b>	<b>92,741</b>

en miles de euros

	Previous period			
	Financial assets available for sale	Loans and receivables <sup>(1)</sup>	Hedge derivatives	Total
Equity instruments	69,300	-	-	69,300
Derivatives	-	-	7,035	7,035
Other financial assets	-	2,634	-	2,634
<b>Long-term/non-current</b>	<b>69,300</b>	<b>2,634</b>	<b>7,035</b>	<b>78,969</b>
Derivatives	-	-	98	98
Other financial assets	-	88	-	88
<b>Short-term/current</b>	<b>-</b>	<b>88</b>	<b>98</b>	<b>186</b>
<b>Total</b>	<b>69,300</b>	<b>2,722</b>	<b>7,133</b>	<b>79,155</b>

(1) Excluding trade receivables.

#### ◆ Equity instruments

Equities mainly relate to the 5% shareholding that the Parent Company has in REN, the holding company that comprises the operation and exploitation of the electricity transmission assets and various gas infrastructures in Portugal. This shareholding was acquired in 2007 and the transaction price totalled €98,822 thousand.

The value of this shareholding is based on the listed price of the share. At 31 December 2011 there is objective evidence of the impairment of the investment in REN and the value adjustment, measured as the difference between the acquisition price and fair value, has been eliminated from equity and recognised in the income statement. The amount of the impairment loss affecting the shareholding recorded in the Consolidated Income Statement totals €12,549 thousand at 31 December 2011 (€29,935 thousand in 2010).

#### ◆ Derivatives

A breakdown of derivatives is set out in note 18.

#### ◆ Other financial assets

This heading mainly relates to guarantees provided and other surety granted by REE to personnel, maturing in the long-term. There is no significant differences between the fair value and carrying value of this heading at 31 December 2011 and 2010.

The following table shows the Group's financial assets at fair value in accordance with the variables used to calculate fair value at 31 December 2011 and 2010:

(thousand euro)	Current period			
	Level 1	Level 2	Level 3	Total balance
Equity instruments	56,390	462	-	56,852
Derivatives	-	32,221	-	32,221
Other financial assets	-	-	3,668	3,668

(thousand euro)	Previous period			
	Level 1	Level 2	Level 3	Total balance
Equity instruments	69,300	-	-	69,300
Derivatives	-	7,133	-	7,133
Other financial assets	-	-	2,722	2,722

## Financial liabilities

The breakdown of the heading Financial liabilities, both current and non-current, of the Red Eléctrica Group at 31 December 2011 and 2010 is as follows:

(thousand euro)	Current period		
	Loans and payables <sup>(1)</sup>	Hedge derivatives	Total
Bank borrowings	1,199,096	-	1,199,096
Obligations and other marketable securities	2,577,777	-	2,577,777
Derivatives	-	54,395	54,395
Other financial liabilities	208	-	208
<b>Long-term/non-current</b>	<b>3,777,081</b>	<b>54,395</b>	<b>3,831,476</b>
Bank borrowings	912,830	-	912,830
Obligations and other marketable securities	58,453	-	58,453
Derivatives	-	1,482	1,482
Other financial liabilities	720,847	-	720,847
<b>Short-term/current</b>	<b>1,692,130</b>	<b>1,482</b>	<b>1,693,612</b>
<b>Total</b>	<b>5,469,211</b>	<b>55,877</b>	<b>5,525,088</b>

(1) Excluding trade payables.

(thousand euro)	Previous period		
	Loans and payables <sup>(1)</sup>	Hedge derivatives	Total
Bank borrowings	2,027,478	-	2,027,478
Obligations and other marketable securities	1,667,811	-	1,667,811
Derivatives	-	32,483	32,483
Other financial liabilities	208	-	208
<b>Long-term/non-current</b>	<b>3,695,497</b>	<b>32,483</b>	<b>3,727,980</b>
Bank borrowings	952,919	-	952,919
Obligations and other marketable securities	118,008	-	118,008
Derivatives	-	1,276	1,276
Other financial liabilities	767,474	-	767,474
<b>Short-term/current</b>	<b>1,838,401</b>	<b>1,276</b>	<b>1,839,677</b>
<b>Total</b>	<b>5,533,898</b>	<b>33,759</b>	<b>5,567,657</b>

(1) Excluding trade payables.

The following table shows the Group's financial liabilities at fair value in accordance with the variables used to calculate fair value at 31 December 2011 and 2010:

(thousand euro)	Current period			
	Level 1	Level 2	Level 3	Total balance
Derivatives	-	55,877	-	55,877
Other financial liabilities	-	-	10,121	10,121

(thousand euro)	Previous period			
	Level 1	Level 2	Level 3	Total balance
Derivatives	-	33,759	-	33,759
Other financial liabilities	-	-	4,245	4,245

#### ◆ Issue of bonds and other marketable and bank borrowings

Details of bonds and other marketable securities and bank loans at 31 December 2011 and 2010 are as follows:

(thousand euro)	Current period				
	Opening balance 31/12/2010	(+) Issues	(-) Repurchases or redemptions	(+/-) Exchange rate adjustments and others	Closing balance 31/12/2011
Securities in debt markets that required the registration of a prospectus	47,431	58,345	(101,018)	-	4,758
Securities in debt markets that did not require the registration of a prospectus	1,343,985	900,000	(50,000)	(2,296)	2,191,689
Other debt securities issued outside of the European Union	373,820	-	-	12,268	386,088
<b>Total</b>	<b>1,765,236</b>	<b>958,345</b>	<b>(151,018)</b>	<b>9,972</b>	<b>2,582,535</b>

(thousand euro)

	Previous period				Closing balance 31/12/2010
	Opening balance 31/12/2009	(+) Issues	(-) Repurchases or redemptions	(+/-) Exchange rate adjustments and others	
Securities in debt markets that required the registration of a prospectus	117,651	251,931	(322,151)	-	47,431
Securities in debt markets that did not require the registration of a prospectus	847,733	500,000	-	(3,748)	1,343,985
Other debt securities issued outside of the European Union	346,668	-	-	27,152	373,820
<b>Total</b>	<b>1,312,052</b>	<b>751,931</b>	<b>(322,151)</b>	<b>23,404</b>	<b>1,765,236</b>

The fair value of bank borrowings and the issue of bonds and other marketable securities at 31 December 2011 and 2010 is as follows:

(thousand euro)

	Carrying value		Fair value	
	2011	2010	2011	2010
Issues in euro	2,196,447	1,391,416	2,302,515	1,442,838
Issues in dollars	386,088	373,820	446,008	403,889
Bank borrowings in euro	2,058,689	2,922,438	1,966,399	2,889,052
Bank borrowings in foreign currency	45,602	49,546	55,422	51,106
<b>Total</b>	<b>4,686,826</b>	<b>4,737,220</b>	<b>4,770,344</b>	<b>4,786,885</b>

The fair value of bank loans and bonds and other marketable securities has been estimated in full using a valuation technique based on the discounting of future cash flows at the market interest rates in force at each date.

At 31 December 2011 accrued interest payable on these debts amounts to €61,330 thousand (€28,996 thousand in 2010).

Issues in euro at 31 December 2011 reflect:

- Issues of Eurobonds within the framework of the Eurobond Issue Program carried out by Red Eléctrica de España Finance, B.V., with a balance of €798,936 thousand (€848,331 thousand in 2010). During 2011 an issue totalling €50 million was amortised using this program.
- Issues of Eurobonds by Red Eléctrica Financiaciones with a balance of €1,392,753 thousand (€495,654 thousand in 2010). In 2011 two bond issues were carried out for €600 million and €300 million.
- There are also issues of short-term promissory notes amounting to €4,758 thousand (€47,431 thousand in 2010). At 31 December 2010 the Parent company has a Spanish Securities and Exchange Commission registered programme to issue promissory notes up to a maximum limit of €250,000 thousand (€250,000 thousand at 31 December 2010). This programme ended in January 2012 and was not renewed.

Issues in US dollars at 31 December 2011 includes €386,088 thousand (€373,820 thousand in 2010), relating to an issue of USD500,000 thousand obtained on the private placement market in the US (USPP).

At 31 December 2011 long-term bank borrowings and credit facilities in euro total €1,208,933 thousand (€1,225,466 thousand in 2010), as well as the syndicated line of credit totalling €849,756 thousand (€799,333 thousand in 2010 and maturing in 2012). In 2010 there was also a bridge loan obtained to finance the acquisition of transmission assets totalling €897,639 thousand, which has been refinanced through the aforementioned bond issues.

Details of maturity of these issues and bank loans at 31 December 2011 are as follows:

## Red Eléctrica Group

### Breakdown of maturities of issues and bank borrowings at 31 December 2011

(thousand euro)

	2012	2013	2014	2015	2016	Subsequent years	Value adjustments	Total
Issues in euro	4,758	800,000	-	-	500,000	900,000	(8,311)	2,196,447
Issues in dollars	-	-	-	54,100	-	332,329	(341)	386,088
Bank borrowings in euros	896,909	35,824	47,652	247,655	197,655	634,844	(1,850)	2,058,689
Bank borrowings in dollars	8,286	8,522	4,065	3,129	3,087	18,565	(52)	45,602
	<b>909,953</b>	<b>844,346</b>	<b>51,717</b>	<b>304,884</b>	<b>700,742</b>	<b>1,885,738</b>	<b>(10,554)</b>	<b>4,686,826</b>

The average interest rate in 2011 was 3.66% (3.24% in 2010).

At 31 December 2011 Group companies have obtained credit facilities that have yet to be drawn down from credit institutions totalling €1,195 million, €950 million in the long-term (€400 million at 31 December 2010) and €245 million in the short-term (€294 million at 31 December 2010). REE has been granted lines of credit pending formalisation totalling €425,000 thousand.

#### ◆ Derivatives

A breakdown of derivatives is set out in note 18.

#### ◆ Other current liabilities

Details of this heading in the accompanying consolidated balance sheet at 31 December 2011 and 2010 are as follows:

(thousand euro)	2011	2010
Dividend payable	90,933	79,174
Fixed asset suppliers and other payables	631,396	689,576
	<b>722,329</b>	<b>768,750</b>

The balance of asset suppliers and other debts mainly includes the balances due to asset suppliers and items pending settlement with the Spanish electricity system for activities that have been carried out.

## 18. Derivative financial instruments

The Red Eléctrica Group contracts two types of derivatives in compliance with its financial risk management policy: Interest rate swaps and Cross currency swaps or exchange rate hedges. Interest rate swaps consist of a financial swap that exchanges variable interest rate debt for fixed interest rate debt, for which the future cash flows to be hedged are the interest payments. Similarly, cross currency swaps allow for the exchange of fixed rate debt in dollars for fixed rate debt in euro and the future cash flows to be hedged are the payment of interest and capital in dollars. The measurement method for both instruments are analysed in Note 4m) of these notes to the consolidated financial statements. The breakdown at 31 December 2011 and 2010 of both types in euro is indicated below:

	Principal	Maturity date	2011				2010			
			Non-current		Current		Non-current		Current	
			Assets	Liabilities	Assets	Liabilities	Assets	Liabilities	Assets	Liabilities
thousand euro										
<b>Interest rate hedge</b>										
Cash flow hedges:										
Interest rate swap	175,000 thousand euro	Until 2012			36	(1,482)	193	(4,347)	98	(1,276)
Interest rate swap	50,000 thousand euro	Until 2016	164		-	-			-	-
Interest rate swap	575,000 thousand euro	Until 2020		(54,395)			6,381	(25,283)	-	-
<b>Interest rate and exchange rate hedge</b>										
Cash flow hedge: (Cross currency swap)										
Interest rate hedge	500,000 thousand dollars	Until 2035	57,454		-	-	471	34,802	-	-
Exchange rate hedge			(25,433)		-	-	(10)	(37,655)	-	-
			<b>32,185</b>	<b>(54,395)</b>	<b>36</b>	<b>(1,482)</b>	<b>7,035</b>	<b>(32,483)</b>	<b>98</b>	<b>(1,276)</b>

The breakdown of derivative financial instruments by maturity at 31 December 2011 is as follows, in thousand euro:

	Principal	Maturity date					2015 and subsequent	Total
			2012	2013	2014			
thousand euro								
<b>Interest rate hedge</b>								
Cash flow hedges:								
Interest rate swap	175,000 thousand euro	Until 2012	(1,446)	-	-	-	(1,446)	
Interest rate swap	50,000 thousand euro	Until 2016	-	-	-	164	164	
Interest rate swap	575,000 thousand euro	Until 2020				(54,395)	(54,395)	
<b>Interest rate and exchange rate hedge</b>								
Cash flow hedge: (Cross currency swap)								
Interest rate hedge	500,000 thousand dollars	Until 2035	-	-	-	57,454	57,454	
Exchange rate hedge			-	-	-	(25,433)	(25,433)	
			<b>(1,446)</b>	<b>-</b>	<b>-</b>	<b>(22,210)</b>	<b>(23,656)</b>	

## 19. Trade and other payables

Details of trade and other payables in the accompanying consolidated balance sheet at 31 December 2011 and 2010 are as follows:

(thousand euro)	2011	2010
Suppliers	251,915	209,101
Other creditors	18,982	16,142
Current tax liabilities	521	40
	<b>271,418</b>	<b>225,283</b>

The heading Suppliers mainly relates to debts deriving from engineering, construction, maintenance and modification work performed on the electric facilities and items yet to be settled in the Spanish electrical system for activities carried out.

## 20. Information regarding the deferral of payment to suppliers additional provision three.

### "Reporting requirements" established by law 15/2010 (5 July)

In accordance with Law 3/2004 (29 December), which establishes measures to fight against delays in payment for commercial transactions, detailed information regarding the payment of pending balances at the end of 2011 and 2010 is provided below:

#### Red Eléctrica Group

#### Balances realised and pending payment at 31/12/2011 and 31/12/2010

(thousand euro)

	Balances realised and pending payment at closing date			
	2011		2010	
	Amount	%	Amount	%
Payments excluded from the disclosure requirement established by Law 15/2010	75,970	19.86 %	293,745	86.27 %
Within the legal deadline (*)	306,501	80.12 %	46,738	13.73 %
Rest	88	0.02 %	16	0.00 %
<b>Total payments during the year (*)</b>	<b>382,559</b>	<b>100 %</b>	<b>340,499</b>	<b>100 %</b>
Average weighted payments after the deadline (days)	63	-	20	-
Deferrals that at the year end exceed the deadline	92	-	232	-

(\*) Total payments for the year do not include the payments made for the services rendered by the Spanish electricity system operator. These payments amounted to €626,598 thousand in 2011 (€538,527 thousand in 2010). However, these payments have been made within the legal deadline except for €512 thousand in 2011 (€0 in 2010), which exceeded the deadline by 97 days.

The payments excluded from the disclosure requirements established by Law 15/2010 relate to those items to which Law 15/2010 is not applicable (items prior to 5 July 2010, the date that law entered into force).

## 21. Tax situation

The Tax Group of which Red Eléctrica Corporación, S.A. is the Parent company is taxed under the Tax Consolidation System in Spain since 2002. The Tax Group distributes the tax load in accordance with the agreements established between Group companies, which adapts to the stipulations of the Resolutions issued by the Audit and Accounting Institute (ICAC) on 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 2011 the tax group is made up of REI, REE and REF in addition to the Parent Company.

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

(thousand euro)	2011	2010
Consolidated book profit for the year before taxes	683,675	560,448
Permanent differences and consolidation adjustments	12,389	12,863
Consolidated tax base	696,064	573,311
<b>Tax rate</b>	<b>30%</b>	<b>30%</b>
Profit adjusted by tax rate	208,819	171,993
Effect of the application of various tax rates	375	(95)
<b>Tax calculated at the current rate in each country</b>	<b>209,194</b>	<b>171,898</b>
Deductions	(1,013)	(1,598)
Corporate income tax adjustments	15,240	-
<b>Corporate income tax</b>	<b>223,421</b>	<b>170,300</b>
Current corporate income tax	22,565	63,080
Deferred corporate income tax	200,856	107,220
<b>Effective tax rate</b>	<b>32.68%</b>	<b>30.39%</b>

The Adjustment to corporate income tax records the decline in deferred tax assets associated with international investments that have raised doubts as to their recoverability.

Current balances payable to and receivable from public institutions at 31 December 2011 and 2010 are as follows:

(thousand euro)	2011	2010
<b>Current receivables balance</b>		
VAT refundable	4,147	65,908
Taxes refundable	1,463	11,068
<b>Current payables balance</b>		
VAT payable	3,412	1,351
Other taxes payable	7,808	6,155
Corporate income tax payable	521	40

VAT refundable in 2010 mainly relates to the input VAT refundable to the Group on the purchase of the transmission assets acquired in 2010.



In 2010 taxes refundable mainly consist of corporate income tax refundable as a result of the accelerated depreciation of certain Group assets in accordance with the provisions of Law 4/2008.

Deferred tax assets and liabilities at 31 December 2011 and 2010 are as follows:

(thousand euro)	2011	2010
<b>Deferred tax assets</b>		
Retirements and other commitments with employees	11,799	11,537
Subsidies	1,844	1,844
Financial derivatives	7,630	11,392
Impairment	16,088	15,579
Unrestricted depreciation	90,116	-
Rest	(333)	21,031
<b>Total deferred tax assets</b>	<b>127,144</b>	<b>61,384</b>
<b>Deferred tax liabilities</b>		
Accelerated depreciation	538,404	262,756
Non-deductible assets	56,508	56,508
Cash flow hedge	6,465	14,611
Rest	6,239	4,551
<b>Total deferred tax assets</b>	<b>607,616</b>	<b>338,426</b>

Under accelerated depreciation, the amount of unrestricted depreciation established by Law 4/2008 (23 December) totals €488,732 thousand in 2011 (€209,641 thousand in 2010). At 31 December 2011 the Company made investments in the periods covered by unrestricted depreciation (2009 – 2011) that it estimates will give rise to the deferral of approximately €227 million in corporate income tax over the next few years.

The timing differences relating to the recognition of expenses and revenues for accounting and tax purposes, at 31 December 2011 and 2010, the accumulated tax effect, assets and liabilities, are as follows:

(thousand euro)	2011		2010	
	Profit and loss account	Revenues and expenses taken directly to equity	Profit and loss account	Revenues and expenses taken directly to equity
	Increases	Increases	Increases	Increases
<b>Deferred tax assets:</b>				
Originating in prior years	38,616	22,768	31,230	33,504
Movements during the year	76,948	(11,188)	7,386	(10,736)
<b>Total Deferred tax assets</b>	<b>115,564</b>	<b>11,580</b>	<b>38,616</b>	<b>22,768</b>
<b>Deferred tax liabilities:</b>				
Originating in prior years	322,482	15,944	207,876	22,622
Movements during the year	277,804	(8,614)	114,606	(6,678)
<b>Total Deferred tax liabilities</b>	<b>600,286</b>	<b>7,330</b>	<b>322,482</b>	<b>15,944</b>

At 31 December 2011 the Company reported deductions for investments made in the Canary Islands, as defined by Law 20-1991 (7 June), pending application in the amount of €45,642 thousand.

Group companies are open to inspection for all taxes that have not become statute-barred. Due to the possible different interpretations to which tax legislation lends itself, the results of future inspection action that may be taken by the tax authorities for the years open to inspection may give rise to tax liabilities, whose amount cannot be currently quantified in an objective manner. However, the Company's Directors estimate that any liabilities that may arise in which respect will not have a significant effect on the Group's Consolidated Financial Statements.

## 22. Revenues and expenses

### a) Net revenue

Details of this heading in the consolidated income statement for 2011 and 2010 are as follows:

(thousand euro)	Current period	Previous period
Domestical market	1,591,605	1,358,291
Export market	45,731	38,961
<b>Total</b>	<b>1,637,336</b>	<b>1,397,252</b>

The heading Domestic market mainly includes revenues from transmission and operating the Spanish electricity grid, which are set by the Ministry of Industry, Tourism and Commerce.

The heading Foreign market mainly includes revenues from the rendering of transmission services in Bolivia, which are set annually by the Electricity Regulator.

### b) Other operating revenues

This heading in the accompanying consolidated income statement mainly includes income from insurance company indemnities for claims and faults covered by the policies arranged.

### c) Supplies and other operating expenses

Details of this heading in the accompanying consolidated income statement for 2011 and 2010 are as follows:

(thousand euro)	2011	2010
Supplies	42,649	45,022
Other operating expenses	278,741	270,922
	<b>321,390</b>	<b>315,944</b>

Materials consumed and other operating expenses mainly comprise repair and maintenance expenses incurred in electricity plants as well as IT and advisory services, rental costs and other services.

#### d) Personnel expenses

Details of staff costs in the consolidated income statement for 2011 and 2010 are as follows:

(thousand euro)	2011	2010
Wages and salaries	102,160	83,803
Social security	19,475	18,027
Contributions to pension plans and other obligations	1,747	1,357
Other items and social charges	5,464	9,522
	<b>128,846</b>	<b>112,709</b>

At 31 December 2011 Wages and salaries total €10,008 thousand in extraordinary expenses deriving from severance payments.

Group companies have capitalised personnel costs amounting to €15,314 thousand at 31 December 2011 and €15,769 thousand at 31 December 2010.

#### ◆ Current employees

The average number of employees at the Group in 2011 and 2010, by professional category, was as follows:

(thousand euro)	2011	2010
Executive team	118	110
Middle management	22	19
Senior technicians	537	529
Junior technicians	596	571
Specialists and administrative staff	503	466
	<b>1,776</b>	<b>1,695</b>

The distribution of the Group's final headcount at 31 December by gender and category is as follows:

(thousand euro)	2011			2010		
	Men	Women	Total	Men	Women	Total
Executive team	99	19	118	97	17	114
Middle management	19	3	22	16	3	19
Senior technicians	372	166	538	365	166	531
Junior technicians	508	93	601	501	99	600
Specialists and administrative staff	406	115	521	397	102	499
	<b>1,404</b>	<b>396</b>	<b>1,800</b>	<b>1,376</b>	<b>387</b>	<b>1,763</b>

At 31 December 2011 there are 11 Directors, including the Executive Director, of which 8 are men and 3 are women (11 Directors in 2010, 8 men and 3 women).

### e) Impairment and profit/(loss) on fixed asset disposals

In 2010 fundamentally recorded the value adjustment for the CGUs in which REI participates (Note 6).

### f) Financial expense

This heading records the financial expenses, net of financial capitalisation, associated with the Group's financial debts. The capitalisation of financial expense in 2011 totalled €24,169 thousand (€25,121 thousand in 2010).

## 23. Transactions with associates and related parties

### a) Balances and transactions with associates

All transactions with associates have been carried out at market prices. The principal transactions carried out by Group companies with companies consolidated under the equity method in 2011 and 2010 are as follows:

#### Red Eléctrica Group

#### Breakdown of balances and transactions with associated companies in the years ended 31 December 2011 and 2010

(thousand euro)

	2011				2010			
	Balances		Transactions		Balances		Transactions	
	Receivables	Payables	Expenses	Income	Receivables	Payables	Expenses	Income
Red Eléctrica del Sur S.A. (Redesur)	90	89	9	989	80	106	-	1,001
<b>Total</b>	<b>90</b>	<b>89</b>	<b>9</b>	<b>989</b>	<b>80</b>	<b>106</b>	<b>-</b>	<b>1,001</b>

## b) Related party transactions

Transactions with associated parties have been carried out under normal market conditions, as follows in thousand euro:

EXPENSES AND INCOME	2011				
	Significant shareholders	Directors and executives	Group persons, companies or entities	Other associated companies	Total
Management or collaboration contracts	-	-	-	-	-
Other expenses	-	-	-	3,719	3,719
<b>EXPENSES</b>	-	-	-	<b>3,719</b>	<b>3,719</b>
Dividends received	-	-	-	4,486	4,486
Other income	-	-	-	19	19
<b>INCOME</b>	-	-	-	<b>4,505</b>	<b>4,505</b>
<b>OTHER TRANSACTIONS</b>					
Dividends and other profits distributed	-	-	-	-	-
Other transactions	-	-	-	1,793	1,793
<b>OTHER TRANSACTIONS</b>	-	-	-	<b>1,793</b>	<b>1,793</b>

EXPENSES AND INCOME	2010				
	Significant shareholders	Directors and executives	Group persons, companies or entities	Other associated companies	Total
Management or collaboration contracts	-	-	-	-	-
Other expenses	-	-	-	1,655	1,655
<b>EXPENSES</b>	-	-	-	<b>1,655</b>	<b>1,655</b>
Dividends received	-	-	-	4,459	4,459
Other income	-	-	-	5	5
<b>INCOME</b>	-	-	-	<b>4,464</b>	<b>4,464</b>
<b>OTHER TRANSACTIONS</b>					
Dividends and other profits distributed	-	-	-	-	-
Other transactions	-	-	-	3,968	3,968
<b>OTHER TRANSACTIONS</b>	-	-	-	<b>3,968</b>	<b>3,968</b>

## 24. Remuneration of members of the board of directors

A breakdown of this remuneration at 31 December 2011 and 2010 in accordance with the information model introduced by the National Securities Market Commission, which was approved in Circular 4/2007 of 27 December 2007 for the Annual Corporate Governance Report, is as follows, in thousand euro:

	2011	2010
<b>Compensation item:</b>		
Fixed compensation <sup>(2)</sup>	404	388
Variable compensation	1,286	1,193
Per diems <sup>(3)</sup>	819	902
Life insurance premiums and pension plan contributions <sup>(2)</sup>	17	12
<b>Total compensation <sup>(1)</sup></b>	<b>2,526</b>	<b>2,495</b>

(1) Remuneration for the Board of Directors, excluding the Chairman's compensation due to his executive duties, totaled €1,886 thousand, the same amount as in 2010. This remuneration has remained unchanged since 2007.

(2) The fixed compensation paid to the Chairman for his executive duties totalled €429 thousand, which is the same amount as in 2010 and unchanged since 2008. As a member of the Board of Directors of REN's Board of Directors, the CEO has received compensation totalling €8 thousand in 2011 (€29 thousand in 2010). Since April 2011 REC is the legal person Director on REN's Board of Directors and the Company therefore directly receives this compensation as of that date. Accordingly, for the CEO the sum of the fixed compensation, life insurance and pension contributions, together with the compensation for his duties as a member of REN's Board of Directors totals €429 thousand in 2011 (€429 thousand in 2010).

(3) The change is due to the fact that in 2011 11 Board meetings were held, whereas in 2010 there were 13.

The compensation paid, by type of Director, at 31 December 2011 and 2010 is as follows, in thousand euro:

	2011	2010
<b>Type of Director:</b>		
Executives	822	796
Investor appointed Directors	517	535
Independent Directors	1,187	1,164
<b>Total Compensation</b>	<b>2,526</b>	<b>2,495</b>

The CEO's compensation, including compensation from REN, would total €831 thousand in 2011 (€825 thousand in 2010). The change in 2011 compensation compared with 2010 is basically due to the variable compensation.

Total remuneration in thousand euro accrued by the members of the Company's Board of Directors in 2011, by Director, is as follows:

	Fixed compensation	Variable compensation	Per diems for attending Board and Commission meetings	Attendance to Committees	Life insurance premiums and pension plan contributions	Total
Mr. Luis M <sup>a</sup> Atienza Serna	404	316	56	29	17	822
Mr. Antonio Garamendi Lecanda	-	97	56	29	-	182
Mr. Manuel Alves Torres <sup>(1)</sup>	-	97	56	29	-	182
Mr. Rafael Suñol Trepát	-	97	56	-	-	153
Mrs. María de los Ángeles Amador Millán	-	97	56	29	-	182
Mr. Francisco Javier Salas Collantes	-	97	56	17	-	170
Mr. José Folgado Blanco	-	97	56	12	-	165
Mrs. Arantza Mendizábal Gorostiaga	-	97	56	29	-	182
Mrs. María Jesús Álvarez <sup>(1)</sup>	-	97	56	29	-	182
Mr. Miguel Boyer Salvador	-	97	56	-	-	153
Mr. Rui Manuel Janes Cartaxo	-	97	56	-	-	153
<b>Total accrued compensation</b>	<b>404</b>	<b>1,286</b>	<b>616</b>	<b>203</b>	<b>17</b>	<b>2,526</b>

(1) Amounts received by Sociedad Estatal de Participaciones Industriales (SEPI).

In addition, the CEO has paid €56 thousand to the Group life-savings insurance policy associated with retirement, charged against compensation for prior years yet to be received.

The variable annual compensation for the CEO is established by the Corporate Governance and Responsibility Committee at the start of each year, using pre-determined objective policies that can be quantified. The objectives are aligned with the strategies and actions established in the Company's Strategic Plan and the measurement of compliance is also determined by the Corporate Governance and Responsibility Committee.

In 2009 an executive compensation plan was established (25th Extraordinary Plan 2009-2013), associated with the Company's 25th anniversary, as a management tool and a mechanism to provide incentives to meet the five-year Strategic Plan and it includes the CEO. Compliance with this program will be evaluated when it expires in 2014. Based on whether or not the established objectives are met, the overall value over the five years with 100% compliance could reach a maximum of 1.8 times annual fixed compensation. As is the case with annual objectives, this programme takes into account pre-determined objective policies that may be quantified, aligned with the medium and long-term view of the Company's Strategic Plan and the setting of the amount is the purview of the Corporate Governance and Responsibility Committee. At 31 December 2011 the Company has recorded an accrual in proportion to the period elapsed, with the assumption that in 2013 the objectives established in the plan will be reached but this accrual will not be individually attributed to compensation until compliance with the programme is evaluated in 2014 or, if the executives covered by that plan cease to be associated with the company, for the reasons stated.

In 2010 the Company liquidated a previous long-term compensation plan totalling €429 thousand.

The executive director contract contains clauses regarding guarantees and safeguards in respect of dismissal or changes in control. This agreement have been proposed by the Appointments, Remuneration and Corporate Governance Committee (currently called Corporate Governance and Responsibility Committee) at the Company and approved by the Board of Directors. These clauses follow usual market practice and include clauses regarding termination of employment and indemnities of one year unless applicable legislation requires a greater indemnity to be paid.

At 31 December 2011 and 2010 no loans, advances or guarantees to members of the Board of Directors of the Parent company are reflected in the balance sheet. Nor are there at that date any pension commitments with members of the Board of Directors.

In 2011 and 2010 the members of the Board of Directors have performed no extraordinary operations or transactions under conditions other than market, directly or through intermediaries, with the Company or Group companies.

Details of the interests held by the members of the Parent Company and related parties, for the purposes of Article 231 of the Capital Companies Act, at 31 December 2011 in the share capital of companies with a similar or complementary activity to that of the Company, 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 Company.



## 25. Management remuneration

In 2011 senior management remuneration and life insurance and pension plan contributions amounted to €966 thousand and €57 thousand, respectively (€957 thousand and €30 thousand, respectively, in 2010). In addition, the CEO has paid €34 thousand to the Group life-savings insurance policy associated with retirement, charged against compensation for prior years yet to be received.

Senior managers who have provided their services in 2011 and 2010 are as follows:

<u>Name</u>	<u>Position</u>
Carlos Collantes Pérez-Ardá	General Manager of Transmission
Esther M <sup>a</sup> Rituerto Martínez	General Manager of Administration and Finance
Alberto Carbajo Josa	General Manager of Operations

At 31 December 2011 and 2010 no loans or advances have been granted to these managers.

There are guarantee or safeguard clauses for two of these managers in the event of dismissal. The clauses of the contracts follow usual market practice and include clauses regarding termination of employment and indemnities of up to two years unless the applicable legislation requires a greater indemnity to be paid. The contracts containing such clauses are approved by the Committee of Appointments, Remuneration Corporate Governance and reported to the Board of Directors.

In 2009 an executive compensation plan was established (25th Anniversary Extraordinary Plan 2009-2013), associated with the Company's 25th anniversary, as a management tool and a mechanism to provide incentives to meet the five-year Strategic Plan. Compliance with this program, which includes these executives, will be evaluated at the end of the period in 2014. Based on whether or not the established objectives are met, the overall value over the five years with 100% compliance could reach a maximum of 1.8 times annual fixed compensation. As is the case with annual objectives, this programme takes into account pre-determined objective policies that may be quantified, aligned with the medium and long-term view of the Company's Strategic Plan and the setting of the amount is the purview of the Corporate Governance and Responsibility Committee. At 31 December 2011 the Company has recorded an accrual in proportion to the period elapsed, with the assumption that in 2013 the objectives established in the plan will be reached but this accrual will not be individually attributed to compensation until compliance with the programme is evaluated in 2014 or, if the executives covered by that plan cease to be associated with the company, for the reasons stated. In 2010 the Company liquidated a previous long-term compensation plan totalling €689 thousand.

## 26. Segment reporting

The Red Eléctrica Group's core activity is the transmission of electricity and operation of the electricity system in Spain through REE which accounts for 93% of the Group's consolidated revenues and 98% of total assets (92% and 97%, respectively, in 2010). All other activities taken together make up the remaining 7% of revenues and 2% of total assets (8% and 3%, respectively, in 2010). It has therefore not been considered relevant to provide information by activity or geographical segment.

## 27. Interests in combined businesses

REE participates in a combined business with a 50% stake together with RTE EDF Transport in the Company Interconexión Eléctrica Francia-España, S.A.S (INELFE), domiciled in Paris and whose purpose is the study and execution of the future expansion of the connection capacity between Spain and France. The combined business is consolidated using the proportional method.

The breakdown of the financial figures in local accounts that are most relevant in 2011 and 2010 is as follows:

(thousand euro)	Current period			
	Total assets	Total liabilities	Ordinary income	Profit for year
<b>INELFE</b>	202,786	198,423	111,444	2,197

(thousand euro)	Previous period			
	Total assets	Total liabilities	Ordinary income	Profit for year
<b>INELFE</b>	11,039	8,872	4,702	76

## 28. Guarantees and other obligations with third parties and other contingent liabilities

The Company secures, jointly and severally with REE, the eurobond program established in Holland up to €1,500 million, with respect to the private issue of bonds in the United States totalling \$500 million carried out by RBV Group, and the Eurobond program carried out by REF up to the amount of €2,500 million.

Additionally, REI secures the loan that the Bolivian company TDE has with International Finance Corporation (hereinafter IFC) and Corporación Andina de Fomento (CAF). The commitments entered into by REI with IFC and CAF include maintaining both a minimum shareholding in TDE and effective control of that company and being secondarily liable for the payments to be made to IFC and CAF. REI guarantees the loan that the Peruvian company TESUR obtained from BBV Banco Continental.

At 31 December 2011 the principal long-term contracts and commitments to which Group companies are party are as follows:

- ◆ Contracts signed with different telecommunication operators for the assignment of use of capacity, management and maintenance of the telecommunication network, maturing in the period 2016 to 2027.
- ◆ Agreements relating to the supply of equipment and materials and the rendering of services associated with the construction of electricity facilities.

At 31 December 2011 the Group has bank guarantees in favour of third parties deriving from its normal course of business amounting to €44,782 thousand (€36,286 thousand in 2010).

## 29. Environmental information

During 2011 Group companies incurred ordinary expenses of €20,447 thousand to protect and improve the environment (€18,909 thousand in 2010). These expenses relate mainly to the application of preventive and corrective measures at facilities in operation. They also include the maintenance of environmental management systems, sundry environmental communication and training activities, environmental research projects and expenses relating to the organisational unit especially devoted to these tasks.

Similarly, in 2011 environmental impact and supervision studies have been performed in relation to new electricity installations, valued at €7,262 (€6,399 thousand in 2010).

Group companies are involved in no litigations relating to environmental protection or improvements which may give rise to significant contingencies. Similarly, in 2011 and 2010 the Group companies have received no significant environmental grants.

## 30. Other information

The auditor of the Group of companies has been PricewaterhouseCoopers Auditores, S.L. since 2006. The fees accruing from the audit of the Group companies in 2011 totalled approximately €227 thousand (€207 thousand in 2010).

Furthermore, in 2011 fees accrued to firms that are directly or indirectly related to the audit firm for professional services other than audit services in the amount of €110 thousand.

## 31. Earnings per share

Details of earnings per share for 2011 and 2010 are as follows:

	2011	2010
Net profit (thousand euro)	460,348	390,150
Number of shares (shares)	135,270,000	135,270,000
Average number of treasury shares in the portfolio (shares)	543,097	693,936
Basic earnings per share (euro)	3.42	2.90
Diluted profit per share (euro)	3.42	2.90

At 31 December 2011 and 2010 the Group has not performed any operations which would result in any differences arising between basic earnings per share and diluted earnings per share.

## 32. Share-based payments

Share-based payments at 31 December 2011 and 2010 are as follows:

### Red Eléctrica Group

#### Share-based payments at 31 December 2011 and 2010

	2011			2010		
	Number of shares	Average price (euro)	Amount in thousand euro	Number of shares	Average price (euro)	Amount in thousand euro
Management	1,136	42.20	48	1,208	39.63	48
Employees	24,688	36.18	893	65,538	37.15	2,435
<b>Total</b>	<b>25,824</b>	<b>36.45</b>	<b>941</b>	<b>66,746</b>	<b>37.19</b>	<b>2,482</b>

These shares have been valued at the listed price on the date of delivery. All of these deliveries have been made by virtue of the authorisation granted to the parent company by shareholders at a General Meeting.

## 33. Events subsequent to 31 December 2011

Together with REE, the Company has secured the issue of bonds in the euromarket on 13 February 2012 by REF, within the framework of the program to issue Guaranteed Euro Medium Term Note Programme (EMTN Programme).

This issue, totalling €250 million and maturing in 8 years, bearing a annual yield of 4.875% and an issue price of 102.131%.

## SCHEDULE I

Company Address • Main activity	Percentage shareholding*	
	Direct	Indirect
<b>Red Eléctrica Corporación S.A., parent company, incorporated in 1985.</b> Paseo Conde de los Gaitanes, 177. Alcobendas. Madrid. (Spain). • Management of the business group, rendering of assistance or support services to investee companies or operation of property owned by the Company. • Management for long-term international energy contracts. Activity cancelled over the course of 2010.		
<b>A) Companies consolidated using the Full consolidation method</b>		
<b>Red Eléctrica de España, S.A.U. (REE)</b> Paseo Conde de los Gaitanes, 177. Alcobendas. Madrid. (Spain). • Transmission services and operation of the Spanish electrical system and the management of the transmission grid.	100%	-
<b>Red Eléctrica Internacional, S.A.U. (REI)</b> Paseo Conde de los Gaitanes, 177. Alcobendas. Madrid. (Spain). • International shareholdings. Rendering of consulting, engineering, construction and telecommunications services. • Performance of electricity activities outside the Spanish electrical system.	100%	-
<b>Red Eléctrica de España Finance, B.V. (RBV)</b> Claude Debussylaan, 24. Amsterdam (Holland). • Financing activities. • Incorporated in 2003 in Holland (Member of the European Union) to issue debt for Red Eléctrica Group for an amount higher than the limit established by Spanish law.	100%	-
<b>Red Eléctrica Financiaciones (REF)</b> Paseo Conde de los Gaitanes, 177. Alcobendas. Madrid. (Spain). • Financing activities.	100%	-
<b>Redcor Reaseguros, S.A (REDCOR)</b> 23, Avenue Monterey. (Luxembourg). • Reinsurance activities. • Incorporated in 2010 in Luxembourg (Member of the European Union) to reinsure the risks affecting group companies, guaranteeing better access to international markets.	100%	-
<b>Red Eléctrica Andina, S.A. (REA)</b> Av. Alfonso Ugarte N° 536 Cercado. Arequipa (Peru).** • Line and substation maintenance services.	-	100% <sup>(1)</sup>
<b>Transportadora de Electricidad, S.A. (TDE)</b> C/ Colombia, N° 00655, casilla, N° 640. Cochabamba (Bolivia). • Transmission of electricity.	-	99.94% <sup>(1)</sup>
<b>Transmisora Eléctrica del Sur , S.A. (TESUR)</b> Juan de la Fuente, 453. Lima (Peru). • Transmission of electricity and the operation and maintenance of electricity transmission networks.	-	55% <sup>(1)</sup>
<b>B) Companies consolidated using the proportional method</b>		
<b>Interconexión Eléctrica Francia-España, S.A.S. (INELFE)</b> Tour Ampère, 34 Rue Henri Régnault, 92068 La Défense Cedex. Paris (France). • Study and execution of the expansion of the capacity of the connection between Spain and France.	-	50% <sup>(2)</sup>
<b>C) Companies consolidated using the Equity method</b>		
<b>Red Eléctrica del Sur, S.A. (REDESUR).</b> Juan de la Fuente, 453. Lima (Peru). • Transmission of electricity and the operation and maintenance of electricity transmission networks.	-	33.75% <sup>(1)</sup>

\* Equivalent to voting rights.

\*\* From February 2011. Previously it was: Urbanización Independencia Americana, D-8. Yanahuara. Arequipa (Peru).

(1) Shareholding through Red Eléctrica Internacional

(2) Shareholding through Red Eléctrica de España.



## SCHEDULE II

### Red Eléctrica Corporación, S.A.

#### Information relating to Members of the Board of Directors at 31 December 2011

Members of the Board of Directors	Position on the Board of Directors	Direct or indirect shareholdings held by the Members of the Board of Directors and related parties in companies with the same, similar or supplementary corporate purpose as the Company	Positions and duties of the Members of the Board of Directors and related parties in companies outside Red Eléctrica Group with the same, similar or supplementary corporate purpose as the Company
Mr. Luis M <sup>a</sup> Atienza Serna	Chairman	----	Director of REN-Redes Energéticas Nacionais, SGPS, S.A.
Mr. José Folgado Blanco		----	----
Mrs. Arantza Mendizábal Gorostiaga		----	----
Mr . Antonio Garamendi Lecanda		----	----
Mr. Manuel Alves Torres		----	----
Mrs. María Jesús Álvarez González		----	----
Mr. Rafael Suñol Trepát		----	----
Mrs. María de los Ángeles Amador Millán		----	----
Mr. Francisco Javier Salas Collantes		----	----
Mr. Miguel Boyer Salvador		----	----
Mr. Rui Manuel Janes Cartaxo			Chairman of REN-Redes Energéticas Nacionais, SGPS, S.A.

The members of the Board of Directors have stated that they are not in any conflict of interest situations for the purposes of Article 229 of the Capital Companies Act. None of the members of the Board of Directors or associated parties has carried out on his own or third-party account any activities of any activity analogous or complementary to the kind of activity which makes up the Company's objects.



3

Consolidated directors'  
**report**



## Business trends. Most significant events

In 2011, RED ELÉCTRICA GROUP obtained satisfactory financial results and attained significant achievements in the various Group activities.

### Activities in Spain

RED ELÉCTRICA GROUP continues to have the objective of providing a quality service to society through efficient management of the Spanish electrical system and the construction and development of a transmission network grid that is robust and reliable, taking all action with the maximum respect for the environment and choosing locations and pathways that have the least socio-environmental impact as possible in order to achieve a more sustainable and efficient energy model.

Investments in the national grid in 2011 totalled €819 million, laying 1,739 km of lines to attain 40,133 km of circuits. During the year 247 substation positions were launched and the transformation capacity increased by 2,700 MVA. The most significant action relating to the transmission network taken during the year was as follows:

- ◆ Advances on the work on the connection with France.
- ◆ The completion of the connection with the Balearic Islands.
- ◆ The connection between the northwestern zone with the plains, that will facilitate the evacuation of wind generated energy from Galicia and the improvement of the connection with Asturias.
- ◆ The development of the central electricity axis, which will reinforce the connection between the Central Mediterranean Coast and the centre of the country.
- ◆ Development of the network that links Aragon with the Central Mediterranean Coast.

The completion of the connection with the Balearic Islands is the most notable point of among the projects carried out in 2011. This link is the first underwater continuous current connection that exists in Spain and its development represents an international milestone of reference due to its uniqueness and technical complexity. The connection involved the laying of two 237 km cables at a maximum depth of 1,485 below sea level and it is the second deepest electricity line in the world.

It will give rise to a significant cost savings for the Spanish electric sector as it allows more expensive island generation to be supplemented by energy from the peninsula and it will improve the reliability and quality of the supply of electricity to the Balearic Island system.

The execution of the project has pursued maximum respect of the environment at all times, avoiding archaeological sites, minimising the impact on protected flora and fauna and possible effects on the tourism and fishing sectors.



As regards the reinforcement of international connections, the following should be noted:

◆ **The new connection with France**

In this connection, the electricity connection between Spain and France started in 2008 and is expected to enter into commercial service in 2014. The connection will allow our current exchange capacity with Europe to double to 6% of maximum demand in Spain. This project is being carried out together with Réseau de Transport d'Électricité (RTE), through the joint venture INELFE, in which the Spanish and French operators each have an equal 50% stake.

This connection has been classified as a priority by the European Union and its characteristics make it a maximum level technological challenge. In 2011 the necessary permits continued to be requested and obtained and work has commenced on the drilling of the tunnel in Junquera and the land preparation work at the conversion station in Santa Llogaia.

◆ **The expansion of the connection with Portugal**

Work is currently being carried out on the Portugal North connection project, which is intended to reinforce the connection between Galicia and northern Portugal.

In 2011 the most notable events were:

- ◆ The performance in the transmission network in Spain has once again been excellent with total availability of the network in 2011 at 97.65%. This reveals the high quality of the installations.
- ◆ The demand for electricity on mainland Spain totalled 255,324 GWh, 2.0% less than in 2010. Adjusting for the effects of work schedules and temperature, the annual decline was 1.1% compared with the 2.9% growth recorded in 2010.

The maximum annual demand for hourly average power and daily energy was reached on 24 January at 44,107 MW and 25 January with 884 GWh, respectively, both of which was 1.7% and 2.5% lower than the historic maximums recorded in 2007.

- ◆ Renewable energies covered approximately 33% of 2011 demand, 3 points less than in the preceding year, mainly due to the decline in hydrological energy sources. Wind energy has maintained its share of demand coverage at 16% of the total, the same as last year despite the fact that wind energy was notably lower than in 2010 and it is the third biggest source of electricity after nuclear and combined cycle plants while solar (photovoltaic and thermoelectric) represented 4% of annual demand coverage. At 2am on 6 November 2011 a new maximum demand coverage by wind energy was recorded at 59.6%, exceeding the previous maximum of 54% attained on 9 November 2010, which gave rise to a management challenge for the system operator.
- ◆ For the eighth consecutive year exports of energy exceeded imports by 6,091 GWh, although that was 27% less than in 2010. This decline is due to the increase in imports through the connection with France, changing the net balance of this connection from positive to negative compared with the preceding year.

## Activities outside of Spain

RED ELÉCTRICA GROUP activities abroad are carried out by REI through its investments in Bolivia (TDE) and Peru (REDESUR, REA and TESUR) and through REC with its investments in Luxembourg (REDCOR) and Holland (RBV).

REI continues to carry out activities intended to continuously improve its international business, materialised through its commitment to make the necessary investments in Bolivia and Peru. In addition, during 2011 the Company continued to optimise its business management, thereby guaranteeing the optimal quality of its electricity services in those countries.

In 2011 TDE maintained a sustained rate of investment in the Bolivian electricity market, commencing the execution of five projects involving an investment of USD9.6 million. The first of these projects, the 230 kW expansion of the Chimoré Substation, has been concluded and launched on 18 December 2011.

It should be noted that in 2011 REDESUR approved a capital reduction totalling USD5,500 thousand, which represents 30% of share capital and consisted of the refunding of monetary contributions to shareholders.

TESUR has continued to develop its financial and supply plans that are necessary to build, operate and maintain the 220 kW transmission network between Tintaya and Socabaya in Peru.

REDCOR's reinsurance activity had a very satisfactory year in terms of coverage and claims.

RBV (financial subsidiary in Holland) amortised a €50 million issue at maturity and this year is focusing on REF's issue activity (financial subsidiary in Spain) consisting of two new issues totalling €300 million and €600 million, respectively.

## Main financial figures

In 2011 **Profits after taxes** totalled €460.3 million, which represents 18.0% growth over the figure obtained in 2010.

**Revenues** in 2011 totalled €1,637.3 million and grew by 17.2%, mainly due to the increase in the asset base generating revenues due to the facilities launched in 2010 and the compensation associated with transmission assets since their acquisition in mid-2010.

**The gross operating profit (EBITDA)** totals €1,215.2 million, which represents 21.3% growth compared with 2010.

The **cost of Supplies and Other operating costs**, increased by 1.7% compared with the preceding year.

**Personnel expenses** increased by 14.3% compared with last year, if the expenses recorded in 2011 relating to severance payments and shares delivered in 2010 for the company's 25th anniversary are excluded the increase would have been 8.2%. The average number of employees increased by 4.8%. The average payroll at RED ELÉCTRICA GROUP at 31 December 2011 is 1,776 employees. The final number of employees was 1,800, 2.1% more than in December 2010.

**Net operating profits (EBIT)** increased by 22.6% compared with 2010. This increase is affected by the fact that in 2010 a provision was recognised for the impairment of assets totalling €18.6 million, compared with €0 million in 2011.

**Financial income/expense** totalled €-161.1 million compared with €-129.1 million recorded in 2010. Financial income amounted to €6.7 million and includes €4.5 million relating to the dividend paid by REN in the second quarter. Net financial expenses from capitalizations totalled €155.3 million compared with €104.3 million last year, mainly as a result of the increase in the average balance of financial debt arising on the acquisition of transmission assets the previous year.

**Investments** made by the GROUP in 2011 totalled €844.3 million. Investments during the year relating to the development of the national transmission grid totalled €818.9 million and €865.4 million the preceding year.

**Dividends** paid at 31 December 2011 total €252.8 million and are 27.2% higher than the payment made in 2010.

The **Net financial debt** carried by RED ELÉCTRICA GROUP at 31 December 2011 totalled €4,692.9 million. At 31 December 2011 the credit rating granted by Moody's and Standard & Poor's has remained consistent in 2011 at A2 and AA-, respectively. After the end of 2011 and as a result of the recent two level cut in the rating for the Kingdom of Spain, Standard & Poor's lowered the rating from AA- to A+.

With regard to interest rates, 78% of the Group's debt is at a fixed rate, while 22% is at variable rates.



During the first quarter of 2011 the average cost of the Group's financial debt has been 3.66%, with an average balance of € 4,759.2 million. During the same period in 2010, the average cost of the debt was 3.24% and the average balance was € 3,885.0 million.

At 31 December 2011, the RED ELÉCTRICA GROUP's equity stood at € 1,813.5 million, 11.6% higher than at the end of 2009. This growth is due to the profits for the period, partially offset by the distribution of 2010 profits and the interim dividend in 2011.

## Stock market trends and yields for investors

As the Group's listed company, REC forms part of the IBEX-35 and its weighting in that index at the end of 2011 was 1.39%. Throughout 2011 the Company's free-float was 80%.

At the end of 2011 the Company's market capitalisation was €4,472.7 million.

The sovereign debt crisis in Europe largely dominated 2011 and solvency problems in eurozone peripheral countries has been moving to the rest of the countries in the Monetary Union in the form of lower growth. In this context, the value of REC shares could not avoid the negative conditions affecting equity markets and fell 6.1% over the course of the year. However, this drop was less than the decline in the IBEX35 and lower than those affecting most European bourses.

Nevertheless, REC has maintained its commitment to maximise value for its shareholders and offered a high dividend yield in 2011.

## Treasury shares

In order to facilitate depth and liquidity levels to investors in 2011 the Company acquired 4,534,765 shares for an overall par value of €9.1 million and a cash value of €167.0 million. The number of shares sold amounted to 4,367,502, with a overall par value of €8.7 million and a cash value of €162.4 million.

At 31 December 2011 the Company held 834,774 treasury shares that represented 0.62% of its share capital, whose overall par value was €1.7 million and their market value was €27.6 million.

The Company has complied with the requirements of Article 509 of the Capital Companies Act, which establishes that the par value of acquired shares listed on a secondary market, together with those already held by the Company and its subsidiaries must not exceed 10% of the share capital. Subsidiaries do not hold any shares in the Company or any treasury shares.

## Risk management

RED ELÉCTRICA GROUP has established a Risk Control System that covers all of its activities and is adequate to its risk profile. The Risk Policy and the General Integral Risk Management and Control Procedure are based on the integrated business management framework established in the COSO II Report (Committee of Sponsoring Organisations).

The main risk identified with respect to attaining REC's objectives is credit risk, given that debt transactions are carried out through GROUP companies, which assume these market and liquidity risks, as well as regulatory, operational and environmental risks that are inherent to the activities carried out by the GROUP.

The policies to hedge against risks are detailed in Note 16 of the Notes to the Consolidated Annual Accounts for the year.

## Environment

RED ELÉCTRICA GROUP faces the challenge of making the development of its electricity infrastructure compatible with the conservation of the environment to attain an efficient balance between business activity and sustainability.

To minimise the effects of its facilities the Group carried out an environmental evaluation of all its projects and is developing several measures to protect the environment in all stages of its activities. To do so it has implemented an Environmental Management System certified by ISO 14001.

Furthermore, RED ELÉCTRICA GROUP has assumed a special commitment to preserve the environment and biodiversity, carrying out several environmental improvement projects in collaboration with the government and NGOs. Among them are those related to the protection of birds and the prevention of forest fires.

In 2011 RED ELÉCTRICA approved its own Climate Change Strategy intended to formalise its commitment to the development of a sustainable energy model, the reduction of its carbon footprint and reinforce its goal of energy efficiency.

All of the activities intended to protect the environment that RED ELÉCTRICA GROUP carries out in its various areas of operation (environmental supervision, protection of biodiversity, pollution prevention, prevention of fires, treatment of safety pathways, environmental training, compensatory measures, etc.) are integrated into the Environmental Management System and are included in the Environmental Report that is published each year.

During 2011 RED ELÉCTRICA GROUP incurred ordinary expenses for the protection and improvement of the environment totalling €20 million. In addition, the investment in environmental action totalled €7 million during 2011.

## Research, development and innovation (R&D&I)

The research, development and innovation activities taken by RED ELÉCTRICA is intended, within its corporate strategy, to guarantee the efficiency, security and sustainability of the facilities that support the electrical system.

In 2011 the Technology Plan 2008-2012 was completed and the New Technological Innovation and Development Plan for RED ELÉCTRICA was approved. The fundamental objective of this plan is to establish the framework for the Company's technological strategy for the period 2012-2016.

At the international level, in 2011 RED ELÉCTRICA's participation in the update of the Research and Development Plan by ENTSO-E and leadership in the recently created ENTSO-E, Monitoring and Knowledge Sharing working group is notable. The purpose of these actions is to define certain compliance indicators for that plan, which will also contribute to attaining the European Union energy policy.

During 2011, the efforts made by RED ELÉCTRICA on R&D&I projects have translated into €7.2 million in expenses and investments for the development of 56 projects.

In 2011 the following projects ended, among others: ATLAN (application for documenting and configuring substations), GAD (active demand management), CONSOLIDA (improvement of electricity generation using thermosolar technology), VULCANO (methodology for evaluating and preventing the risk of fires and conflicts between electricity and railway lines), ANEMOS PLUS (operation of the electrical system with a high penetration of wind energy) and MERGE (impact of the electric vehicle on the European electricity network).

In 2011 the Group has continued to work in Spain and in Europe on the projects TWENTIES (integration of renewable energies), OPTIMATE (new market mechanism simulation platform), PEGASE (definition of operating platforms and applications at the European level), VERDE (research and development of the technologies to introduce mass numbers of electric vehicles in Spain and PRICE (intelligent management of demand).

## Corporate responsibility

In the area of corporate responsibility, RED ELÉCTRICA GROUP has become one of the most advanced companies and occupies a leadership position in the rankings that evaluate both the results obtained by company management and the level of involvement and support for sustainable development in all areas of activity.

RED ELÉCTRICA GROUP's objective is to consolidate as a sustainable, ethical and responsible GROUP, integrated into society, attentive to all its stakeholders and a point of reference in the markets in which it operates.

This orientation towards sustainable development is reflected at the strategic level and seeking excellence and responsibility when carrying out activities is a basic strategy at the GROUP and is transversally rolled out at the operating level through the management of the business.

The continuous advances in improving excellence in management, shown by the recognition and awards obtained (obtaining the European Seal of Excellence 500+ in 2003 and the Price Phillip Award for Business Excellence - Industrial Quality in 2005) has led REE to become a candidate for the 2011 EFQM European Business Excellence Awards, competing with respect to management and results in Spain and at the international level.

After this evaluation, REE has continued to improve its results in excellence management, obtaining a score of 650 points. In addition, the Group was a finalist and obtained an award for excellence "Assume responsibility for a sustainable future" for its work carried out in the corporate responsibility area. In addition to the EFQM award, REE has been recognised as engaging in "good practices" in the award category and in another two areas: "Achieving balanced results" and "Adding value for customers".

A quality process management system has been implemented and it includes all activities managed by the Company and involves a custom methodology that has been considered to be the best practice among Spanish companies.

Since 2006 REC forms part of the Dow Jones Sustainability World Index and since 2008 the FTSEE4Good.

In addition, in 2011 REC joined the ECPI Ethical Index EMU. It also joined the Aspi Eurozone and STOXX ESG Leaders indexes.

## The human team

The professionals at RED ELÉCTRICA GROUP constitute one of its strategic assets. In accordance with the Company's values, employee management is done in a socially responsible manner through the application of management policies that guarantee fair and equitable treatment and promote integration into the business project and their development.

In 2011 actions were focused on the implementation of the New Employee Management Model, a multi-year project that involves the human resource practice (professional classification, management by category of competency, selection, training, development and compensation models), and its main purpose is to expand the professional development horizon for company employees and to increase organisational efficiency. In 2011 performance evaluation, compensation reviews and professional development systems were launched and the existing employment policy was reviewed.

These activities undoubtedly contribute to create among employees a commitment with the company and its business project, one of the basic pillars of its management.

The Company's final headcount totalled 1,801 employees, which is a 38 employee increase over 2010.

## Events taking place after 31 December 2011

In order to extend the average maturity date of its debt and reduce its exposure to variable rates in accordance with its risk management policy, RED ELÉCTRICA GROUP issued bonds on the euromarket on 13 February 2012 through Red Eléctrica Financiaciones, S.A.U., within the framework of the Guaranteed Euro Medium Term Note program (EMTN program).

This issue, totalling €250 million and maturing in 8 years, bearing a annual yield of 4.875% and at an issue price of 102.131%.

## Foreseeable development

After consolidating the TSO model in 2010 subsequent to the acquisition of the transmission assets owned by distribution companies, RED ELÉCTRICA GROUP will continue to pursue the objective of making the investments in the grid that are necessary in accordance with the Infrastructure Plan, which will allow it to guarantee the reliability and security of the Spanish electricity system.

In turn, RED ELÉCTRICA GROUP will continue to adequately integrate the assets acquired, which is based on the development of the Facilities Renewal Plan, the adaptation of protection systems and the development of remote control systems for facilities.

At the same time, the RED ELÉCTRICA GROUP will face the challenge of efficiently integrating renewable energies within the management of the system operator, without putting supply security at risk.

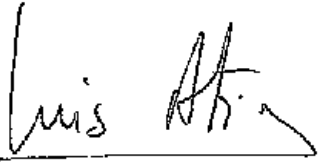
RED ELÉCTRICA GROUP will combine this expansion and network improvement plan with the objective of attaining operating efficiency to obtain financial strengthening in order to generate permanent value.

The performance of the tasks required by regulations and the investments to be made in the coming years, together with a transparent, sufficient and stable compensation environment will secure the growth of RED ELÉCTRICA GROUP.

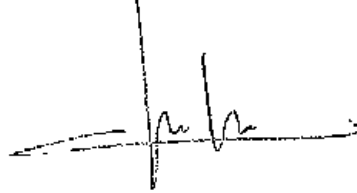
This will result in the creation of long-term value, lasting competitive advantages and the attainment of a better corporate reputation, focused on optimal service to society and the commitment to a sustainable energy system.



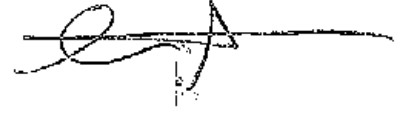
**FIRMA DE LOS MIEMBROS DEL CONSEJO DE ADMINISTRACION EN CUMPLIMIENTO DEL ARTICULO 253 DE LA LEY DE SOCIEDADES DE CAPITAL.**



Luis Atienza Serna  
Presidente



Antonio Garamendi Lecanda  
Consejero



Manuel Alves Torres  
Consejero



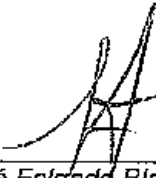
Rafael Suñol Trepal  
Consejero



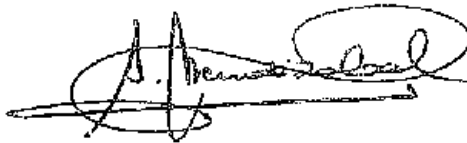
Mª Angeles Amador Millán  
Consejera



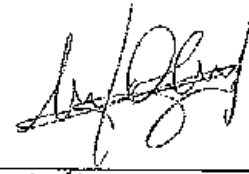
Francisco Javier Salas Collantes  
Consejero



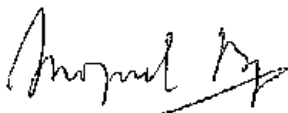
José Folgado Blanco  
Consejero



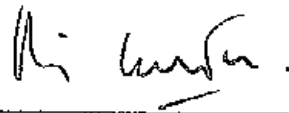
Arantza Mendizábal Gorostiaga  
Consejera



Mª Jesús Álvarez González  
Consejera



Miguel Boyer Salvador  
Consejero



Rui Manuel Janes Gartaxo  
Consejero

**Corporate  
Governance  
Report  
2011**

On the road  
to sustainable  
energy

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The Annual Corporate Governance Report (also known as "ACGR") for fiscal year 2011<sup>(1)</sup> of RED ELÉCTRICA CORPORACIÓN, S.A. (hereinafter also referred to as RED ELÉCTRICA or the Company) has been structured into a main body comprising three Titles, divided into Chapters.

The Titles refer to the legal framework applicable to RED ELÉCTRICA (Title I), to the main corporate governance aspects and principles at RED ELÉCTRICA (Title II) and to the year 2011 at RED ELÉCTRICA (Title III).

In addition, two Official Annexes are included: Annex 1 relating to the ACGR format established by Circular 4/2007, of December 27, 2007, of the Spanish National Securities Market Commission (the "CNMV"), and Annex 2 on additional information under Article 61. bis of Securities Market Law 24/1988, of July 28, 1988 (the "LMV"), which was prepared following the instructions notified by the CNMV to listed corporations in December 2011.

<sup>(1)</sup> Unless another date is expressly indicated in this report, its contents are deemed to refer to December 31, 2011.

# 1

## **TITLE I: Legal Framework Applicable to Red Eléctrica**

## Chapter I. External Framework

The Board of Directors of RED ELÉCTRICA CORPORACIÓN, S.A. has been complying each year in its capacity as a corporation, in accordance with the requirements of the applicable legislation – Article 116 of the Securities Market Law (the "LMV") introduced by Law 26/2003, known as the Transparency Law – and of its Board Regulations – Article 38 thereof – with the obligation to prepare and approve an ACGR, which is notified to the CNMV as a material event and published on the Company's website, and which is attached as an Annex to the Company's annual management report.

The recent change in the regulating framework in this area, approved in 2011, has ratified both the obligation of companies to annually approve an ACGR – Article 61 bis of the Securities Market Law, introduced by Final Provision Five of Sustainable Economy Law 2/2011, of March 4, 2011 (the "LES") – and the obligation of incorporating the ACGR into the management report, in a separate section – Article 538 of Corporate Enterprises Law (the "LSC"), approved by Legislative Royal Decree 1/2010, of July 2, 2010, as amended by Law 25/2011, of August 1, 2011.

The new legal rules have regulated with precision the minimum content of the future ACGR, incorporating new features compared with the previous ACGR format the structure and minimum content of which are regulated by Ministerial Order ECO 3722/2003, of December 26, 2003, and by Circulars 1/2004 and 4/2007, of December 27, 2007, of the CNMV.

The two official Annexes to this ACGR are based on the above legislation.

On the date of approval of this ACGR, the regulations implementing the new Article 61 bis LMV had yet to be published, a circumstance which is expected to take place in 2012.

The legal framework that affects the different aspects of the corporate governance of Spanish corporations has been subject to numerous changes in the past two years, which has led to the immediate modification of the main internal rules of the Company in order to adapt them to the new legislation.

The most important legal rules in the area of corporate governance approved during 2010 and 2011 have been the following:

- ◆ Law 12/2010, of June 30, 2010, reforming, among others, the Audit Law, the Securities Market Law, and the Revised Corporations Law (now repealed by the Corporate Enterprises Law). This Law, which entered into force on July 2, 2010, transposes Directive 2006/43/EC of the European Parliament and of the Council of May 17, 2006 on statutory audits of annual accounts and consolidated accounts into Spanish law, and essentially affects the composition, structure and functions of the Audit Committee.
- ◆ Legislative Royal Decree 1/2010, of July 2, 2010, approving the Revised Corporate Enterprises Law and repealing, among others, the former Corporations Law and Title X (Articles 111 to 117) of the Securities Market Law, relating to listed companies (save for Articles 114.2 and 114.3, and Articles 116 and 116 bis, which have also been subsequently repealed by Sustainable Economy Law 2/2011, of March 4, 2011).
- ◆ Sustainable Economy Law 2/2011, of March 4, 2011, which in its Subprovision 3 of Final Provision Five adds a new chapter VI in title IV of the Securities Market Law which includes Articles 61 bis and 61 ter, which expanded the minimum content of the Annual Corporate Governance Report and established the obligation of the Board of Directors to prepare an Annual Report on Directors' Compensation.
- ◆ Law 25/2011, of August 1, 2011, partially reforming the Corporate Enterprises Law and incorporating Directive 2007/36/EC, of the European Parliament and of the Council of July 11, 2007, on the exercise of

certain rights of shareholders in listed companies. Although the title of the Law only refers to a partial reform of the Corporate Enterprises Law, it also amends provisions of the Securities Market Law and of Law 3/2009, of April 3, 2009, on structural modifications to commercial companies. This Law, which entered into force on October 2, 2011, has introduced, among others, the following new features in the area of corporate governance:

- It establishes measures aimed at reducing the organizational and operating costs of corporate enterprises.
- It eliminates differences between a corporation (S.A.) and a limited liability company (S.L.).
- It introduces the possibility of meetings of the Board of Directors being called by at least one-third of its members if, after a request to the chairman, the latter has not called the meeting within one month.
- It clarifies the rules on infringements and penalties for breaching treasury stock obligations and for violating statutory prohibitions in this connection, establishing a very broad scope of punishable conduct.
- It introduces a new Article 11 bis in the Corporate Enterprises Law which regulates the electronic headquarters or corporate website. Of particular note in this Article are the provisions regulating the creation of the corporate website, establishing for this purpose that the website must be resolved on by the Shareholders' Meeting and such resolution must be registered at the Commercial Registry or notified to all of the shareholders.
- It repeals Article 289 of the Corporate Enterprises Law which required disclosure on the website/newspapers of the following bylaw amendments:
  - ♦ Company name.
  - ♦ Corporate purpose.
  - ♦ Registered office.
- It overhauls the rules on call notices and the right to information in relation to Shareholders' Meetings of corporations.
- It incorporates some new features in the rules on listed corporations, mainly in the following areas:
  - ♦ In the information that the company's website must contain.
  - ♦ In some aspects relating to the outcome of votes.
  - ♦ In the shareholders' right to information.
  - ♦ In matters relating to the representation by proxy of shareholders at Shareholders' Meetings.
  - ♦ In the dealings between the financial intermediary and its clients for the purposes of casting votes.

## Chapter II. Internal Framework

The internal rules by which Red Eléctrica Corporación, S.A. is governed are subject to continuous modification in order to incorporate corporate governance best practices into the Company and to achieve greater transparency in the information provided to investors.

By way of a summary of the main changes in the area of corporate governance that have taken place in the Company's internal rules in the past 5 years, in 2007, on a voluntary basis and before it was legally required, the Corporate Bylaws, Shareholders' Meeting Regulations and Board Regulations were adapted to the recommendations contained in the Unified Code of Recommendations for the Good Governance of Listed Companies (the "Conthe Code"), approved on May 19, 2006 by the Special Working Group advising the CNMV on the harmonization and update of the Olivencia and Aldama Report recommendations for the good governance of listed companies.

Further amendments were made to the Corporate Bylaws and Shareholders' Meeting Regulations in 2008 in order to adapt them to Law 17/21007, of July 4, 2007.

Continuing with such policy, in 2009 the Internal Code of Conduct on the Securities Market was modified, and in 2010, the Board of Directors, in a meeting held on January 28, approved a new version of the Board Regulations to adapt them to the corporate restructuring carried out in 2008 by the Red Eléctrica Group and to the aforementioned new version of the Internal Code of Conduct on the Securities Market. In May 2010, the Shareholders' Meeting approved an amendment of the Bylaws in relation to the shareholders' preemptive subscription right, to adapt them to Law 3/2009, of April 3, 2009.

In 2011, the Shareholders' Meeting of April 13, 2011, approved an amendment of the Corporate Bylaws and the Shareholders' Meeting Regulations in order to adapt them to the new legal requirements established in Law 12/2010, of June 30, 2010 (basically affecting the composition, structure and functions of the Audit Committee) and Legislative Royal Decree 1/2010, of July 2, 2010, approving the Revised Corporate Enterprises Law (fully repealing the Corporations Law and partially repealing the Securities Market Law).

At present, in corporate governance matters the Company is also governed by the internal rules and procedures listed below which, as an internal legal regime, go beyond the applicable statutory requirements.

These rules, as of December 31, 2011, consisted of:

- ◆ The Corporate Bylaws.
- ◆ The Shareholders' Meeting Regulations.
- ◆ The Board Regulations.
- ◆ The Company Chairman Succession Plan.
- ◆ The Internal Code of Conduct on the Securities Market.
- ◆ The Procedure for proxies, voting and information by remote means at the Shareholders' Meeting (relating to the 2011 Annual Shareholders' Meeting).
- ◆ The Code of Ethics.
- ◆ The Operating Rules of the Shareholders' Electronic Forum.

## The Corporate Bylaws

The Corporate Bylaws are constantly adapted, not only to the law, but also to best corporate governance practices and principles and have been successively amended for such purpose by the Annual Shareholders' Meeting in recent years. The Annual Shareholders' Meeting held on May 22, 2008 approved an amendment to the Corporate Bylaws, within the framework of the corporate reorganization process, in order to adapt them to the requirements of Law 17/2007 of July 4, 2007 amending Electricity Industry Law 54/1997 of November 27, 1997 to adapt it to the provisions of Directive 2003/54/EC of the European Parliament and of the Council of June 26, 2003 concerning common rules for the internal market in electricity.

In 2010, the Annual Shareholders' Meeting amended Article 9 of the Corporate Bylaws in order to adapt it to Law 3/2009, of April 3, 2009, recognizing the shareholders' preemptive subscription right solely in the case of capital increases with the issue of new shares with a charge to monetary contributions and issues of debentures which are convertible into new shares.

The Annual Shareholders' Meeting held on April 13, 2011 approved another amendment of the Bylaws to adapt them to the new legal requirements established in Law 12/2010, of June 30, 2010, and in Legislative Royal Decree 1/2010, of July 2, approving the Revised Corporate Enterprises Law.

The legislative modifications approved in the area of corporate governance in 2011, in particular, Law 25/2011, of August 1, 2011, have led the Company to initiate a new review of the Bylaws to adapt them to the new legal requirements, a review which will conclude with the approval of a proposal by the Board of Directors, for submission to the next Shareholders' Meeting.

The main new features of the aforementioned Law 25/2011 have been described in Chapter I of this report.

The detailed content of the proposed reform of the Bylaws that is prepared by the Board of Directors, at the proposal of the Corporate Responsibility and Governance Committee, will be made public together with the call notice for the Annual Shareholders' Meeting.

All of the amendments to the Bylaws have been notified to the CNMV and registered at the Commercial Registry.

## The Shareholders' Meeting Regulations

The Regulations were approved by the Shareholders' Meeting of July 17, 2003, and amended by the Annual Shareholders' Meeting of May 22, 2008, in order to adapt them to the aforementioned Law 17/2007 of July 4, 2007.

The Shareholders' Meeting Regulations are the legal charter for shareholders of RED ELÉCTRICA, in line with best corporate governance practices, and include all of the new forms of shareholder protection and participation, with a view to recognizing, promoting and strengthening shareholder rights at the Company as far as possible.

The Annual Shareholders' Meeting held on April 13, 2011 approved the modification of the Shareholders' Meeting Regulations, the same as with the Bylaws, to adapt them to the new legal requirements established by Law 12/2010, of June 30, 2010, and by Royal Legislative Decree 1/2010, of July 2, 2010, approving the Revised Corporate Enterprises Law.



Simultaneously with the review of the Bylaws, a process has been initiated to review the Shareholders' Meeting Regulations, to adapt them to the reforms introduced by Law 25/2011, of August 1, 2011, partially reforming the Corporate Enterprises Law, which will conclude with a proposal from the Corporate Responsibility and Governance Committee to the Board of Directors, for submission to the next Shareholders' Meeting.

The detailed content of the proposed reform of the Shareholders' Meeting Regulations that is prepared by the Board of Directors, at the proposal of the Corporate Responsibility and Governance Committee, will be made public together with the call notice for the Annual Shareholders' Meeting.

All of the amendments to the Shareholders' Meeting Regulations approved have been notified to the CNMV and registered at the Commercial Registry.

### The Board Regulations

The Board Regulations were approved at the Board meeting held on January 28, 2010, amending the previous text dated December 20, 2007.

As indicated in Article 22 of the Corporate Bylaws, the principal purpose of the Regulations is to establish the basic rules on the organization and functioning of the Board of Directors and its Committees, the rules of conduct for its members and the system of supervision and control of the Board of Directors and its Committees, with a view to ensuring the highest standards of professionalism and efficacy in its actions. All of this is carried out by encouraging the active participation of its members, placing the interests of the Company and of its shareholders above their own interests, while upholding the law, the Corporate Bylaws and corporate governance principles.

In 2011, the Board Regulations were subject to an in-depth view by the Corporate Responsibility and Governance Committee, to adapt them to the legislative modifications approved in 2010 and 2011 and mentioned in Chapter I of this Title, once the Shareholders' Meeting of April 13, 2011 approved the modification of the Corporate Bylaws and the Shareholders' Meeting Regulations to adapt them to Law 12/2010, of June 30, 2010 and to Legislative Royal Decree 1/2010, of July 2, 2010. The Corporate Responsibility and Governance Committee has drawn up a proposed modification of the Board Regulations to be submitted for approval by the Board, following the necessary technical adjustments, once the regulations implementing the new rules governing the ACGR and governing the new Annual Report on Directors' Compensation are published.

The Regulations of the Board of Directors have been notified to the CNMV and registered at the Commercial Registry.

### The Company Chairman Succession Plan

The Board meeting held on October 27, 2011 approved the Company Chairman Succession Plan, following an increasingly common corporate governance practice worldwide, whereby listed companies prepare and approve plans governing the succession of their most senior executive or CEO. These plans are aimed at reducing the impact that the handover will have on the organization, by determining a model profile for candidates and ensuring continuity in the corporate business. They also seek to reduce as far as possible the risks and adverse effects that may arise from the appointment of a new chairman, until he or she is

fully integrated into the post. The Company Chairman Succession Plan was approved on the basis of the special conditions present in Red Eléctrica's chief executive, which position is held by the chairman of the Board of Directors, as established by Article 25 of the Corporate Bylaws. The Plan establishes a succession procedure split into several phases, attributing responsibilities to the managing bodies participating in it; all with a view to creating an environment in which the appointment of a new chairman may be carried out in an orderly and efficient manner that does not affect the Company's ordinary operations.

### **The Internal Code of Conduct on the Securities Market**

It was approved by the Board of Directors on June 25, 2009, and replaced the former text approved on July 20, 2006. In a meeting held on June 30, 2011, the Board of Directors approved an update to the Code to adapt it to the Group's new corporate structure, and to include the new name of the Appointments, Compensation and Corporate Governance Committee which is now known as the Corporate Responsibility and Governance Committee.

The update to the Internal Code of Conduct on the Securities Market has been registered at the CNMV.

### **The procedure for proxies, voting and information by remote means at the Shareholders' Meeting**

At a meeting held on February 24, 2011, the Board of Directors approved the rules on voting and proxies by remote means and the exercise of the right to information by electronic means for the Annual Shareholders' Meeting for fiscal year 2010. The use of electronic voting at the Shareholders' Meeting held on April 13, 2011 has, once again, clearly grown, as 664 shareholders holding 208,839 shares exercised their right to vote or delegate their vote electronically. This means that 14% of the 4,788 shareholders present at the Shareholders' Meeting, in person or by proxy, took part in the meeting by telematic means, matching the percentage obtained at the Shareholders' Meeting held on May 20, 2010, compared to 379 shareholders holding 133,711 shares who used it in 2009, and 315 shareholders holding 64,670 shares who used it in 2008.

### **The Code of Ethics**

The Code of Ethics was approved at the Board meeting of July 26, 2007, after an extensive process of public disclosure during which more than one hundred comments were received from all employees of the Group.

The Code reflects the corporate identity and commitments made to the business community and to the various stakeholders affected by the activities of the RED ELÉCTRICA Group. The Code contains the fundamental principles that must guide all members of the Board of Directors, the management bodies and employees of the RED ELÉCTRICA Group and it can also be invoked by stakeholders. Particularly notable is the internal procedure for the management of inquiries and complaints contained in the Code to ensure it is fully complied with. This procedure is already in operation.

The Code was voluntarily prepared by the Company, and has been communicated to all Red Eléctrica Group personnel.



An Ethics Manager has been appointed, tasked with the administration of the system for the detection and handling of breaches and complaints, and the monitoring and development of the Code of Ethics.

Throughout 2009, the Audit Committee closely monitored the implementation of the Company's Code of Ethics, continuing the work begun in this area in 2008.

In addition, the information sessions and presentations begun in 2008 regarding the Code of Ethics were completed in 2009 with the active participation of the Ethics Manager, both at the corporate headquarters and in all regional offices, in order to ensure the appropriate dissemination of the principles and recommendations of the Code, including those relating to the procedure for reporting financial and accounting irregularities, paying particular attention to any questions raised or clarification required.

In June 2009, the Ethics Manager presented the Annual Report on the Management of the Code of Ethics to the Board. This was the first report on the functioning of the Code of Ethics management system and has been assumed by the Company as an obligation, so it will be prepared annually.

The Annual Report on the Management of the Code of Ethics for fiscal year 2010 was approved on July 21, 2011. The Report describes the actions taken by the Company to raise awareness of the scope of the Code of Ethics and of the procedure for managing queries and complaints. Reference is also made to the queries made, the large majority of which related to how the commitments reflected in the Code should be interpreted in specific situations. Mention is also made of the complaints received and handled by the Ethics Manager, as well as their resolution.

To boost ethical and responsible management, a plan has been drawn up known as the Plan to promote ethical management 2010-2012. This Plan highlights the Red Eléctrica Group's goal of pursuing its activity responsibly, by building a solid organizational culture, based on trust and on corporate values.

The Plan develops structures and systems, and implements awareness, training and dissemination projects, all of which will contribute to the consolidation of the Company's culture of ethical management. In 2011, a process was initiated to review and improve the Code of Ethics, which is set to conclude in fiscal year 2012.

### **Operating Rules of the Shareholders' Electronic Forum**

These were approved by the Board of Directors in its meeting of February 24, 2011.

The Shareholders' Electronic Forum set up by Red Eléctrica Corporación, S.A. on its website – [www.ree.es](http://www.ree.es) – on the occasion of the holding of its Shareholders' Meetings, responds to the need established in the last paragraph of Article 117.2 of Securities Market Law 24/1988, of July 28, 1988, introduced by Law 12/2010, of June 30, 2010, and in Article 528.2 of the Revised Corporate Enterprises Law (the "LSC"), approved by Legislative Royal Decree 1/2010, of July 2, 2010.

The Shareholders' Electronic Forum is aimed at facilitating communication among the Company's shareholders (individuals or legal entities, and any voluntary associations that may be created) on the occasion of the holding of the Company's Shareholders' Meetings. Shareholders have the possibility of sending, for publication on the Forum, communications in accordance with the Law, accompanied by their contact details, thereby enabling shareholders to communicate with each other.

# 2

**TITLE II:**  
**Main Corporate  
Governance Aspects and  
Principles at Red Eléctrica**

## Chapter I. Fundamental Corporate Governance Principles at Red Eléctrica

RED ELÉCTRICA's fundamental corporate governance principles are based on the external and internal legal framework described above and on corporate governance best practices established in Spain (the Unified Good Governance Code) and abroad (policies, practices and recommendations set by foreign institutional investors, proxy advisors and international organizations such as the OECD).

There follows a summary of the best practices adopted by the Company, by group, each of which is described at a later stage in greater detail.

### The Board of Directors

- ◆ A low number of directors.
- ◆ A participative and proactive board.
- ◆ A percentage of Independent Directors (64%) in excess of the international requirements.
- ◆ A single Executive Director.
- ◆ The essential responsibilities for management of the Company, detailed in Article 5 of the Board Regulations, are expressly reserved for the Board of Directors in plenary session and cannot be delegated.
- ◆ The responsibilities that cannot be delegated cannot be carried out by the Executive Director or the Board Committees.
- ◆ The Board of Directors carries out an annual evaluation of its own operation, of the operation of the Board Committees and of the Board Chairman, and periodically with specialist external advice, as in the current process (KPMG advisory services).
- ◆ In 2011 the Board of Directors approved a Succession Plan for the office of Company Chairman, to ensure, when the time comes, an orderly and well-planned handover that will not adversely affect the corporate interest or the corporate business.
- ◆ The Board of Directors has taken on board the best recommendations on gender diversification. Three Board members (27.27%) are female, placing the Company at the vanguard of the IBEX 35. The Board of Directors prepares and approves an annual report on gender diversification, which this year is available on the Company's website.
- ◆ The Board Chairman is also the Senior Executive (Executive Director) of the Company, by express decision of the Board of Directors and of the Shareholders' Meeting, and pursuant to the Corporate Bylaws.
- ◆ The powers and responsibilities of the Executive Director are limited by:
  - The legal reservation of responsibilities of the Board of Directors that cannot be delegated.
  - The functions and responsibilities attributed to the Board Committees in the Corporate Bylaws and the Regulations of the Board of Directors.
  - The effective control exercised by the Board of Directors, at each monthly meeting, over the ordinary activities of the Executive Director.

The immediate effective control exercised by the Board of Directors, at each monthly meeting, over any extraordinary or urgent measures taken by the Executive Director.

- ◆ A high percentage of attendance and dedication to the exercise of their responsibilities by the Directors.
- ◆ Use of new technologies to facilitate the operation of the Board and provide Directors with information and documentation: the Directors' Portal.

### The Board Committees

- ◆ Committees formed by the Board of Directors, with an eminently technical profile, to support it in the performance of its responsibilities, designed to achieve greater efficiency and transparency.
- ◆ Comprising qualified professionals occupying important posts in other institutions and/or companies.
- ◆ Comprising a majority of Independent Directors (in the case of the Corporate Responsibility and Governance Committee, which has four members, two are Independent Directors, one of whom is the Committee Chairman and has the casting vote in the event of a tie, meaning that it is controlled by the Independent Directors).
- ◆ Chaired by Independent Directors, as envisaged in the Corporate Bylaws and the Board Regulations; the term of office of Committee chairmen is limited to three years, after which term they may not be re-elected until at least one year has elapsed from the date of their termination in office.
- ◆ No Directors belong to both Committees, favoring their total independence.
- ◆ The Committees hold regular monthly meetings and are genuine specialist technical bodies that provide great added value to the Board.
- ◆ The term of office of all Committee members is three years; members may be re-elected.
- ◆ The functions and responsibilities of the Committees are established in the Corporate Bylaws and in the Board Regulations, which provide them with a stable legal framework.

### The Compensation Policy for the Board of Directors and the Executive Director

- ◆ There is total transparency and openness in the breakdown of each Director's individual compensation.
- ◆ The maximum limit of overall annual compensation for the Board of Directors is established in Article 20 of the Corporate Bylaws (1.5 % of the Company's net annual profit approved by the Shareholders' Meeting).
- ◆ Board compensation and the Board Compensation Report are submitted for approval by the Shareholders' Meeting as two separate and independent items on the Agenda.
- ◆ The vote of the Annual Shareholders' Meeting on Board compensation and the Board Compensation Report is binding.
- ◆ Total Board compensation is divided between:
  - Fixed compensation: Fees for attending Board and Board Committee meetings.
  - Variable compensation: A sum linked to meeting of Company targets and strategies established in advance by the Board of Directors.

The targets and criteria determining the variable compensation of the Board of Directors are set in

advance by the Corporate Responsibility and Governance Committee and are also assessed and evaluated at the end of each year by that Committee.

- ◆ Total Board compensation remains unchanged since 2007.
- ◆ There are no stock option plans for Company Directors.
- ◆ The Board compensation policy is also based on other principles:
  - Moderation.
  - Link to actual dedication.
  - Link to Company performance, with continuous reduction in its weight in relation to Company results.
  - Aligned with the long-term interests of both the Company and the Shareholders.
  - Acting as an incentive, but without conditioning Directors' independence (particularly in the case of Independent Directors).
  - Transparency.
  - Aligned with general practice at listed companies.
- ◆ The compensation of the Executive Director has a fixed and a variable component.
- ◆ The compensation of the Executive Director is aligned with market practice.
- ◆ The annual variable compensation of the Executive Director cannot exceed 50% of his annual fixed compensation.
- ◆ The annual variable compensation of the Executive Director also depends on strategies, targets and criteria established in the Strategic Plan, set by the Corporate Responsibility and Governance Committee, at the end of the year.
- ◆ The Executive Director has long-term variable compensation linked to fulfillment of strategies and targets established by the Corporate Responsibility and Governance Committee.

### Relations with Shareholders and Institutional Investors

The Company's relations with its shareholders and institutional investors are general in nature and no specific or special relationships are held with any of them.

The Company regularly organizes road shows, conducted by senior management, at principal financial centers in Spain and abroad where there is a high concentration of institutional investors, to inform them of its activities and its business performance, in an attempt to forge closer ties with these investors.

In light of the high percentage of foreign institutional shareholders (close to 70% in 2011), and as in previous years, the Company has conducted visits to investors and proxy advisors to explain its corporate governance practices and policies to them directly, aiming to establish appropriate mechanisms for the regular exchange of information with Spanish and foreign institutional investors and with the main proxy advisors, with a view to continuing to adapt to the most advanced international corporate governance standards.

Under no circumstances does the Company disclose to institutional shareholders any information that might place them in a privileged or advantageous situation vis-à-vis the other shareholders; rather, all information exchanged is public information.

All the above is in accordance with the provisions of the Board Regulations.

## Chapter II. Shareholder Structure

The Company's capital is comprised of 135,270,000 fully subscribed and paid-in shares of a single class and series, each with a par value of €2, represented by book entries and listed on the four Spanish stock exchanges.

At December 31, 2011, the State-owned Industrial Holdings Company (Sociedad Estatal de Participaciones Industriales or "SEPI") directly owned a significant stake in the Company, holding 27,054,000 shares, which represent 20% of capital.

There are no individuals or legal entities that exercise or may exercise control over the Company, as provided in Article 4 of the Securities Market Law.

Thus, the shareholding structure of the Company consists of a 20% stake held by SEPI, with the remaining 80% being free float. As explained below, no other shareholder may hold a stake greater than 5%.

Within the free float, of note is the high percentage of foreign shareholders, in particular, of institutional investors, who at December 31, 2011, represented 70% of the capital stock, which explains the importance that the Board of Directors attaches to international corporate governance practices and recommendations.

The entry into force of Law 17/2007 of July 4, 2007 introduced various changes affecting the Company's shareholders.

The purpose of these changes is, inter alia, to guarantee the Company's independence as regards the other activities and participants in the electricity sector, since the activities pursued by RED ELÉCTRICA (transmission of electricity and operation of the electricity system) are considered by the State legislature to be an essential service. Specifically, the second paragraph of Additional Provision Three of Law 17/2007, of July 4, 2007, establishes new maximum limits on shareholdings in the Company, which are summarized below:

- ◆ Any individual or legal person may hold shares in the Company, provided that the sum of its direct and indirect holdings in the Company does not exceed five percent (5%) of capital and that it does not exercise more than three percent (3%) of voting rights. These shares may not be pooled for any purpose whatsoever.
- ◆ Parties engaging in activities in the electricity sector and any individuals or legal entities that directly or indirectly hold more than five percent (5%) of capital may not exercise more than one percent (1%) of voting rights at the Company.
- ◆ The special regime for SEPI is maintained, whereby it must hold at least ten percent (10%) of capital in all cases.

The legal provisions regarding the general and special shareholding regime are set out in Articles 5 and 14, the Sole Additional Provision of the Corporate Bylaws, and in Article 6.3 of the Shareholders' Meeting Regulations, which were amended at the Annual Shareholders' Meeting of May 22, 2008 in order to adapt them to the provisions of Law 17/2007 of July 4, 2007, described above.

The legal regime established by Directive 2009/72/EC, of July 13, 2009, which proclaims the mandatory independence of transmission companies and operators of European electricity systems, has endorsed the legal limits on holdings and voting rights applicable to the Company's shareholders, established in Law 17/2007.



## Chapter III. The Shareholders' Meeting

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

Its resolutions, adopted pursuant to the Shareholders' Meeting Regulations and the Corporate Bylaws, are binding on all shareholders, notwithstanding their legal right to withdraw from the company. The Shareholders' Meeting shall have the power to adopt all resolutions specific to its status as the Company's sovereign body. In particular, and without limitation, it is responsible for:

- ◆ Approving the individual and consolidated financial statements of RED ELÉCTRICA, the management by the Board of Directors, and the proposed distribution of income.
- ◆ Appointing and removing Directors, ratifying or revoking their appointment by co-optation, and appointing and reappointing the auditors.
- ◆ Approving programs or authorizing transactions involving treasury stock.
- ◆ Approving the establishment of Director compensation systems linked to the share value.
- ◆ Resolving to issue debentures, increase or reduce capital, change the legal form, merge, spin off or dissolve the Company, and make any amendment to the Corporate Bylaws.
- ◆ Authorizing the Board of Directors to increase capital pursuant to the provisions of the Corporations Law.
- ◆ Approving transactions the effect of which is equivalent to the modification of the Company's corporate purpose.

The rules on the organization and functioning of the Shareholders' Meeting are contained in the Corporate Bylaws (Articles 11 through 18) and in the Shareholders' Meeting Regulations.

The Annual Shareholders' Meeting of April 13, 2011, approved, among other resolutions, an amendment of the Bylaws and of the Shareholders' Meeting Regulations, which, among other objectives, sought to adapt the powers of the Shareholders' Meeting to the new legal regime established in the Corporate Enterprises Law; the new powers of the Shareholders' Meeting are not substantially different from the previous powers, being more a technical adaptation to the current legislation.

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

- ◆ The quorum requirement and the result of the votes on each of the resolutions approved by the Shareholders' Meetings in the previous year.
- ◆ Information relating to the right of attendance and procedures for granting proxies for Shareholders' Meetings, in accordance with the provisions of the Corporate Bylaws and Shareholders' Meeting Regulations.
- ◆ Information on electronic voting and proxies.
- ◆ Information on securities issues.
- ◆ Information on the rating granted by the credit rating agencies.
- ◆ Increased information on shareholdings, with greater detail on significant holdings, treasury stock and side agreements between shareholders.

Law 25/2011 has introduced certain modifications into the content of companies' websites; most of these are already reflected on RED ELÉCTRICA's current website.

In addition, to facilitate the exercise of the right of shareholders to information, the following steps are taken:

- ◆ Call notices are always posted more than one month in advance, which is the established statutory period.
- ◆ All documentation submitted for approval by the Shareholders' Meeting and especially the financial statements and the Annual Corporate Governance Report are made available to all shareholders at the corporate headquarters, on the website and at the Shareholder Information Office.
- ◆ An entire section of the agenda of the Shareholders' Meeting is devoted to reporting on the principal characteristics of the Annual Corporate Governance Report.
- ◆ The annual reports on the activities of the Audit Committee and of the Corporate Responsibility and Governance Committee, which can be found at the end of the Annual Corporate Governance Report, are made available to all shareholders.
- ◆ A Shareholder Bulletin is published quarterly, containing the main news about the Company.
- ◆ The Chairman of the Audit Committee is available to all shareholders during Shareholders' Meetings to deal with any matters falling within his jurisdiction as may arise.
- ◆ The items included on the agenda for the Shareholders' Meeting are as detailed as possible.
- ◆ Separate voting on each item is permitted, including via remote voting, with a view to giving shareholders full decision-making freedom and independence in respect of each item submitted to vote.
- ◆ The Shareholder Information Office specifically deals with requests made by Company shareholders. Shareholders may submit questions in writing regarding the information available to the public or notified to the competent authorities and make inquiries through the Shareholder Information Office.

Shareholder rights are regulated in Article 15 of the Corporate Bylaws, which expressly refers to the right to information and attendance of Shareholders' Meetings, and in Articles 6 through 10 of the Shareholders' Meeting Regulations. Specifically, the rights are as follows:

### Right to Information

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

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

An open, free-flowing and accessible dialog is maintained with shareholders. Communications are made with the utmost transparency, providing all available information to shareholders at the same time as it is received by other participants in the securities and financial markets.

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

The Company undertakes to make documentation and information relating to the meeting agenda

available to shareholders, free of charge, both at the Shareholder Information Office and on the Company website, including the following documentation:

- ◆ The call notice of the Shareholders' Meeting, containing the proposed resolutions and the corresponding reports by the Board of Directors.
- ◆ The Company's individual and consolidated financial statements and the proposed distribution of income for the year.
- ◆ The Company's individual and consolidated management reports for the year.
- ◆ The audit reports relating to the Company's individual and consolidated financial statements.
- ◆ The Annual Corporate Governance Report.
- ◆ The Corporate Social Responsibility Report.
- ◆ The report on the compensation policy for the Board of Directors, included in the annual public documentation submitted to the Annual Shareholders' Meeting.
- ◆ The environmental report.
- ◆ Any other report the inclusion of which is obligatory or is determined by the Board of Directors.

Law 25/2011 of August 1, 2011, has established, with precision, certain information that must be posted on the website when the Shareholders' Meeting is called, and although the strict wording of the Law is specific, its scope, as far as content is concerned, is covered by the current Shareholders' Meeting Regulations. However, the adaptation to this Law of the relevant Articles of the Shareholders' Meeting is planned to be proposed to the next Annual Shareholders' Meeting.

Law 25/2011 gives an even greater role to company websites, as it introduces a new Article 11 bis into the Corporate Enterprises Law, which regulates the electronic headquarters and corporate website. In addition, this incorporates into Article 516 of the Corporate Enterprises Law the obligation of listed companies to use their websites to publish the call notice for the Shareholders' Meeting, something which Red Eléctrica Corporación, S.A. has been doing for several years.

Law 25/2011 also introduces changes into the call notice for the Shareholders' Meeting, in general to promote shareholders' rights to information.

### Right to Attend

Shareholders may attend the Shareholders' Meeting if they are up to date in the payment of capital calls and evidence their share ownership, by way of certification in their name, in the accounting register of book entries five days before the meeting is due to be held. Company Directors and Executives must attend Shareholders' Meetings.

As a general rule and in order for the proceedings of meetings and the resolutions adopted to reach the widest audience, the media are allowed access to Shareholders' Meetings. To this effect, Article 15 of the Corporate Bylaws and Article 10 of the Shareholders' Meeting Regulations provide that shareholders with the right to attend may be represented at the Shareholders' Meeting by another shareholder with the right to attend, in the manner established in the Corporations Law.

Law 25/2011 has eliminated bylaw restrictions on attending Shareholders' Meeting and, accordingly, the bylaw requirement of being represented at the Shareholders' Meeting by another shareholder is no longer considered applicable. Now the shareholder may be represented by any person. The necessary adaptation of the relevant Articles of the Bylaws and of the Shareholders' Meeting Regulations is planned to be proposed to the next Shareholders' Meeting.

There is no bylaw restriction requiring a minimum number of shares to attend the Shareholders' Meeting (application of the one share, one vote principle).

Company Directors and Executives are required to attend Shareholders' Meetings.

As a general rule and in order for the proceedings of meetings and the resolutions adopted to reach the widest audience, the media are allowed access to Shareholders' Meetings and Meetings are broadcast in an audiovisual format, with simultaneous translation into English.

### Right to Participate and New Technologies

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

In line with the most well-known recommendations in this area, the Shareholders' Meeting Regulations are in line with the regime established by Law 26/2003 of July 17, 2003 regarding the development of shareholder rights and the rules regarding the organization and functioning of the Shareholders' Meeting.

Thus it is provided that shareholders owning 5% of capital may request that the Board, prior to issuing the call, include any item on the agenda for the next Shareholders' Meeting. The Board of Directors must include the items requested in the manner that best suits the Company's interests, provided that they refer to matters falling within the scope of the powers of the Shareholders' Meeting.

Shareholders may also make proposals regarding items on the agenda and suggestions regarding any activities and interests of the Company that, in their opinion, should be discussed at the Shareholders' Meeting. In both cases, shareholders may make proposals and suggestions through the Shareholder Information Office.

Law 25/2011 has introduced certain adjustments and provisions aimed at reinforcing shareholders' rights to participate in the Shareholders' Meeting, which will require the necessary adaptations to the Bylaws and Shareholders' Meeting Regulations, which are planned to be submitted for approval to the next Annual Shareholders' Meeting.

In 2005, Red Eléctrica placed its bets on an electronic voting system. It was one of the pioneers of this system, which allows shareholders to exercise their voting rights electronically via the Company website, [www.ree.es](http://www.ree.es). Since then, the Company has enabled shareholders to vote electronically at all its Shareholders' Meetings.

Continuing the approach of making it easier for shareholders to use advanced electronic means to exercise their rights, the Board of Directors meeting held on February 24, 2011, approved the rules on electronic voting and proxies for the Shareholders' Meeting of April 13, 2011. The procedure has been satisfactory, as

664 shareholders holding 208,839 shares exercised or delegated their vote electronically. This meant that 14% of the 4,788 shareholders present in person or by proxy at the Meeting participated in the Meeting by electronic means. This matched the percentage obtained at the Shareholders' Meeting held in 2010 and nearly doubled the number of shareholders who exercised or delegated their vote electronically at the Shareholders' Meeting held in 2009, when 379 shareholders holding 133,711 shares used the electronic vote.

In addition, presentations to analysts and the Shareholders' Meeting are broadcast in real time on the Company website. Webcasts of presentations are available on the Company website. In 2007, 2008, 2009, 2010 and 2011, the Shareholders' Meeting was broadcast via live video webcast, with simultaneous translation into English.

Of note in 2011, as already mentioned above, was the start-up of the Shareholders' Electronic Forum for the Shareholders' Meeting held on April 13, 2011, which was intended to implement the requirements of Article 528.2 of the Corporate Enterprises Law. The purpose of the Forum is to facilitate communication among the shareholders of Red Eléctrica with a view to publishing proposals to supplement the agenda contained in the call notice for the Shareholders' Meeting, issuing requests for adhesion to such proposals, presenting initiatives in order to reach the percentage to exercise the minority right envisaged in the law or making offers or requests for voluntary representation.

This tool was incorporated into the Shareholders' Meeting Regulations, in Article 8.4 thereof, following its approval by the Shareholders' Meeting held on April 13, 2011.

In addition, in 2011 the Company used certain social networks (Facebook and Twitter) to publicize and provided information on the holding of the Annual Shareholders' Meeting.

It is also worth mentioning that a new duty for the Company was included in the proposed amendment of the Corporate Bylaws and the Shareholders' Meeting Regulations approved at the Annual Shareholders' Meeting of April 13, 2011, namely, equal treatment of shareholders, which is a provision that was already contained in the Regulations of the Company's Board of Directors (Article 35).

As noted above, Law 25/2011 has established the duty for corporate enterprises to have a website, which must be approved by the Shareholders' Meeting and registered at the Commercial Registry and, accordingly, the Board of Directors intends to submit the creation of the RED ELÉCTRICA website to the next Annual Shareholders' Meeting for ratification and approval.

## Chapter IV. The Board of Directors

### Organization, powers and composition

As of December 31, 2011, the Board of Directors was composed of 11 directors (1 executive director, 3 nominee directors and 7 independent directors).

The Board of Directors governs and represents the Company with the support of the Audit Committee and the Corporate Responsibility and Governance Committee.

The rules on the organization and functioning of the Board are contained in the Corporate Bylaws (Articles 19 through 26) and in the Board.

The Board approves the annual meeting calendar at the end of the preceding year and recognizes the right of Directors to make amendments to the agenda of each meeting, provided sufficiently in advance (in practice, at least 6 days beforehand), together with the call notice and meeting documentation.

Pursuant to the Corporate Bylaws and the Board Regulations, the principle guiding the Board's actions at all times is the defense of the viability and value of the Company in the long term, and the protection and promotion of the Company's general interests.

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

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

In particular, the Board of Directors has expressly reserved (Article 5 of the Board Regulations) on a non-delegable basis, the following responsibilities:

- a) Approval of the general policies and strategies of the Company and, in particular:
  - i) Approval of the strategic or business plan of the Company and its Group, as well as the annual budget and management objectives.
  - ii) Approval of the investment and financing policy.
  - iii) Approval of the definition of the structure of the corporate Group.
  - iv) Approval of the corporate governance policy.
  - v) Approval of the corporate responsibility policy.
  - vi) Approval of the policy regarding compensation and evaluation of senior executives.
  - vii) Approval of the policy for control and management of the principal risks of the Company and of the Group, and knowledge and periodic monitoring of internal control, prevention and reporting systems.
  - viii) Approval and, if applicable, proposal to the Shareholders' Meeting of the dividend and treasury stock policies, in particular, the limits thereof.
  - ix) The other policies and strategies specifically envisaged in the Board Regulations.

- b)** The following decisions:
  - i)** Directors' compensation and, in the case of Executive Directors, the additional consideration for their executive functions and other contractual conditions that must be observed.
  - ii)** Financial information that the Company must periodically disclose as a listed company.
  - iii)** Investments or transactions deemed to be strategic by virtue of their high amount or special characteristics, unless their approval corresponds to the Shareholders' Meeting.
  - iv)** The creation or acquisition of holdings in special-purpose vehicles or entities domiciled in countries or territories that are considered tax havens, and any other transactions and operations that could impair the transparency of the Group.
- c)** Related-party transactions, as defined by the legislation in force from time to time, that are material or outside the ordinary course of business of the Company and must be reported obligatorily to the securities markets, pursuant to the aforementioned legislation, following a report by the Audit Committee.
- d)** The annual evaluation of:
  - i)** The quality and efficiency of the functioning of the Board and the performance by the Chairman of his functions, based on a report referred thereto by the Corporate Responsibility and Governance Committee.
  - ii)** The functioning of its Committees, based on the reports referred thereto by them.

Pursuant to the Corporate Bylaws, Directors hold office for a term of 4 years.

In line with the recommendations of the Unified Code of Recommendations for the Good Governance of Listed Companies (the "Conthe Code"), the maximum term of office for Independent Directors has been established in the Board Regulations at twelve (12) years. All other types of Director may be reappointed indefinitely by the Shareholders' Meeting.

Mr. Antonio Garamendi Lecanda has completed the maximum term of 12 years as an independent director of RED ELÉCTRICA. In accordance with Article 7.2 c) of the Board Regulations, with the Unified Good Governance Code, and with the best international good governance practices, this is the maximum term for being considered an independent director, so if his reappointment is proposed to the next Annual Shareholders' Meeting, he will be classified under the "other external directors" category.

If the Annual Shareholders' Meeting approves the reappointment of Mr. Garamendi as a director of the Company, he should be immediately replaced as chairman of the Corporate Responsibility and Governance Committee, an office which should be held by an independent director, as established in the Corporate Bylaws and the Board Regulations.

Proposals for the removal of independent directors should not be made before the end of the term of office specified in the Corporate Bylaws for which they were appointed, except where there is sufficient cause, subject to a report by the Corporate Responsibility and Governance Committee.

The names of the Directors, the dates of their first and last appointment, position on the Board, type of Director, election procedure and Board Committee membership, at December 31, 2011, were as follows:

Name of Director	First Appointment	Last Appointment	Position on the Board	Type of Director	Appointment procedure	Board Committee Membership
Luis M <sup>a</sup> Atienza Serna	07.08.04	05.21.09	Chairman	Executive	Shareholders' Meeting	Corporate Responsibility and Governance Committee (member)
Antonio Garamendi Lecanda	07.20.99	05.22.08	Member	External Independent*	Shareholders' Meeting	Corporate Responsibility and Governance Committee (Chairman)
Manuel Alves Torres	10.26.99	05.22.08	Member	External Nominee (SEPI)	Shareholders' Meeting	Corporate Responsibility and Governance Committee (member)
Rafael Suñol Trepal	12.16.04	05.21.09	Member	External Nominee (SEPI)	Shareholders' Meeting	-
M <sup>a</sup> Ángeles Amador Millán	05.26.05	05.21.09	Member	External Independent	Shareholders' Meeting	Corporate Responsibility and Governance Committee (member)
Francisco Javier Salas Collantes	06.28.05	05.20.10	Member	External Independent	Shareholders' Meeting	-
José Folgado Blanco	05.22.08	05.22.08	Member	External Independent	Shareholders' Meeting	Audit (member)
Arantza Mendizábal Gorostiaga	05.22.08	05.22.08	Member	External Independent	Shareholders' Meeting	Audit (chairwoman)
María Jesús Álvarez González	05.22.08	05.22.08	Member	External Nominee (SEPI)	Shareholders' Meeting	Audit (member)
Rui Manuel Janes Cartaxo	05.20.10	05.20.10	Member	External Independent	Shareholders' Meeting	-
Miguel Boyer Salvador	05.20.10	05.20.10	Member	External Independent	Shareholders' Meeting	-

\* Until the end of his term, which expires in April/May 2012.



## Professional Profiles of the Directors

The Company's Directors are professionals of high standing with broad professional experience. Their contribution to the management of the Company is the experience and knowledge necessary to meet the Company's needs.

Set out below are the principal activities pursued by Board members outside the Company at December 31, 2011:

### Chairman, Executive Director



**Luis Mª Atienza Serna**, born August 30, 1957.

Degree in Economics and Business Studies, Universidad de Deusto.  
Certificate in Advanced European Studies, Université de Nancy (France), Centre for Advanced European Studies.  
Centre for Advanced European Studies; Certificate in Development Economics (D.E.A.), Université de Nancy, Faculty of Law and Economics.

#### Formerly:

Minister for Agriculture, Fisheries and Food.  
Secretary General for Energy and Mineral Resources, Ministry of Industry and Energy.  
Chairman, Institute for Energy Saving and Diversification (IDAE).  
Chairman, Geomining Technological Institute of Spain.  
Chairman, Centre for Energy, Environmental and Technological Research (CIEMAT).  
Secretary General, Agrarian Structures, Ministry of Agriculture, Fisheries and Food.  
Economy Minister, Basque Autonomous Community Government.  
Member of the Basque Parliament.  
Lecturer, School of Economics and Business Studies, International Business Administration Institute and Institute for European Studies, Universidad de Deusto.  
Member of the Boards of Directors of Instituto Nacional de Hidrocarburos (INH), Corporación Logística de Hidrocarburos (CLH) and Ente Vasco de la Energía (EVE).  
He has given many courses, seminars and lectures, and has published articles on economic, energy and agrarian policy and European research in the economic and general press, including working documents for university institutes and research centers.

#### Currently:

Member of the Directory of the European Network of Transmission System Operators for Electricity (ENTSO-e).  
Chairman of the Very Large Power Grid Operators (VLPGO-GO14).  
Chairman of the Spanish-British Social Gathering Association.  
Individual representative of the corporate director of Red Eléctrica Corporación, S.A., on the Board of Directors of the Portuguese company REN-REDES ENERGÉTICAS NACIONAIS, SGPS.

## External Independent Director



**Antonio Garamendi Lecanda**, born February 8, 1958.  
Entrepreneur. Law Degree, Universidad de Deusto.

### Formerly:

General Representative of La Equitativa, S.A. in Vizcaya.  
Managing Director of Bankoa, S.A. Correduría de Seguros.  
Chairman, Handyman, S.L.  
Chairman of the "Negocios de Comunicación" Group (*La Gaceta de los Negocios, Dinero, Radio Intereconomía* and OTR News Agency).  
Director, Babcock & Wilcox Española, S.A.  
Director, Albura, S.A. (Red Eléctrica de Telecomunicaciones).  
Director, Tubos Reunidos, S.A.  
Member, Strategic Committee, Grupo Alta Gestión, S.A.  
Chairman, Spanish Confederation of Young Entrepreneurs (CEAJE).  
Chairman, Business Creation Commission, CEOE.  
Member, Vizcaya Chamber of Real Estate.  
Member, Board of Trustees, Guggenheim Museum.  
Deputy Chairman, Entel Ibai, S.A.  
Member of the Strategic Committee of Sodexho Pass, S.A. Group.  
Member of the Executive Board of the Vizcaya Business Confederation (CEBEK).

### Currently:

Chairman, Galea Empresarial, S.L.  
Chairman, Palacio de Moronati, S.L.  
Managing Director, Iniciativas de Comunicación Económica, S.A. (ICESA).  
Insurance Broker. Willis Iberia, S.A.  
Chairman of the AYUDARÉ Foundation.  
Chairman, Energy Committee, CEOE. Member, CEOE Executive Committee and Managing Board.  
First Deputy Chairman, Spanish Confederation of Small and Medium-Sized Enterprises (CEPYME).  
Member and Treasurer, Confemetal and Fundación Formetal.  
Committee Member, Institute for Economic Studies (IEE).  
Member of the Executive Committee of the Vizcaya Federation of Metal Companies.  
Member, Vizcaya Chamber of Commerce.

### External Nominee Director proposed by SEPI



**Manuel Alves Torres**, born March 18, 1954.  
Degree in Economics and Business Studies.

#### Formerly:

Head of Budgeting of Standard Eléctrica, S.A.

Graduate Technical Expert, Deputy Enterprise Director, Deputy Corporate Director of the INI.

Director of Planning and Supervision of the INI, of Teneo and of SEPI.

Member of the Board of Directors of: Potasas de Subiza, Potasas de Suria, Grupo Ence, Grupo Inespal, Enatcar, Clínica Castelló, Minas de Almagrera, Agencia Efe, Binter Canarias, Hipódromo de la Zarzuela and Sedettur.

#### Currently:

Director of Planning and Control, SEPI.

Member, Management Committee, SEPI.

SEPI representative, Fundación SEPI (formerly Fundación Empresa Pública) and Fundación Laboral SEPI.

Member, Board of Directors, Tragsa.

### External Nominee Director proposed by SEPI



**Rafael Suñol Trepas**, born July 4, 1944.  
Degree in Economics and Business Studies, E-1969, ADE-ESADE 1980, PADE-IESE 1999.

#### Formerly:

Managing Director of Aurica, SCR, S.A.

Partner of Socios Financieros and president of Activa Ventures.

Director and Deputy Chairman of Fecsa and Director of Endesa.

Managing Director of Banco de Fomento.

Chairman of Banco de Crédito Industrial and Director of ICO.

Assistant General Manager of GDS, Caja de Barcelona, after working for Banco Urquijo, Barcelona.

Chairman of Crédito & Docks and of Dinvergestión, and Director of companies related to Banco Central.

Director of Ericsson España, Frida Alimentaria and Visual Tools, and Chairman of Cobrhi.

#### Currently:

Director of Peugeot España, Inypsa, Serveis Funeraris de Barcelona and Mémora and Dalkia España.

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### External Independent Director



**Mª Ángeles Amador Millán**, born October 10, 1949.  
Law Degree, Universidad Complutense de Madrid.

#### Formerly:

Technical General Secretary, Ministry of Public Works and Urban Development.  
Undersecretary, Ministry of Health and Consumer Affairs.  
Minister for Health and Consumer Affairs.  
Member of Parliament for Segovia.  
Member of Parliament for Madrid.  
Deputy Chairwoman, Constitutional Committee, Lower House of Parliament.

#### Currently:

Practicing attorney.  
Member, Governing Board of the Madrid Bar Association.  
Board member, Fundación Arte y Derecho.  
Member, Advisory Board, Accenture.

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### External Independent Director



**Francisco Javier Salas Collantes**, born March 6, 1948.  
Degree in Economics, specializing in Business Economics.

#### Formerly:

Specialist in credit analysis activities, International Division, Manufacturers Hanover Trust Co. (New York).  
Director of Economic and Financial Planning and Director of Economy and Finance, Empresa Nacional del Uranio (ENUSA).  
Finance Director, National Industry Institute (INI).  
Director-General of Corporate Management, responsible for the following INI offices: Finance, Planning and Control, Technology and Investment.  
Chairman, INI. and Teneo.  
Chairman, Iberia, Líneas Aéreas de España, while also Chairman of INI. and Teneo.

**Currently:**

Founding Member and Manager of SAGA Servicios Financieros (Management and M&A Consultants).  
 Director of GED CAPITAL DEVELOPMENT, S.A., SGEGR and of GED IBERIAN PRIVATE EQUITY, S.A., SGEGR.  
 Chairman of Bloqmarine Internacional, S.L.  
 Member, Advisory Board, YOUNG & RUBICAM, S.L.  
 Chairman of Fundación Entorno, Empresa y Medioambiente. Trustee, Instituto de Cuestiones Internacionales y Política Exterior (INCIPE).  
 Trustee, APMIB Foundation (Deputy Chairman).  
 Member of the Advisory Board of the Fundación de Estudios Financieros.  
 Director of Abengoa Solar.

**External Independent Director**

**José Folgado Blanco**, born April 3, 1944.

Degree in Economics. Final-year award with special distinction.  
 Doctorate in Economics, Universidad Autónoma de Madrid.

**Formerly:**

Manager of the Economics Department of the CEOE.  
 Member of the Economic and Social Board representing business organizations.  
 Secretary of State for Budgets and Expenditure. Ministry of Economy and Finance, since May 1996.  
 Secretary of State for Economy, Energy and Small and Medium-Sized Enterprises. Ministry of Economy, since April 2000.  
 Secretary of State for Energy, Industrial Development and Small- and Medium-Sized Enterprises. Ministry of Economy, since July 2002.  
 Parliamentary representative of the province of Zamora and Deputy Chairman of the Economy and Finance Committee, since March 2004.

**Currently:**

Tenured Professor of Public Finance and Tax Systems, Universidad Autónoma de Madrid.  
 Mayor of Tres Cantos (Madrid) since June 2007.  
 Member of the Social Board, Universidad Autónoma de Madrid.

### External Independent Director



**Arantza Mendizábal Gorostiaga**, born February 22, 1950.  
Degree in Economics.  
Doctorate in Economics.  
Professor of Applied Economics.

#### Formerly:

Professor and researcher, industrial and technological policy.  
Acting Rector, Universidad del País Vasco (UPV-EHU).  
Professor visiting fellow at St. Anthony's College (Oxford).  
Member of Parliament.  
Spokeswoman, Industry, Tourism and Trade Committee, Lower House of Parliament.  
MP member, Economy and Finance Committee, Lower House of Parliament.  
MP member, Budget Committee, Lower House of Parliament.

#### Currently:

Professor of Applied Economics at the School of Economics and Business Administration and Director of the European Documentation Center, Universidad del País Vasco.

### External Nominee Director proposed by SEPI



**María Jesús Álvarez González**, born June 21, 1957.  
Degree in Law and Economics and Business Administration.

#### Formerly:

Member of the Board of Directors of Enusa Industrias Avanzadas, S.A.  
Member of the Board of Directors of Equipos Nucleares, S.A.  
Member of the Board of Directors of Clínica Castelló, S.A.  
Member of the Board of Directors of Indra Sistemas, S.A.  
Member of the Board of Directors of Infoinvest, S.A.  
Member of the Board of Directors of Infoleasing, S.A.  
Member of the Board of Directors of Empresa Nacional de Residuos Radioactivos, S.A. (ENRESA).  
Member of the Board of Directors of Aluminio Español, S.A.  
Member of the Board of Directors of Agencia Efe, S.A.

She has held various executive positions within SEPI and engaged in various activities in the banking and industrial sectors.

**Currently:**

Economic and Financial Director of Sociedad Estatal de Participaciones Industriales (SEPI).  
 Member of the Management Committee of SEPI.  
 Member of the Board of Trustees of Fundación SEPI and of Fundación Laboral SEPI.

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**External Independent Director**

**Miguel Boyer Salvador**, born February 5, 1939.  
 Degree in Physical Science and Economics, with special distinction,  
 Universidad de Madrid.

**Formerly:**

Director of Studies, National Industry Institute (INI.)  
 Head of Strategic Planning, Explosivos Río Tinto.  
 Member of Parliament for Jaén.  
 Director of Planning and Studies, Instituto Nacional de Hidrocarburos.  
 Minister for Economy, Finance and Trade.  
 Chairman, Banco Exterior de España.  
 Member of the Review Committee, European Organization for Nuclear Research (CERN, Geneva).  
 Member – as one of two experts – of the Expert Group on the Economic and Monetary Union of the European Union ("Delors Commission").  
 Chairman, Cartera Central.  
 Chairman and Managing Director, Grucycsa.  
 Deputy Chairman, FCC Construcción.  
 Chairman, Compañía Logística de Hidrocarburos (CLH).

**Currently:**

Representative of Corporación Financiera Issos, on the Board of Directors of Reyal-Urbis, S.A.

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### External Independent Director



**Rui Manuel Janes Cartaxo**, born on July 9, 1952.  
Degree in Economics, Universidad Técnica de Lisboa.

#### Formerly:

Lecturer, Instituto Superior de Economía y Gestión (ISEG).  
Economist, research area, Banco de Portugal.  
Consultant, OECD Department of Research (Paris).  
Financial Director, Ministry of Finance.  
Executive Director, CN-Comunicações Nacionais, SGPS, S.A.  
Executive Director, TRANSGÁS, S.A.  
CEO of GALP POWER.  
Executive Director, GALP ENERGÍA SGPS.  
Assistant to the Portuguese Minister of Economy and Innovation.  
CFO of REN-REDES ENERGÉTICAS NACIONAIS, SGPS.

#### Currently:

Chairman and CEO of REN-REDES ENERGÉTICAS NACIONAIS, SGPS.

### Nondirector Secretary of the Board of Directors



**Rafael García de Diego Barber**, born July 27, 1951.

He was appointed Secretary of the Board of Directors and legal advisor at the Board meeting held on May 4, 1995.

Law degree, Universidad Complutense, Master's Degree in Tax Counseling for Businesses, Instituto de Empresa.

#### Formerly:

Lawyer, Loss Department, Zurich, S.A., Lawyer and Secretary to boards of directors of companies in the Inmobiliario Pradis Group, Lawyer and tax advisor of Ageco, a financial and tax management company of Banco Internacional de Comercio, S.A., Lawyer of the Legal Department of Sociedad Española de Carbón Exterior, S.A. (CARBOEX), Lawyer of the Legal Department and Head of the Legal Department of Red Eléctrica de España, S.A.

#### Currently:

Member of the Madrid Bar Association, Head of the Legal Department of Red Eléctrica de España, S.A. since 1995, Director of the Dutch company Red Eléctrica de España Finance B.V., Joint Director of Red Eléctrica Financiaciones, S.A.U. and Director of the Luxembourg company REDCOR Reaseguros, S.A.



### Nondirector Deputy Secretary of the Board of Directors



**Fernando Frías Montejo**, born March 11, 1965.

He was appointed Deputy Secretary of the Board of Directors at the meeting held on April 21, 2005.

Degree in Law and Certificate in Business Studies, Universidad Pontificia de Comillas (ICADE-E-I).

#### Formerly:

Member of the Legal Department of Red Eléctrica de España, S.A. since 1990 and secretary of the Board of Directors of Infraestructuras de Alta Tensión, S.A., Red de Alta Tensión, S.A. and Tenedora de Acciones de Redesur, S.A.

#### Currently:

Member of the Madrid Bar Association, and member of the Legal Department of Red Eléctrica de España, S.A. since 1990.

### Attendance at and Failure to Attend Board and Committee Meetings

Set out below are the data on attendance and failure to attend by Company Directors at meetings of the Board of Directors and of the Audit and Corporate Responsibility and Governance Committees in 2011.

- ◆ Board of Directors: There were seven (7) absences from the eleven (11) Board meetings held in 2011, giving rise to an attendance rate of 94%.
- ◆ Audit Committee: Of the ten (10) Audit Committee meetings held in 2011, no Directors failed to attend.
- ◆ Corporate Responsibility and Governance Committee: Of the eleven (11) Corporate Responsibility and Governance Committee meetings held in 2011, no Directors failed to attend.

### Chairman of the Board

- ◆ The Chairman of the Board of Directors is also the Chairman of the Company, its Chief Executive and the person responsible for senior management, administration and full representation of the Company.
- ◆ Notwithstanding the above, Board of Directors, in the Board Regulations, has reserved, on a non-delegable basis, the responsibilities and powers that it considers strategic and which have been described in this Chapter.
- ◆ The Executive Director is subject to specific checks on his responsibilities by the Board of Directors, to which he must request subsequent ratification regarding urgent decisions that he has had to adopt or, as the case may be, request prior authorization. The Committees effectively control the corporate management within the scope of their respective powers.

## Directors' Duties

- ◆ The internal corporate governance rules strictly regulate the duties of Directors, in general, and their diligence and loyalty obligations, in particular.
- ◆ Directors must act with due diligence, being required to play a proactive role on the Board and on its Committees.
- ◆ The Board Regulations also regulate breaches of the corporate governance rules by Directors.

## Principle of Security and Duty of Loyalty

- ◆ The Board Regulations establish, inter alia, the following obligations on Directors:
  - To gather the relevant information and adequately prepare for meetings of the Board and the Board Committees to which they belong, and regularly attend them.
  - To actively participate in deliberations so that their opinions effectively contribute to decision-making and to perform any specific tasks entrusted to them by the Board of Directors.
  - To prompt the investigation of any irregularity in the management of the Company of which they may become aware, and the monitoring of any risk situation.
  - To request the call of special Board meetings, as the case may be, and gather the information necessary for the efficient performance of their functions.
  - To oppose resolutions that are contrary to the law, the Corporate Bylaws or the corporate interest.

## Conflicts of Interest

- ◆ Directors must refrain from attending and participating in deliberations that touch on matters in which they have a direct or indirect personal interest.
- ◆ Directors must report any potential conflict of interest they may have with the Company and, where there is a conflict, they must refrain from participating in the transaction to which the conflict of interest relates.
- ◆ Nominee Directors must disclose to the Board any conflict of interest between the Company and the shareholder that proposed their appointment where the conflict of interest relates to matters submitted to the Board and must refrain from participating in the adoption of the corresponding resolutions.

## Confidentiality

- ◆ Directors must maintain secrecy regarding the deliberations of the Board of Directors and the Committees of which they are members.
- ◆ Directors must refrain from disclosing any information, data, reports or background information to which they may have access in the discharge of their office, even after they have vacated office.

## Noncompetition

- ◆ Directors may not engage in activities that may compete with the Company.
- ◆ Directors may not provide their professional services to companies with a corporate purpose that is analogous, in whole or in part, to that of the Company that may give rise to a conflict of interest between them.



- ◆ Independent Directors are required to consult the Board of Directors before accepting any executive position with another company or entity.
- ◆ Directors are required to report any holdings they may have in companies that engage in any activity that is identical, analogous or complementary to that of the Company or competes to some degree with the Company, as well as any positions or functions exercised at such companies and the performance, for their own account or for the account of another, of activities that are identical, analogous or complementary to the type of activity constituting the corporate purpose.
- ◆ The Board Regulations establish a new restriction for Independent Directors, who may not sit on more than two boards of directors of other listed companies.

### Information not in the Public Domain

- ◆ Directors may not use Company information that is not in the public domain for private purposes, except with the prior approval of the Board of Directors.

### Business Opportunities

Directors may not, for their own benefit or the benefit of related persons or third parties, take direct or indirect advantage of any business opportunity of the Company, unless the opportunity is offered to the Company beforehand, and the Company declines to take it and Board authorizes the Director to do so, subject to a report by the Corporate Responsibility and Governance Committee.

### Directors' Portal

The Directors' Portal is an innovative project that was launched in January 2010 with a view to applying new technologies in the day-to-day work of the members of the Board of Directors and its Committees.

This initiative seeks to place the most modern telematic means at the disposal of the directors to enhance efficiency in the functioning of the Board of Directors and its Committees. The Portal has been designed with the aims of making the current processes more efficient, and ensuring the security of the information.

The content of the portal is divided into various sections on documentation, distinguishing between documents for Board meetings, documents for the two Committees, other documents of special interest prepared by the Board, various areas within the corporate information of the Company, the main legislation affecting the activities of the Company, all the corporate information of interest to Directors for the discharge of their duties, information on the activities and functioning of the various organizational areas of the Company, information in the press affecting the Company and other information which may be useful for Directors to gain a better understanding of the activity and functioning of the Company and for the performance of their duties as Directors.

In 2010, the contents of the Directors' Portal were expanded to include all available information on corporate responsibility matters.

In 2011 technical improvements were made and corporate information was expanded, thereby enhancing a tool which is highly valued by the Directors.

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

## Evaluation of the Board

In line with annual practice, at the beginning of 2011 the Board initiated, through the Corporate Responsibility and Corporate Governance Committee, the self-evaluation process relating to the Board of Directors, its Committees and its Chairman.

By an express decision of the Corporate Responsibility and Governance Committee, the self-evaluation process is being conducted with the support of external advisers with expertise in the area (KPMG) thereby providing the process with a more objective and independent external viewpoint.

The conclusions from the KPMG report on the findings of the evaluation performed make clear the high level of commitment on the part of the Directors, their pride in belonging to the organization, their commitment to excellence in managing the Company and to the ongoing incorporation of corporate governance best practices. The same report sets out certain opportunities for improvement in the Board's practices, including those relating to enhancing communication with shareholders and investors in general, strengthening the role of independent directors in the Board's tasks or the role of the Board in defining and monitoring the risk control policy.

## Board Compensation Policy

The main elements and aspects of the Board's compensation policy have been described in Chapter I of this Title II, to which readers are referred.

The Annual Report on Directors' Compensation which, for the first time, is provided to shareholders and investors in general, separately from this Annual Corporate Governance Report, sets out in detail all the information on the compensation of the Board of Directors and of Senior Management.

## Committees of the Board of Directors

Since the Company's listing on the securities markets in 1999, its financial statements and economic and financial information have been prepared under the supervision and oversight of the Audit Committee, leading to greater transparency and reliability.

Pursuant to the Board Regulations and the Corporate Bylaws, there is a specific Committee for corporate governance matters called the Corporate Responsibility and Governance Committee.

Both Committees constitute support committees for the Board of Directors and have not been expressly delegated any powers by the latter.

## Audit Committee

The powers, organization and functioning of the Audit Committee are governed by the Corporate Bylaws and by the Board Regulations of RED ELÉCTRICA, adapted to current commercial legislation and the recommendations of the Conthe Code.

Throughout 2011, the Committee was comprised of External Directors, with a majority of Independent Directors. At a meeting on July 27, 2011, the Board of Directors, following a report from the Corporate Responsibility and Governance Committee, approved the reappointment for a term of 3 years of two of its directors as board members (Ms. Arantza Mendizábal Gorostiaga and Ms. María Jesús Álvarez González) and designated Mr. José Folgado Blanco as a new board member for a term of 3 years following the expiration of the term for which Mr. Francisco Javier Salas Collantes had been appointed.

The composition of the Audit Committee at December 31, 2011 was as follows:

Director	Position	Type of Director
Arantza Mendizábal Gorostiaga	Chairwoman	External Independent
José Folgado Blanco	Member	External Independent
María Jesús Álvarez González	Member	External Nominee (SEPI)

Chapter IV of Title III of this document contains the Annual Report on the Activities of the Audit Committee for fiscal year 2011.

### Corporate Responsibility and Governance Committee

In accordance with best international corporate governance practices and particularly those indicated in the Conthe Code, in 2007 the Company's Board of Directors changed the name of the Committee to the Appointments, Compensation and Corporate Governance Committee. Pursuant to the Corporate Bylaws it was assigned functions relating to the corporate governance of the Company, among others.

In 2009, the Committee carried out a review of the Board Regulations which led to the approval of a new set of Regulations at the meeting held on January 28, 2010. Some of the most notable amendments approved included the change of name to the Corporate Responsibility and Governance Committee and the express allocation to such Committee of broad powers in the area of corporate responsibility and risk control.

At 2011 year-end and at the date of approval of this Report, the Corporate Responsibility and Governance Committee was composed of four Directors, three of whom were External Directors and one an Executive Director: of the External Directors, two were Independent Directors and one was a Nominee Director.

At a meeting held on July 27, 2011, the Board of Directors, following a report from the Corporate Responsibility and Governance Committee and at the proposal of the Chairman of the Board of Directors, approved the reappointment of two of its directors as board members (Mr. Luis M<sup>a</sup> Atienza Serna and Mr. Manuel Alves Torres) for a term of 3 years.

At 2011 year-end and on the date of approval of this Report, the composition of the Committee was as follows:

Director	Position	Type of Director
Antonio Garamendi Lecanda	Chairman	External Independent
María Ángeles Amador Millán	Member	External Independent
Luis María Atienza Serna	Member	Executive
Manuel Alves Torres	Member	External Nominee

If the Annual Shareholders' Meeting approves the reappointment of Mr. Garamendi as a director of the Company, given that he is no longer considered an independent director because 12 years have elapsed since his first appointment as a director, he should be immediately replaced as chairman of the Corporate Responsibility and Governance Committee, since this office must be held by an independent director, as established in the Corporate Bylaws and in the Board Regulations.

The Executive Director and Chairman of the Company, Mr. Luis Maria Atienza Serna, is a member of the Committee by unanimous decision of the Board of Directors, which considers his presence on the

Committee to be of special interest, without prejudice to his abstaining or absenting himself during discussion of any matters that could affect him personally or give rise to a conflict of interest.

Of the four members of the Corporate Responsibility and Governance Committee, three are External Directors and two of them are Independent Directors, meaning that they constitute a relative but not absolute majority.

Further to the comments on Recommendation 44, it must again be stated that Independent Directors have a voting majority on the Corporate Responsibility and Governance Committee, since in the hypothetical event of a tie between Independent and other Directors, the Chairman, who must be an Independent Director, has a casting vote.

Chapter IV of Title III of this document contains the Annual Report on the Activities of the Corporate Responsibility and Governance Committee for fiscal year 2011.

## Chapter V. Senior Management

The persons holding senior management positions at the Company throughout 2011, excluding the chief executive, were as follows:

Name	Position
Carlos Collantes Pérez-Ardá	Director-General of Transmission
Esther María Rituerto Martínez	Director-General of Finance and Administration
Alberto Carbajo Josa	Director-General of System Operation

Article 16 of the Board Regulations establishes, among the basic responsibilities of the Corporate Responsibility and Governance Committee, that of informing about any appointments and removals of senior executives of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company, that the Chairman proposes to the Board of Directors. However, in 2011 no senior managers were appointed or removed.

The above executives report directly to the Chief Executive and Chairman of the Company and form part of the main executive bodies in the organization, the Management Committee and the Executive Management Committee.

The compensation policy applicable to these executives aims to promote the achievement of the strategic objectives of value creation at the Company by attracting, retaining and motivating the best talent available in the market.

Compensation for the Company's senior executives is based on the principles of moderation, actual dedication and linkage to the results of the Company.

The annual reports on the compensation policy for the Board approved by the Board of Directors and by the Annual Shareholders' Meetings in recent years present information on the total compensation paid to these executives.

As regards compensation for fiscal year 2011, please see the Annual Report on Directors' Compensation, which includes information on senior executives.

## Chapter VI. Risk Policy and Internal Control Systems

### General aspects

The purpose of the Risk Policy of the Red Eléctrica Group, approved by the Board of Directors on July 24, 2008, is to establish principles and guidelines to ensure the systematic identification, analysis, assessment, management and control of material risks that may affect the Red Eléctrica Group's objectives and activities, applying uniform criteria, within the established risk limits.

Material risks of the Red Eléctrica Group are those that may significantly affect the overall objectives of the Red Eléctrica Group, related to:

- ◆ Sustained creation of value over time.  
Sustained profit growth, which must allow appropriate returns for investors and enable the company to implement its strategy.
- ◆ The continuity and quality of the energy supply in the electricity systems.  
The achievement of this objective involves on the one hand the management by the Operator of the Spanish Electrical System and on the other the reliability and availability of the transmission network.
- ◆ The construction of the electricity transmission infrastructure network necessary to meet future needs.  
Red Eléctrica, as the sole transmission company of the Spanish Electrical System, must design, fulfill the formalities for and construct the facilities specified by energy planning. This overall objective must be achieved on a cost-effective basis.
- ◆ The compatibility of the above objectives with social and environmental concerns.  
This Policy establishes criteria on the acceptable level of risk for each of the overall objectives, which may be summarized as follows: all material risks that could jeopardize achievement of the overall objectives must have a low probability/impact value. Steps must be taken to ensure that any risks that do not meet this value are lowered to such level.

The general guidelines contained in the Risk Policy are as follows:

- ◆ Risk management must be fundamentally proactive and also geared towards the medium and long term, taking into account possible scenarios in an ever more globalized environment.
- ◆ In general, risks must be managed according to the relationship between the importance of the risk (probability/impact) and the investment and resources necessary to reduce it.
- ◆ Notwithstanding the above, the impact the risks may have on the electricity system itself must also be taken into account with respect to activities relating to the electricity system.
- ◆ Processes must be designed with efficiency and efficacy in mind and contemplate controls to mitigate risks, taking the form of systems based on international standards (good practices) that are periodically verified and improved.
- ◆ Contingency plans must be established to reduce the impact of material risks.
- ◆ The insurance necessary to cover any losses that may occur must be arranged.



The most significant risks to which the Group is exposed, and which form part of the risk control system, are:

- a) Regulatory, since the principal business activities of the Group are subject to regulation.
- b) Operational, basically arising from its assigned activities within the electricity system and the requirement to care for and protect the natural environment.
- c) Market, since most revenues, as well as certain expenses, may be influenced by variables such as inflation and interest rates.
- d) Business and Credit (or counterparty), albeit to a lesser extent due to the lesser weight of the subsidiaries in the overall Group and the existing regulation regarding invoicing and collection for transmission and operation activities.

The risk control system covers both risks from internal processes and risks from the environment in which it operates, covering all activities performed by the Group, evaluating the impact of each risk on four aspects: strategy, the income statement, the electricity system and reputation.

Of all risks monitored by the system, 11 % relate to regulatory risks, 75% to operational risks and 14% to business, market or credit risks. These figures are consistent with a Group whose fundamental mission is to ensure the functioning of the electricity system as a whole in a heavily regulated environment and with the level of solvency supported by the ratings given to it by international rating agencies.

In 2011 the risk control system was subjected to an independent review of its design by the specialist consultant Ernst & Young, based on the ISO 31000 standard (Risk management. Principles and guidelines). The conclusion issued by Ernst & Young on January 14, 2012 reads as follows:

"As a result of our review, we can conclude that the design of the Risk Management System of Red Eléctrica Corporación, applied to its different activities, is in accordance with the principles established in the ISO 31000 standard on Principles and Guidelines."

Furthermore, it should be noted that in 2007 Red Eléctrica embarked on a project to align, review and improve its System for Internal Control over Financial Reporting (ICFR), with the basic aim of improving the efficiency and security of processes for preparing economic and financial information on the Company, adopting international best practices early on, on a voluntary basis. This ICFR is described in detail in one of the sections of Official Annex II to this ACGR, as an Annex which includes information additional to the current ACGR in accordance with Article 61 bis of Securities Market Law 24/1988, of July 28, as amended by Sustainable Economy Law 2/2011, of March 4, 2011.

In particular, Annex II on the ICFR includes information, among other aspects, on the mechanisms making up the risk management and control systems in relation to the process for reporting financial information (ICFR) of Red Eléctrica, which refer to its control environment, to financial information risk evaluation, to control activities, to the tasks of reporting and communication and to the supervision and operation of the system.

The Board Regulations expressly entrust the **Board of Directors** with the responsibility of approving the comprehensive risk management policy of the Company and of the Group, and of being familiar with and periodically monitoring the internal control, prevention and reporting systems.

Twice a year the Board reviews the risk control system and the material risks, notwithstanding the information that it regularly receives from the Audit Committee in the context of the monitoring carried out by such Committee on an ongoing basis.

The **Audit Committee** is responsible for the periodic supervision of the risk management system, to ensure that the main risks are adequately identified, managed and disclosed.

The **Management Committee**, comprised of executives from the key strategic areas of the Company, is responsible for:

- Promoting implementation of the integral risk management policy.
- Monitoring the Risk Map, and agreeing on the appropriate actions to facilitate the achievement of the global objectives.

The risk control function is performed on a centralized basis by the **Regulation Office**, which reports to the Office of the Chairman.

### Procedures

The RED ELÉCTRICA Group constantly designs and implements processes to ensure its compliance with the various regulations and to mitigate or reduce the related risks.

These processes have been integrated into systems structured according to a set of internal standards and procedures based on international standards (ISO 9001, ISO 14001 and OHSAS 18001), which are subject to systematic audits of the adequacy of their design and compliance, and include mechanisms for controlling the objectives that they must meet.

### Projects

All proposals for significant projects from an economic or strategic point of view include the corresponding risk analysis, allowing risks to be evaluated when the related decisions are to be made. These decisions are made by the competent corporate body according to the established limits, with the most important projects requiring the approval of the Board of Directors.

### Verification

The design and adaptation to existing regulations of, and correct compliance with, the internal rules and procedures is systematically reviewed by the Internal Audit and Risk Management functions, which form an integral part of the Regulation Office, and these procedures are also supervised by the Audit Committee.

Internal rules and their compliance are also subject to external audits on a periodic basis, by international ISO and OHSAS standards certification bodies.

### Self-evaluation of regulatory compliance

In 2011, an internal rule was approved and implemented which requires all units of the organization to establish mechanisms for identifying, disseminating and updating the regulations applicable to them, as well as performing an annual self-evaluation of compliance with such regulations.

## Chapter VII. Related-Party Transactions

In relation to the Directors, Article 29.3 a) of the Board Regulations establishes that Directors must notify the Board of Directors, through the Chairman or the Secretary, of any conflict of interest to which they are subject and refrain from attending and participating in deliberations affecting matters in which they have a direct or indirect personal interest or in which there is any sign of a conflict of interest. Pursuant to that Article, a personal interest will also be considered to exist when the matter affects a person related to the Director or to a company with which he has an employment or professional relationship or at which he has an executive position or a significant shareholding.

For the purposes of the preceding paragraph, 'related persons' are those defined as such from time to time in the applicable legislation.

In accordance with the provisions of Article 29.3 b) of the Board Regulations, Nominee Directors must disclose to the Board of Directors any conflict of interest between the Company and the shareholder that proposed their appointment where said conflict affects matters submitted to the Board and they must refrain from participating in the adoption of the corresponding resolutions.

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

Under Article 7 of the Internal Code of Conduct on the Securities Market, persons subject or temporarily subject thereto must generally attempt to avoid situations of direct conflict of interest or conflicts concerning persons related to them and must inform the Oversight Body of any situations of conflict of interest that may reasonably arise within fifteen (15) days of such situations coming to their attention, so that the Oversight Body may adopt the corresponding decisions in advance. Directors must give notice of the situations described in the preceding paragraph through the Office of the Secretary of the Board of Directors.

Persons subject or temporarily subject to the Code must keep up to date the information regarding conflicts of interest they have disclosed, reporting any such changes as may occur. Without prejudice to the obligations specified in the preceding paragraph as regards conflicts of interest, Directors must comply with the requirements contained in the Corporate Bylaws and in the Board Regulations and, in general, with all requirements arising from the corporate/commercial legislation on corporations.

The Oversight Body will keep an up-to-date itemized Register of the conflicts of interest disclosed by the various persons subject or temporarily subject to the Code, and will adopt the appropriate security measures for its safekeeping and storage. In any event, access to the Register will be restricted.

It should be noted that for the above purposes, in accordance with Article 11 of the Internal Code of Conduct on the Securities Market, the Oversight Body is the Directorate-General of Administration and Finance, which will act in collaboration with the Secretary of the Board of Directors as regards any legal issues resulting from the application or interpretation of the Code. In addition, the Oversight Body has been entrusted with the general functions of ascertaining, registering, disseminating and monitoring compliance with the obligations and duties established in the Internal Code of Conduct. The Oversight

Body will have all necessary powers to perform the duties entrusted to it in the Internal Code of Conduct and must periodically report to the Audit Committee on the degree of compliance with the Code and on any incidents that may occur.

The Audit Committee is responsible for supervising compliance with the Internal Code of Conduct and the performance of the functions of the Oversight Body, the person responsible for the material transaction and the Office of the Secretary of the Board of Directors contemplated therein, as well as the internal resolution of any such questions and conflicts raised by parties subject or temporarily subject to the Code as may be submitted to the Committee by the Oversight Body. The Audit Committee will evaluate compliance with the Internal Code of Conduct on an annual basis and will adopt any appropriate measures for its optimum implementation and improvement. It is also responsible for proposing to the Corporate Responsibility and Governance Committee, for referral to the Board of Directors, any amendments it deems necessary in light of the Board's commitment to continuous adaptation, as well as the adoption of corporate governance best practices in the area and of the applicable legislation.

In relation to Company executives, Article 2.1.3 of the Internal Code of Conduct on the Securities Market establishes that Company executives, as defined in Chapter 1, are deemed to be subject to the Code and, accordingly, will be subject to potential conflicts of interest. Article 5.2.2 of the Internal Code provides that, when circumstances so require, the Oversight Body may decide to include as persons subject to the Code, on a temporary basis, any persons participating in a material transaction that have access to inside information. The parties affected will be given individual written notice of their inclusion on or exclusion from those lists.

In accordance with the provisions of Article 31 of the Board Regulations, the Board of Directors formally reserves the right to be informed of any material transaction of the Company with a significant shareholder, unless as a result of its nature and conditions it falls within the jurisdiction of the Shareholders' Meeting.

In May 2010, at the proposal of the Audit Committee, the Board of Directors approved a policy on controlling related-party transactions and defined objective parameters for controlling related-party transactions, material or otherwise, recurring annual related-party transactions, and related-party transactions requiring mandatory notification to the markets. The Audit Committee monitors this policy annually.

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## TITLE III: Fiscal Year 2011 at Red Eléctrica

## Chapter I. Principal Corporate Resolutions

The principal corporate resolutions adopted by the Company in 2011 as regards corporate governance were as follows:

1. The Company's 2010 Annual Corporate Governance Report was approved following a favorable report by the Corporate Responsibility and Governance Committee at the Board meeting held on February 24, 2011.
2. At a meeting held on February 24, 2011, the Board of Directors also approved all the proposed resolutions and reports to be submitted to the Annual Shareholders' Meeting for fiscal year 2011, which was called at such meeting.
3. At the same meeting referred to above, the Board of Directors approved the procedure for proxies, voting and information by remote means at the Annual Shareholders' Meeting for fiscal year 2010.
4. In addition, as a new development, at the aforementioned meeting the Board of Directors approved the Operating Rules of the Shareholders' Electronic Forum.
5. The following resolutions were adopted, as separate and independent items on the agenda, by the Annual Shareholders' Meeting held on April 13, 2011:
  - ◆ To approve the Financial Statements (balance sheet, income statement, statement of changes in equity, cash flow statement and notes to financial statements) and the management report of Red Eléctrica Corporación, S.A. for the year ended December 31, 2010.
  - ◆ To approve the Consolidated Financial Statements (consolidated balance sheet, consolidated income statement, consolidated overall income statement, consolidated statement of changes in equity, consolidated cash flow statement and notes to the consolidated financial statements) and the Consolidated Management Report of the Consolidated Group of Red Eléctrica Corporación, S.A. for the year ended December 31, 2010.
  - ◆ To approve the distribution of income proposed by the Board of Directors at the meeting held on February 24, 2011 and, as a result, distribute 2010 income.
  - ◆ To approve the management by the Board of Directors of Red Eléctrica Corporación, S.A. in 2010.
  - ◆ To approve the appointment of the auditors of the Parent Company and of the Consolidated Group.
  - ◆ To approve the amendment of the Corporate Bylaws to update their provisions as a result of various legislative reforms relating to corporations. Specifically, the following Articles: Article 1 ("Name and legal regime"), Article 6 ("Accounting record of shares"), Article 7 ("Rights attaching to shares"), Article 8 ("Increase and reduction of capital stock"), Article 11 ("Shareholders' Meeting"), Article 12 ("Types of Shareholders' Meeting"), Article 13 ("Call to the Shareholders' Meeting"), Article 14 ("Quorum"), Article 15 ("Right to information and attendance of Shareholders' Meetings"), Article 17 ("Presiding panel, deliberations"), Article 18 ("Minutes"), Article 20 ("Board of Directors"), Article 22 ("Board Committees and delegation of powers"), Article 23 ("Audit Committee"), Article 24 ("Appointments and Compensation Committee"), Article 29 ("Audit"), Article 32 ("Rules and method of liquidation") and Article 33 ("Scope of these Bylaws").
  - ◆ To approve the amendment of the Regulations of the Shareholders' Meeting to update their provisions as a result of various legislative reforms relating to corporations: Specifically, the following articles: Article 1 ("Purpose and entry into force of the Regulations"), Article 2 ("Company website"),

Article 3 ("Powers of the Shareholders' Meeting"), Article 5 ("Call notice"), Article 6 ("Shareholders' rights"), Article 8 ("Shareholders' right to information"), Article 9 ("Right to attend"), Article 11 ("Quorum"), Article 15 ("Constitution, deliberation and adoption of resolutions"), and Article 16 ("Minutes of the Shareholders' Meeting and certificate") of the Regulations of the Shareholders' Meeting.

- ◆ To approve the following authorizations for the derivative acquisition of treasury stock, voting separately on each of them:
    - Authorization for the derivative acquisition of treasury stock by the Company or by companies of the Red Eléctrica Group, and for the direct award of treasury stock to employees and Executive Directors of the Company and of the companies of the Red Eléctrica Group, as compensation.
    - Approval of a Compensation Plan for members of Management and the Executive Directors of the Company and of the companies of the Red Eléctrica Group.
    - Revocation of previous authorizations.
  - ◆ In relation to the Board compensation policy:
    - Approval of the report on the compensation policy for the Board of Directors of Red Eléctrica Corporación, S.A.
    - Approval of the compensation of the Board of Directors of Red Eléctrica Corporación, S.A. for 2010.
  - ◆ To delegate the broadest powers to be exercised on a several basis to the Chairman and to each of the members of the Board of Directors, and to the Secretary and Deputy Secretary of the Board, so that they may implement, execute and register each and every one of the resolutions adopted by the 2010 Shareholders' Meeting.
  - ◆ To report to the Shareholders' Meeting on each of the following matters:
    - The 2010 Annual Corporate Governance Report of Red Eléctrica Corporación, S.A.
    - The elements contained in the Management Report relating to Article 116 bis of the Securities Market Law.
6. The Board of Directors, in a meeting held on July 27, 2011, within the framework of the ongoing commitment to adopt corporate governance best practices, approved the Report on Gender Diversity which was submitted to the Corporate Responsibility and Governance Committee. Of note in the Report, as a new development, was the grant of the Equality in the Workplace logo by the Ministry of Health, Social Policy and Equality. This Report was published on the Company's website.
  7. At the same Board meeting referred to in the preceding point, an analysis was performed of the Company's Equality Policy, which was approved with a favorable report by the Corporate Responsibility and Governance Committee. Red Eléctrica's Equality Policy will be carried out by implementing in the organization the appropriate internal procedures and an Integral Equality Plan, which will be subject to ongoing monitoring and evaluation by such Committee.
  8. The Board of Directors, in a meeting held on October 27, 2011, at the proposal of the Corporate Responsibility and Governance Committee and in accordance with the provisions of Article 16 of the Board Regulations, approved the Plan for the Succession of the Chairman of the Company, complying with an increasingly common corporate governance recommendation worldwide, whereby large listed companies prepare and approve plans for the succession of their most senior executive or CEO, in order to reduce the impact that the change will have on the organization, endeavoring to ensure continuity in the corporate business and reducing, as far as possible, the risks and adverse effects

that may arise from the appointment of a new chairman, until he or she is fully integrated into the post. The chairman succession plan of the Company was approved on the basis of the special conditions present in Red Eléctrica's chief executive, which position is held by the chairman of the Board of Directors, as established in Article 25 of the Corporate Bylaws, which will require the candidate to have a particular set of skills, abilities and experience. The Plan establishes a succession procedure split into several phases, establishing the bodies responsible for the procedure, in order to create an environment in which the appointment of the Chairman may be carried out in an orderly and efficient manner that affects the normal operation of the Company as little as possible.

## Chapter II. Main Awards and Recognition

There follows a list of the main awards and recognition received by the Company in fiscal year 2011 in the area of corporate governance; although some of them were obtained in the context of distinction in the area of corporate responsibility, the corporate governance aspect was acknowledged.

1. Inclusion, for the sixth year running, in the renowned Dow Jones Sustainability World Index (DJSI) with a score of 76 points out of 100.
2. "SAM Bronze" distinction of the Sustainability Yearbook 2011, a publication which distinguishes companies that stand out for their actions in corporate responsibility and sustainability and which make up the DJSI. Distinction awarded by the sustainability agency that analyzes the performance of Red Eléctrica in the area of sustainability and corporate responsibility.
3. Obtainment of an overall score of 4.5 points out of a maximum of 5 in the FTSE4Good index, following the last review performed in September 2011. This index, specialized in sustainability, includes listed companies throughout the world which meet the requirements pre-established by the stock exchange index.
4. Inclusion in September 2011 in the family of indexes of STOXX Global ESG Leaders, a company specialized in sustainability, which offers a representative sample at world level of leading companies in environmental, social and good governance standards, following the analysis performed of the information provided by Sustainalytics on the management of the company in the environmental, social and governance areas. In creating this index, consideration is given to the rankings of noteworthy companies in each area, that is, the sub-indexes STOXX Global ESG Environmental Leaders, the STOXX Global ESG Social Leaders and the STOXX Global ESG Governance Leaders.
5. Inclusion in the Aspi Eurozone index in September 2011, prepared by an agency specialized in sustainability, for its noteworthy efforts in the areas of corporate governance, environment, human rights, human resources, commitment to community and good business conduct.
6. Continuation of the Company in 2011 in the EMU ECPI Equity indexes, which include the 300 ethical companies within the EMU (Economic and Monetary Union), since its inclusion in 2008 for its responsible practices in social, environmental and corporate governance matters. With respect to these indexes, Red Eléctrica was included in the Ethical EMU Equity index in 2011.
7. First place, for the sixth year running, according to the study "Corporate Social Responsibility (CSR) in the annual reports of IBEX 35 Companies" published by the Corporate Social Responsibility Observatory. The Company ranks among the top companies in the area of corporate governance.



8. First place, for the fourth year running (and first place obtained in a total of 5 editions), in the 2011 report on the study of Corporate Social Responsibility of the IBEX 35, published by the Corporate Social Responsibility Observatory. The Company ranks first in corporate governance matters.
9. Third place in the Reporta Report for 2011, on the quality of financial and non-financial public information of companies in the General Index of the Madrid Stock Exchange (IGBM), (report published by the financial communications agency, Deva). The Report classifies Red Eléctrica as the most transparent company, which takes into account, among others, corporate governance matters.
10. EFQM (European Foundation for Quality Management): Red Eléctrica obtained in 2011 the Award for business excellence in the category "Assuming responsibility for a sustainable future", within the distinctions which EFQM awards each year to the best European companies in the adoption of the most advanced business management and practices systems.

## Chapter III. Material Events Disclosed to Markets

Immediately after their approval by the Board of Directors, the call notice and proposed resolutions and other documentation relating to the Shareholders' Meeting are notified to the CNMV and published on the Company website.

On the same day as the Meeting is held or on the immediately following business day, the Company sends the text of the approved resolutions to the CNMV by means of the relevant disclosure of a material event.

Once they have been notified to the CNMV, the text of the approved resolutions is also made available on the Company website.

To promote the right to information of shareholders of the Company abroad, who represent nearly 70% of all shareholders, all the documentation that is submitted for information purposes and for approval at the Shareholders' Meeting, including the Annual Corporate Governance Report, is translated into English and published in English on the Company's website, on the same day that the material events in question are published.

The material events notified to the CNMV in 2011 were as follows:

### 1. Information on corporate transactions

On January 28, 2011, the SEPI notified that it had initiated administrative proceedings to obtain the necessary authorizations to sell up to 10% of the capital stock of Red Eléctrica Corporación, S.A.

### 2. Call notices for meetings or information events

On February 1, 2011, Red Eléctrica announced that it would publish the results for fiscal year 2010 and the 2011-2015 strategic plan on February 25.

### 3. Initial public offering and sale of notes and other instruments

On February 4, 2011, it was communicated to the CNMV that Red Eléctrica Corporación, S.A., through its subsidiary Red Eléctrica Financiaciones, S.A. Sole-Shareholder Company, had made a six hundred (600) million euro issue of notes on the euromarket.

#### 4. Call notices for meetings or information events

On February 10, 2011, the Company announced a change in the schedule for the presentation of the 2010 results and the 2011-2015 strategic plan that was going to take place on Friday, February 25.

#### 5. Corporate transactions

On February 17, 2011, the Company communicated that RED Eléctrica de España, S.A. Sole-Shareholder Company had completed the acquisition of the assets of the transmission grid from Hidrocantábrico Distribución Eléctrica, S.A. Sole-Shareholder Company.

#### 6. Information on results

The FY2010 results of the Red Eléctrica Group were published on February 25, 2010.

#### 7. Information on dividends

On February 25, 2011, the Company notified the CNMV that the Board of Directors of Red Eléctrica Corporación, S.A. had resolved at a meeting held on February 24, 2011 to propose to the Annual Shareholders' Meeting the payment to holders of shares entitled to a dividend of a gross dividend of €1.8751 per share.

#### 8. Call notices and resolutions of shareholders' meetings and general assemblies

On February 25, 2011, it was communicated to the CNMV that the Board of Directors in its meeting of February 24, 2011 had resolved to call the Annual Shareholders' Meeting.

#### 9. Interim financial information

The Company sent information on the results for the second half of 2010 on February 25, 2011.

#### 10. Annual Corporate Governance Report

On February 25, 2011, the 2010 Annual Corporate Governance Report, approved by the Board of Directors at the meeting held on February 24, 2011, was communicated to the CNMV.

#### 11. Strategic plans, forecasts and presentations

On February 25, 2011, the Company sent the CNMV the 2010-2015 Strategic Plan.

#### 12. Call notices and resolutions of shareholders' meetings and general assemblies

On March 9, 2011, the Company informed the CNMV of the call notice for the Shareholders' Meeting and the proposed resolutions.

#### 13. Information on corporate transactions

On April 8, 2011, the SEPI notified that the Council of Ministers had authorized the sale of up to 10% of Red Eléctrica Corporación, S.A.

#### 14. Call notices and resolutions of shareholders' meetings and general assemblies

On April 14, 2011, the Company communicated to the CNMV the full wording of the resolutions adopted at the Annual Shareholders' Meeting held on April 13, 2011 at the proposal of the Board of Directors of Red Eléctrica de Corporación, S.A.

#### 15. Initial public offerings and sale of notes and other instruments

On April 14, 2011, it was communicated to the CNMV that Red Eléctrica Corporación, S.A., through its subsidiary Red Eléctrica Financiaciones, S.A. Sole-Shareholder Company, had made a three hundred (300) million euro issue of notes on the euromarket.

**16. Interim financial information**

The Company sent information on the results for the first quarter of 2011 on May 4, 2011.

**17. Information on results**

The Company sent information on the results for the first quarter of 2011 on May 4, 2011.

**18. Information on corporate governance**

On July 11, 2011, Red Eléctrica Corporación, S.A. communicated that the Board of Directors of the Company, at a meeting held on June 30, 2011, had resolved to amend the Internal Code of Conduct on the Securities Market approved on June 25, 2009.

**19. Loans, credit facilities and guarantees**

On July 14, 2011, the Company communicated that Red Eléctrica de España, S.A. Sole-Shareholder Company had entered into a credit line agreement for €600 million and for a term of 5 years, to be used to cover the maturity of the syndicated loan in July 2012.

**20. Information on results**

On July 28, 2011, Red Eléctrica Corporación, S.A. posted the results for the first half of 2011.

**21. Interim financial information**

On July 28, 2011, the Company reported its results for the first half of 2011.

**22. Composition of other management and control bodies**

On July 29, 2011, the Company communicated the renewal of the committees of the Board of Directors.

**23. Information on corporate governance**

On August 5, 2011, the Company reported the acquisition of shares of the Company by a member of the Board of Directors.

**24. Credit ratings**

On August 16, 2011, it was communicated that Standard & Poor's had affirmed the credit ratings of Red Eléctrica Corporación, S.A. and its subsidiary Red Eléctrica de España, S.A. Sole-Shareholder Company at AA- in the long term and at A-1+ in the short term and revised upwards the outlook on them to stable.

**25. Credit ratings**

On October 24, 2011, it was communicated that Moody's was maintaining the rating of Red Eléctrica at A2 and the outlook at negative and Standard & Poor's was maintaining the rating at AA- and the outlook at negative.

**26. Interim financial information**

The Company reported its results for the third quarter of 2011 on October 28, 2011.

**27. Information on results**

On October 28, 2011, the Company published the report on its results for the first nine months of 2011.

**28. Information on dividends**

On December 22, 2011, the CNMV was informed that the Board of Directors of Red Eléctrica Corporación, S.A., at a meeting held on December 22, 2011, had resolved to distribute an interim dividend for 2011 in the gross amount of €0.676400 per share, which represents an increase of 15.0% with respect to the interim dividend for 2010.

## Chapter IV. Annual Reports on Board Committee Activities

The 2011 Annual Reports on the Activities of the Corporate Responsibility and Governance Committee and of the Audit Committee are reproduced in full below.

### Report on the Activities of the Corporate Responsibility and Governance Committee in 2011

#### 1. Introduction

The Committee's Action Plan for 2012, as provided in Article 16.6 a) of the Board Regulations, provides for the preparation of an annual report on the activities carried on, to be incorporated in the Annual Corporate Governance Report.

#### 2. Structure, composition and functions

##### 2.1. Structure

Article 24.2 of the Corporate Bylaws and Articles 15 and 16 of the Board Regulations govern the structure, composition and functions of the Corporate Responsibility and Governance Committee.

The Committee is assigned powers regarding the appointment and removal of Directors and senior executives, their compensation, compliance with Director duties and observance of corporate governance principles and rules. Article 16.5 of the Board Regulations approved on January 28, 2010 has attributed new corporate responsibility functions to the Committee.

The Committee meets as often as is appropriate for the sound performance of its functions. In any event, the Committee must meet at least once every quarter, whenever called by its Chairman or so requested by two of its members, and whenever the Board of Directors or its Chairman requests that a report be issued or proposals be adopted.

Article 15.5 of the Regulations of the Board of Directors provides that meetings may be called, and the associated documentation sent, by telematic means that guarantee due security and confidentiality for the call notice and the related documentation.

The call notice, including the agenda, will be sent by the Committee Chairman or Secretary to each of its members at least three days in advance of the date scheduled for the meeting, unless the meeting needs to be called sooner for reasons of urgency.

Article 15.5 of the Board Regulations allows Committee meetings to be held for reasons of urgency and on an exceptional basis by conference call, videoconferencing or any other remote means of communication that enables them to be held, provided that all Committee members agree to it.

The Committee may be constituted with the attendance of the majority of its members and adopt decisions or recommendations by a majority vote, which decisions or recommendations must be recorded

in the Minutes at the end of the meeting. In order to better perform its duties, the Committee may propose to the Board of Directors that advice be sought from independent professionals and may access any type of Company information or documentation that it may require to perform its functions.

Article 15 of the Board Regulations provides that the Corporate Responsibility and Governance Committee will be comprised of a minimum of three and a maximum of five members, as determined by the Board, with a majority of External Directors and at least half of its members must be Independent Directors. The Chairman of the Committee will be an Independent Director elected by its members and the Committee Secretary is the Secretary of the Board of Directors.

Committee members are appointed and removed by the Board of Directors at the proposal of the Board Chairman. Committee members hold office for a period of three years, may be reappointed and stand down when they cease to be Directors or when so resolved by the Board of Directors, subject to a report by the Appointments, Compensation and Corporate Governance Committee. The Chairman is appointed by the Committee for a period of three years and may be reappointed after one year has elapsed since he vacated office.

## 2.2. Composition

At 2011 year-end and on the date of approval of this Report, the Corporate Responsibility and Governance Committee was composed of four Directors: three external directors and one executive director. Of the external directors, two are independent directors and one is a nominee director.

At its meeting of July 27, 2011, the Board of Directors, following a report from the Corporate Responsibility and Governance Committee and at the proposal of the Board of Directors, approved the reappointment of two of its directors as board members (Mr. Luis M<sup>a</sup> Atienza Serna and Mr. Manuel Alves Torres) for a term of 3 years.

At 2011 year-end and on the date of approval of this Report, the composition of the Committee was as follows:

Director	Position	Type of Director
Antonio Garamendi Lecanda	Chairman	External Independent
María Ángeles Amador Millán	Member	External Independent
Luis María Atienza Serna	Member	Executive
Manuel Alves Torres	Member	External Nominee

The Executive Director and Chairman of the Company, Mr. Luis Maria Atienza Serna, is a member of the Committee by unanimous decision of the Board of Directors, which considers his presence on the Committee to be of special interest, without prejudice to his abstaining or absenting himself during discussion of any matters that could affect him personally or give rise to a conflict of interest.

The independent directors have a voting majority on the Corporate Responsibility and Governance Committee, since in the hypothetical event of a tie between independent and other directors, the chairman, who must be an Independent Director, has a casting vote.

Mr. Antonio Garamendi Lecanda has completed the maximum term of 12 years as an independent director of RED ELÉCTRICA. As established in Article 7.2 c) of the Board Regulations, and in the UNIFIED GOOD

GOVERNANCE CODE and in the international corporate governance best practices, this is the maximum term for being considered an independent director. Accordingly, if his reappointment is proposed at the next Annual Shareholders' Meeting, he will be classified under the "other external directors" category.

If the Annual Shareholders' Meeting approves the appointment and reclassification of Mr. Garamendi as director of the Company, he should be immediately replaced as chairman of the Corporate Responsibility and Governance Committee, since this office must be held by an independent director, as established in the Corporate Bylaws and the Board Regulations.

### 2.3. Functions

Pursuant to Article 24 of the Corporate Bylaws, the basic responsibilities of the Corporate Responsibility and Governance Committee are as follows:

- a) To report on (and, in the case of Independent Directors, make) any proposals to be submitted by the Board of Directors to the Shareholders' Meeting for the appointment or removal of Directors, including in cases of co-optation.
- b) To propose the compensation policy for Directors and senior executives to the Board of Directors and ensure its observance.
- c) To assume such reporting, supervising and proposing functions in the area of corporate governance as may be determined by the Board of Directors, as long as no ad hoc Committee has been set up for those functions.

The above basic responsibilities are detailed in Article 16 of the Board Regulations, which establishes the following:

#### 16.1 In relation to appointments, performance and removals:

- a) To report in advance on (and, in the case of Independent Directors, make) any proposals to be submitted by the Board of Directors to the Shareholders' Meeting for the appointment or removal of Directors, including in cases of co-optation.
- b) To report, prior to their submission to the Board of Directors, on proposals for the appointment or removal of the Secretary and the Deputy Secretary of the Board of Directors.
- c) To propose the system for selecting Independent Directors to the Board of Directors.
- d) To ensure that the candidates for filling a vacant directorship meet all of the requirements imposed in the legal provisions and in these Regulations.
- e) To evaluate the skills, knowledge and experience required on the Board and consequently define the functions and skills required of the candidates for each vacancy.
- f) To evaluate the time and dedication necessary for Directors to be able to perform their duties with due quality and efficiency, evaluating for these purposes whether their position as a Director is compatible with membership on other management bodies of companies.
- g) To report on such appointments and removals of senior executives of the Company and of Red

Eléctrica de España, S.A. Sole-Shareholder Company as the Chairman may propose to the Board of Directors.

- h)** To examine or organize, in the manner deemed appropriate, the process for succession of the Chairman and, as appropriate, to make proposals to the Board so the handover takes place in a planned and orderly fashion.
- i)** To ensure that gender diversity is taken into account when filling vacancies.
- j)** To consult with the Chairman, particularly when dealing with matters relating to Executive Directors.

#### 16.2 In Relation to compensation

- a)** To propose to the Board:
  - The compensation policy for the Directors and senior executives of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company;
  - The individual compensation and other contractual conditions of Executive Directors;
  - The basic terms and conditions of the contracts of senior executives of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company.
- b)** To consult with the Chairman of the Company, particularly when dealing with matters relating to Executive Directors and senior executives of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company.
- c)** To ensure compliance with the compensation policy established by the Company.

#### 16.3 In relation to fulfillment of Directors' duties:

- a)** To ensure the fulfillment by the Directors of the obligations established in these Regulations, to report to the Board on their fulfillment, and to issue the relevant reports and proposals and, as applicable, on the measures to be adopted in the event of breach.
- b)** To authorize Directors to use corporate assets.

#### 16.4 In relation to corporate governance rules:

- a)** To supervise compliance with the corporate governance rules, making proposals for improvement to the Board of Directors, and to receive information in this respect and, as appropriate, issue an annual report on the measures to be implemented and submit it to the Board.
- b)** To refer to the Board of Directors the proposals of the Audit Committee on the amendment of the Internal Code of Conduct on the Securities Markets.

#### 16.5 In relation to corporate responsibility policy:

- a)** To propose and promote the Company's policy on corporate responsibility.
- b)** To report on and supervise corporate responsibility initiatives and proposals made or decided on by the organizational units responsible, and, as appropriate, refer the relevant report or proposal to the Board of Directors.
- c)** To annually prepare a report on corporate responsibility policy.

#### 16.6 Other functions:

- a)** To keep the Board informed of its activities and to prepare an annual report to be included in the Annual Corporate Governance Report and an Action Plan for each year.
- b)** To propose and report on any other matter related to the foregoing that may be requested by

the Chairman or by the Board of Directors.

- c) To report to the Board on the performance of their duties by the Chairman and the plenary session of the Board.
- d) To verify the type of each Director for the purposes of the pertinent explanations by the Board to the Shareholders' Meeting that is to make or ratify the Director's appointment, and for the recording of the appointment in the Annual Corporate Governance Report.
- e) Any other powers attributed to it by the Board.

### 3. Activities carried on in 2011

Of the eleven (11) Corporate Responsibility and Governance Committee meetings held in 2011, no Directors failed to attend.

The Board of Directors was advised on a timely basis of the matters considered at each Committee meeting and copies of the Minutes of those meetings were sent immediately to the Directors.

The most significant steps taken by the Corporate Responsibility and Governance Committee in 2011 were:

#### 3.1. In Relation to appointments, removals and reappointments

- ◆ Monitoring of the process of appointing/reappointing directors and preparing reports and proposals for the Board of Directors. In particular, the Committee has provided favorable reports to the Board of Directors on the following proposals from the chairman of the Board of Directors:
  - To reappoint Ms. Arantza Mendizábal Gorostiaga as a member of the Audit Committee, to discharge her office for a term of three years.
  - To reappoint Ms. María Jesús Álvarez González as a member of the Audit Committee, to discharge her office for a term of three years.
  - To appoint Mr. José Folgado Blanco as a member of the Audit Committee, to discharge his office for a term of three years.
  - To reappoint Mr. Luis M<sup>a</sup> Atienza Serna as a member of the Corporate Responsibility and Governance Committee, to discharge his office for a term of three years.
  - To reappoint Mr. Manuel Alves Torres as a member of the Corporate Responsibility and Governance Committee, to discharge his office for a term of three years.
- ◆ Analysis of the compatibility of the office of director in another company on the part of an independent director.

#### 3.2. In Relation to compensation

- ◆ Analysis of the findings of the 2010 executive team evaluation process.
- ◆ Approval of the proposed Business, Managerial and Management Committee objectives for 2011.
- ◆ Analysis of the proposed grant of extraordinary bonuses.
- ◆ Approval of the proposed 2011 compensation policy for the executives of Red Eléctrica Corporación, S.A., Red Eléctrica de España, S.A. Sole-Shareholder Company and of Red Eléctrica Internacional, S.A. Sole-Shareholder Company.



- ◆ Evaluation of the level of achievement of the 2010 Business, Managerial and Management Committee objectives.
- ◆ Review and monitoring (quarterly) of the level of achievement of the Business, Managerial and Management Committee objectives for 2011.
- ◆ Review and monitoring of long-term objectives relating to 2009-2013.
- ◆ Analysis and review of proposals relating to compensation for the Board of Directors and to the Board's Compensation Policy Report, for fiscal year 2010, which the Board submits to the Annual Shareholders' Meeting.
- ◆ Analysis of the proposal for the Annual Share Award Program for non-executive personnel, reporting favorably to the Board of Directors.
- ◆ Referral to the Board of Directors of the proposed compensation of the Board and its Committees for fiscal years 2011 and 2012.
- ◆ Review of compensation matters relating to Senior Management.

### 3.3. In Relation to corporate governance rules

- ◆ Approval of the Company's knowledge activities program for directors for 2011.
- ◆ Implementation over several months of the self-evaluation process for the Board of Directors, its Committees, and the Chairman of the Board of Directors and Chief Executive Officer, commenced at the beginning of 2011 which, by express decision of the Corporate Responsibility and Governance Committee, is being carried out with the support of external advisers with expertise in the area (KPMG), which provides the process with a more objective and independent external viewpoint.
- ◆ Preparation of the proposed 2010 Annual Corporate Governance Report, for referral to the Board of Directors.
- ◆ Preparation of the proposed Annual Gender Diversity Report for referral to the Board of Directors.
- ◆ Analysis and assessment of the Company's Equality Policy.
- ◆ Preparation of the procedure for electronic voting at the 2010 Annual Shareholders' Meeting, for approval by the Board of Directors.
- ◆ Preparation of the operating rules for the Shareholders' Electronic Forum, for approval by the Board of Directors.
- ◆ Review of the contents of the call notice and agenda for the Annual Shareholders' Meeting, and issue of a favorable report on the following sections relating to the call notice for the Annual Shareholders' Meeting:
  - Proposed amendment of the Bylaws and of the Shareholders' Meeting Regulations for their adaptation to the current legislation.
  - Proposed authorization from the Shareholders' Meeting to the Board for the derivative acquisition of treasury stock.
  - Proposed compensation of the Board of Directors and the report on the compensation policy for the Board of Directors, for fiscal year 2010.

- ◆ Review and approval of the Annual Report on the Monitoring of and Compliance with the Code of Ethics, presented by the Ethics Manager.
- ◆ Review of the proposed update to the Internal Code of Conduct on the Securities Market, for its adaptation to the Group's new corporate structure. The Committee has reported favorably on this proposal, for its approval by the Board of Directors.
- ◆ Review and preparation of the proposed amendment to the Board Regulations, to be submitted for approval by the Board of Directors, following the necessary technical adjustments, once the regulations implementing the Annual Corporate Governance Report and the new Annual Report on Directors' Compensation are published.
- ◆ Analysis and approval of the outline for the new design of the Annual Corporate Governance Report for fiscal year 2011, which takes into account the main new provisions established by Article 61 bis of the Sustainable Economy Law.
- ◆ Preparation and approval of the proposed Company Chairman Succession Plan.
- ◆ Approval of the proposed Criminal Risk Prevention Program for the companies of the Red Eléctrica Group, following the changes introduced by Organic Law 5/2010, of June 22, 2010, amending the Criminal Code.
- ◆ Approval of the Company's knowledge activities program for directors for fiscal year 2012.

### 3.4. In Relation to corporate responsibility policy

- ◆ Analysis of the Annual Report on Corporate Responsibility Policy.
- ◆ Analysis and monitoring of the external awards and recognition obtained by the Company in the area of corporate responsibility.

### 3.5. Other steps

- ◆ Approval of the Annual Report on the Committee's activities in 2010, for incorporation into the Annual Corporate Governance Report.
- ◆ Approval of the Committee's Action Plan for 2012.
- ◆ Approval of the meeting schedule for 2012.

## 4. Attendance by Directors at Meetings

Of the eleven (11) meetings held, no Directors were absent and no proxies were granted by Directors.

## Report on the Activities of the Audit Committee in 2011

### 1. Introduction

The Audit Committee Action Plan for 2012 envisages the preparation, in the first quarter of the year, of a report on the Committee's activities in 2011, to be included in the Annual Corporate Governance Report of the Company, which constitutes the purpose of this document.

### 2. Structure, composition and functions

#### 2.1. Structure and Composition

The Audit Committee is comprised of three members, pursuant to Article 23 of the Corporate Bylaws and Article 13 of the Board Regulations, from between a minimum of three and a maximum of five members, all of whom are External Directors and are appointed for a period of three years.

The Chairman of the Committee is elected by its members from among the Independent Directors who sit on the Committee, and the Committee Secretary is the Secretary of the Board of Directors.

Throughout 2011, the Committee was comprised of External Directors, with a majority of Independent Directors.

At its meeting of July 27, 2011, the Board of Directors, following a report from the Corporate Responsibility and Governance Committee, approved the reappointment for a term of 3 years of two of its directors as board members (Ms. Arantza Mendizábal Gorostiaga and Ms. María Jesús Álvarez González) and appointed Mr. José Folgado Blanco as a new board member for a term of 3 years following the expiration of the term for which Mr. Francisco Javier Salas Collantes had been appointed.

The composition of the Audit Committee at December 31, 2011 was as follows:

Director	Position
Arantza Mendizábal Gorostiaga (independent director)	Chairwoman
María Jesús Álvarez González (nominee director)	Member
José Folgado Blanco (independent director)	Member
Rafael García de Diego Barber	Non-Director Secretary

The Directors on the Committee are particularly qualified to hold their positions, with broad professional experience, having held positions of the highest responsibility outside the RED ELÉCTRICA Group, in functions related to those entrusted to the Committee. Particularly notable is their appropriate grounding in economic, financial and accounting matters.

Set out below are brief summaries of the professional careers of its members:

- ◆ Ms. Arantza Mendizábal Gorostiaga holds a Doctorate in Economics and is Professor of Applied Economics at the Faculty of Economics of Universidad del País Vasco. She has been a distinguished researcher in the areas of industrial and technological policy, an MP member of the Economy and Finance Committee, the Budget Committee and Spokeswoman for the Industry, Trade and Tourism Committee of the Lower House of Parliament. In addition to her duties as Professor, she is currently the Director of the European Documentation Center of Universidad del País Vasco. She was appointed Chairwoman of the Audit Committee on July 20, 2009, for a period of three years.
- ◆ Ms. María Jesús Álvarez González holds a degree in Law and Economics and Business Administration. She has held various executive positions within SEPI and engaged in various activities in the banking and industrial sectors. In addition, she has been a member of the Boards of Directors of Enusa Industrias Avanzadas, S.A., Equipos Nucleares, S.A., Clínica Castelló, S.A., Indra Sistemas, S.A., Infoinvest, S.A., Infoleasing, S.A., Empresa Nacional de Residuos Radioactivos, S.A. (ENRESA), Aluminio Español, S.A., and Agencia Efe, S.A. She is currently the Economic-Finance Director of Sociedad Estatal de Participaciones Industriales (SEPI), member of the Management Committee of SEPI, and member of the Board of Trustees of the SEPI Foundation and of the SEPI Labor Foundation.
- ◆ Mr. José Folgado Blanco holds an Economics Degree, with honors, and a Doctorate in Economics from the Universidad Autónoma de Madrid. He has been the Director of the Economics Department of the CEOE, Member of the Economic and Social Council on behalf of the Business Organizations, Secretary of State of Budgets and Expenditure. Ministry of Economy and Finance, since May 1996, Secretary of State for the Economy, Energy and Small and Medium-sized Enterprises of the Ministry of Economy, since April 2000, Secretary of State of Energy, Industrial Development and of Small and Medium-sized Enterprises of the Ministry of Economy, since July 2002, MP of the province of Zamora in the Lower House of Parliament and Deputy Chairman of the Economics and Finance Committee, since March 2004. He is currently a Professor of Public Finance and Tax Systems at the Universidad Autónoma de Madrid on leave, Mayor of Tres Cantos (Madrid) since June 2007 and member of the Social Council of the Universidad Autónoma de Madrid.

The Committee Secretary is Mr. Rafael García de Diego Barber, the Secretary of the Board of Directors and the Head of the Company's Legal Department.

Mr. Luis Villafruela Arranz, Director of Regulation, and Ms. Esther Rituerto Martínez, the Director-General of Administration and Finance, also regularly attended Committee meetings to report on various matters falling within their areas of responsibility.

The meeting of February 2011, at which the financial statements of the Company and of its Group for fiscal year 2010 were reviewed, was attended by the external auditor of the Company and its Group for such fiscal year, PriceWaterhouseCoopers, which explained, as is customary, the philosophy and processes of the audit performed on the Group's companies. The Committee resolved to provide the Board with a favorable report on the presentation of the 2010 financial statements.

The Shareholders' Meeting of April 13, 2011, approved an amendment of the Corporate Bylaws to adapt them, among other rules, to the new legal requirements established in Law 12/2010, of June 30, 2010, which basically affect the composition, structure and functions of the Audit Committee. The purpose of the amendment has been to make certain technical adjustments to the Bylaws but without essentially affecting the composition or essence of the functions already attributed to the Audit Committee of the Company.

In particular, with respect to the composition of the Committee, the formal bylaw obligation has been established of having, at least, one independent director appointed taking into account his/her skills and experience in the areas of accounting, audits or both (although the Bylaws already contained the obligation that the chairman of the Audit Committee be an independent director; and the Board Regulations already expressly provided that when appointing all the members of the Committee, account would be taken of their skills and experience in the areas of accounting, audits or risk management).

## 2.2. Functions

Under Article 23 of the Corporate Bylaws and Article 14 of the Board Regulations, the functions of the Audit Committee include the provision of support to the Board of Directors in its function of supervision of the process of preparing economic and financial information, the internal control of the Company, the independence of the external auditor, compliance with statutory provisions and internal regulations, provisions relating to the Company's shareholders and any powers expressly attributed to it by the Board of Directors.

The above-mentioned amendment of the Bylaws approved by the Annual Shareholders' Meeting held in 2011 has also to a certain degree affected the functions of the Committee, adapting them to the strict wording of the new legislation; these functions have not changed in essence with respect to the functions established and implemented in the Board Regulations.

Accordingly, the new powers of the Audit Committee formally incorporated into the Bylaws include the following:

- ◆ To supervise the efficacy of the Company's internal control, any internal audit, and risk management systems, as well as discuss with the auditors any significant weaknesses of the internal control system detected in the course of the audit.
- ◆ To supervise the process of preparing and filing regulated financial information.
- ◆ To receive each year from the auditors written confirmation of their independence from the Company or from entities related to the Company directly or indirectly, as well as information on additional services of any kind provided to such entities by those auditors or by persons or entities related to those auditors in accordance with the provisions of the legislation in force.
- ◆ To issue, before the auditors' report is issued, a report each year expressing an opinion on the independence of the auditors or audit firms.

Among the powers that the Board Regulations attribute to the Audit Committee, the following, divided into groups, stand out:

1. In relation to economic and financial information, responsibility for supervising the process of preparation and integrity of the financial information of the Company and, where appropriate, its Group, ensuring that legislative requirements are taken into account, the consolidated group is adequately defined, and the applicable accounting principles and methods are correctly applied.

In addition, the need to review and report to the Board in advance on economic and financial information that the Company must disclose and send to the market supervisory bodies has been established. Following the recommendations of the Unified Good Governance Code, the Committee must ensure that any interim financial statements are prepared using the same accounting methods as annual financial statements and, where it sees fit, it may ask the external auditor to conduct a limited review.

2. In relation to internal control and risk management systems, the internal audit function has been given responsibility for ensuring the sound functioning of the internal reporting and control systems; the Audit Committee has been assigned the functions of monitoring the independence and efficacy of the internal audit function; supervising and controlling the process of selection, appointment, reappointment and removal of the head of the internal audit function, as well as its action plans; supervising and controlling the resources allocated to the internal audit function, including its budget; receiving periodic information on its activities; and verifying that senior management of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company is acting on the conclusions and recommendations in its reports.

The head of internal audit must present an annual work program to the Committee, directly report on any incidents arising during its implementation and submit an activities report at the end of each year.

In addition, following the recommendations of the Unified Good Governance Code, the Committee must periodically supervise the internal control and risk management systems, so that the principal risks are adequately identified, managed and disclosed; and must also supervise the procedure established by the Board to enable employees to communicate any potentially significant irregularities, particularly financial and accounting irregularities, that they may detect at the Company.

3. In relation to the external auditor, particularly noteworthy is the responsibility for ensuring that the Company discloses any change of auditor to the CNMV as a material event and, if applicable, any disagreements with the outgoing auditor, and also for ensuring that the Company, within the scope of its responsibilities, complies with current rules regarding the provision of non-audit services, limits on concentration of the auditor's business and, in general, any other rules established to safeguard the independence of auditors. In the event of resignation of the external auditor, it must review the underlying circumstances, and verify that senior management of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company is acting on the recommendations of the external auditor.
4. In relation to compliance with legal provisions and internal regulations, the Regulations establish the obligation on the Audit Committee to supervise compliance with the Internal Code of Conduct on the Securities Market and with the functions of the Oversight Body provided in that Code, periodically informing the Corporate Responsibility and Governance Committee of the degree of compliance with the Code and of any incidents that occur; to annually evaluate compliance with the rules of the Internal Code of Conduct on the Securities Market, and review compliance with the actions and measures resulting from reports or inspections by the supervisory and control authorities of the securities market.
5. In relation to the Company's shareholders, the Committee is responsible for entertaining and, if applicable, responding to any initiatives, suggestions or complaints raised by the shareholders within the scope of its jurisdiction and for reporting to the Shareholders' Meeting, as applicable, on any issues falling within its jurisdiction that are raised by shareholders.
6. The Other Responsibilities section provides for the Committee's duty to report to the Board on any related-party transactions proposed that require the Board's authorization and, in the event they take place, informing the Board in relation to transactions creating or acquiring interests in special-purpose vehicles or entities domiciled in countries or territories that are considered tax havens, and also on any transactions and operations that could impair the Group's transparency.

The principal activities undertaken by the Audit Committee in 2011, based on the above areas of responsibility, are described below.

### 3. Activities carried on in 2011

The Audit Committee has pursued its activities in accordance with the Annual Plan, approved by the Committee on December 13, 2010, in light of the responsibilities assigned to it in the Corporate Bylaws and the Board Regulations. This plan served as a guide for the preparation of the corresponding schedule of Committee meetings.

In addition, the Audit Committee reported on its activities to the Board of Directors at the Board meetings immediately following each Committee meeting, and provided the Directors with copies of the Minutes of its meetings.

The Audit Committee met ten (10) times in 2011, and reported ten times to the Board on its activities.

In 2011, the Audit Committee performed the following main tasks:

#### 3.1. In relation to economic and financial information

- ◆ Analysis of the projected results for the Red Eléctrica Group, and of the criteria being used for the 2010 year-end.
- ◆ Review of the 2010 Financial Statements of the Company and its Consolidated Group and review of the External Auditor's Report.
- ◆ Analysis of the proposed appropriation of income and distribution of dividends by Red Eléctrica Corporación, S.A., and issue of a favorable report.
- ◆ Supervision of the sections of the 2010 Annual Corporate Governance Report, within the scope of the Committee's jurisdiction.
- ◆ Follow-up on quarterly treasury stock reports.
- ◆ Analysis and review of certain financing conditions relating to the transmission assets acquired in 2010 and referral of the report to the Board of Directors.
- ◆ Analysis of proposed financing granted by the European Investment Bank to the French-Spanish venture known as INELFE, for the Spain-France electrical interconnection and favorable report to the Board.
- ◆ Analysis of the proposal, to be submitted to the Board of Directors, for the grant of powers related to the formalization of loans or credit facilities between Group companies.
- ◆ Analysis of the proposed renewal of the EMTN program, due to expiration of the annual program. Issue of favorable report submitted to the Board of Directors.
- ◆ Review of the financial information to the supervisory bodies of the markets relating to the first and third quarters and to the first half of 2011.
- ◆ Analysis of the proposal and issue of favorable report on a long-term financing arrangement.
- ◆ Analysis of the Financial Statements as of June 30, 2011.

- ◆ Analysis of the report on Red Eléctrica Group inter-company transactions performed in 2010.
- ◆ Favorable report on financing to the Peruvian company of the Group, TESUR, for construction of an electrical line in Peru.
- ◆ Analysis of the report on the formalization of a syndicated loan.
- ◆ Analysis of the report on the trend in the credit rating of Red Eléctrica and the rating granted by the rating agencies.
- ◆ Analysis of the 2011 year-end schedule of the Red Eléctrica Group.
- ◆ Analysis of the Company's 2012-2016 Strategic Plan.
- ◆ Examination of the content and scope of the 2012-2016 Investment Plan and favorable report to the Board of Directors.
- ◆ Analysis of the 2012 Budget of the companies of the Red Eléctrica Group and favorable report to the Board of Directors.
- ◆ Analysis of the proposed distribution of a 2011 interim dividend and referral of a favorable report to the Board.
- ◆ Analysis of the communication of results to the CNMV.

### 3.2. In relation to internal control and risk management systems

- ◆ Analysis of the audit report on the Financial Reporting Internal Control System (SOX) carried out by a specialized external auditor.
- ◆ Analysis of the half-yearly Integral Risk Management Report.
- ◆ Analysis of the administrative and accounting Internal Control Report issued by PricewaterhouseCoopers Auditores, S.L. for the financial statements of the Red Eléctrica Group as of December 31, 2010.

### 3.3. In relation to the internal audit function

- ◆ Supervision and control of the means and resources assigned to the Internal Audit function for fiscal year 2011.
- ◆ Analysis of the periodic report on the prevention of occupational risks in 2011.
- ◆ Analysis of the report on internal audits conducted in 2010.
- ◆ Quarterly review of the report verifying compliance with the recommendations under the reports from the Internal Audit service.
- ◆ Analysis of the report on the quality of the Internal Audit Service at Red Eléctrica, prepared by the Internal Audit Institute of Spain.
- ◆ Analysis and approval of the proposed update of the Internal Audit Charter, which is based on the experience gained since the approval of the first charter, in June 2008, and of the recommendations for improvement made by the Internal Auditors Institute following the evaluation of the quality of the Internal Audit and Risk Management Department performed in May 2011.
- ◆ Analysis and approval of the 2012 Internal Audit Plan.



### 3.4. In relation to external auditors

- ◆ Analysis of the report on the independence of the external auditor issued by the latter.
- ◆ Analysis of the proposed appointment of external auditors of the companies of the Group and referral to the Board of same.
- ◆ Analysis of the report from the external auditor, which presents an unqualified opinion, on the consolidated financial statements for the first half of 2011.
- ◆ Analysis of the 2011 preliminary external auditors' report prepared by PricewaterhouseCoopers.

### 3.5. In relation to compliance with legal provisions and internal regulations

- ◆ Analysis of the half-yearly follow-up report on the internal rules of the Company.
- ◆ Analysis of the annual report evaluating compliance with the Internal Code of Conduct on the Securities Market.
- ◆ Analysis of the proposal and favorable report to the Board, in relation to the update of the Internal Code of Conduct on the Securities Market to adapt it to the Group's new corporate structure.
- ◆ Analysis of the report on the status and follow-up of the Company's Rules and Procedures.
- ◆ Analysis of the report on tax implications for Red Eléctrica of Royal Decree-Law 9/2011 on measures aimed at improving the quality and cohesion of the national health system, contributing to tax consolidation, and increasing the maximum amount of State guarantees for 2011.
- ◆ Analysis of the annual follow-up report on compliance with the Code of Ethics of Red Eléctrica.

### 3.6. In relation to the company's shareholders

- ◆ Analysis of the resolutions proposed by the Board to the Shareholders' Meeting in the areas falling within the Committee's jurisdiction, and of the resolution to call a Shareholders' Meeting.
- ◆ Follow-up of any initiatives, suggestions and complaints made by the shareholders during the year.
- ◆ Presence of the Chairwoman of the Audit Committee at the Annual Shareholders' Meeting of the Company, in order to respond in person to any questions raised by shareholders.

### 3.7. Other activities

- ◆ Approval of the 2010 Annual Report on the Activities of the Audit Committee, to be incorporated into the Annual Corporate Governance Report.
- ◆ Analysis of the report on the renewal of the Red Eléctrica Corporate Insurance Program and approval of such Program.
- ◆ Analysis of quarterly information on transactions with related parties.
- ◆ Analysis of the proposed acquisition of shares in the capital stock of the Portuguese company OMIP and of the Spanish company OMEL and favorable report to the Board.
- ◆ Analysis of the report on the supplementary agreements relating to the purchase of transmission assets from Endesa in 2010.

- ◆ Analysis of the authorization for recurring related-party transactions for fiscal year 2012.
- ◆ Approval of the Committee's Action Plan for 2012.
- ◆ Approval of the 2012 meeting schedule.

#### 4. Director Attendance at Meetings

Of the ten (10) meetings held in 2011, no Directors were absent and no proxies were granted by Directors.

#### 5. Review of the 2011 Financial Statements

At the meeting approving the report on the activities of the Audit Committee in 2011, and in relation to the 2011 fiscal year, the Audit Committee:

- ◆ Reviewed the 2011 Financial Statements of the Company and of its Consolidated Group and the External Auditor's Report.
- ◆ Analyzed the proposed appropriation of income and distribution of dividends by Red Eléctrica Corporación, S.A. for fiscal year 2011.

In both cases, the Committee reported favorably on these proposals.

A large, stylized number '4' in a brown, hand-drawn font, centered within a thin brown rectangular border.

## OFFICIAL ANNEXES

## Annex 1

ANNUAL CORPORATE GOVERNANCE REPORT FOR RED ELÉCTRICA CORPORACIÓN S.A.  
FOR THE 2011 FISCAL YEAR, IN ACCORDANCE WITH CIRCULAR 4/2007, OF DECEMBER  
27, 2007, OF THE SPANISH NATIONAL SECURITIES MARKET COMMISSION (CNMV)<sup>(2)</sup>

# ANNUAL CORPORATE GOVERNANCE REPORT

## FISCAL YEAR 2011

PARTICULARS OF ISSUER  
C.I.F. A-78003662

Company Name:  
RED ELÉCTRICA CORPORACIÓN, S.A.

Registered Office:  
Pº Conde de los Gaitanes, 177  
La Moraleja – Alcobendas  
28109 MADRID

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<sup>(2)</sup> Unless another date is expressly indicated in this report, its contents are deemed to refer to December 31, 2011.

## A Ownership Structure

**A.1.** Complete the following table on the Company's capital:

Date of last change	Capital (€)	Number of shares	Number of voting rights
05-17-1999	270.540.000	135.270.000	135.270.000

State whether there are multiple classes of shares with different related rights: YES  NO

Class	Number of shares	Par value per share	Number of voting rights per share	Other rights

All the shares belong to the same class and series and confer the same rights on their holders.

**A.2.** List the direct and indirect owners of significant holdings in the Company at year-end, excluding Directors:

Name of shareholder	Number of direct voting rights	Number of indirect voting rights <sup>(*)</sup>	% of total voting rights
State-owned Industrial Holdings Company (SEPI)	27,054,000	—	20 %
HSBC Holdings, PLC	—	4,381,395	3.239%
Talos Capital Limited	4,175,785	—	3.087%
The Children's Investment Fund Management (UK) LLP	—	4,175,785	3.087%
First Eagle Investment Management LLC	—	4,132,499	3.055 %
MFS Investment Management	—	4,120,324	3.046 %
Fidelity International Limited	—	1,358,111	1.004 %

<sup>(\*)</sup> Through:

Name of direct owner of holding	Number of direct voting rights	% of total voting rights

Indicate the most significant movements in the shareholder structure during the year:

Name of shareholder	Date of transaction	Description of transaction

**A.3.** Complete the following tables on the members of the Company's Board of Directors who own Company shares:

At December 31, 2011, the direct and indirect shareholdings of the Directors in RED ELÉCTRICA's capital, both in individual and aggregate terms, were as follows:

Name of Director	Number of direct voting rights	Number of indirect voting rights <sup>(*)</sup>	% of total voting rights
Luis M <sup>a</sup> Atienza Serna	24,390	—	0.01803
Antonio Garamendi Lecanda	6,710	—	0.00496
Manuel Alves Torres	510	—	0.00038
Miguel Boyer Salvador	0	—	—
Rafael Suñol Trepal	20	—	0.00001
M <sup>a</sup> Ángeles Amador Millán	0	—	—
Francisco Javier Salas Collantes	20	—	0.00001
José Folgado Blanco	0	—	—
Arantza Mendizábal Gorostiaga	0	—	—
M <sup>a</sup> Jesús Álvarez González	0	—	—
Rui Manuel Janes Cartaxo	0	—	—

<sup>(\*)</sup> Through:

Name of direct owner of holding	Number of direct voting rights	% of total voting rights
<b>% total of voting rights in possession of the Board of Directors</b>		
	0.02339	

Complete the following tables on the members of the Company's Board of Directors who hold Company share options:

Name of Director	Number of direct options	Number of indirect options	Equivalent number of shares	% of total voting rights

**A.4.** Give details of any relationships of a family, commercial, contractual or corporate nature existing between the owners of significant holdings, insofar as they are known to the Company, unless they have scant relevance or arise from the ordinary course of business:

Names of related parties	Type of relationship	Brief description

**A.5.** Give details of any relationships of a commercial, contractual or corporate nature existing between the owners of significant holdings and the Company, unless they have scant relevance or arise from the ordinary course of business:

Names of related parties	Type of relationship	Brief description

The significant shareholder of the Company, SEPI, does not have any relationship with the Company and/or its Group that is material or falls outside the ordinary course of business of a contractual, corporate or commercial nature.

**A.6.** Indicate whether any side agreements affecting the Company have been disclosed to the Company as provided in Article 112 of the Securities Market Law. If so, provide a brief description and list the shareholders bound by the agreement:

YES  NO

Parties to side agreement	% of capital affected	Brief description of the agreement

At December 31, 2011, the Company had no record of any agreements or covenants between shareholders that require them to adopt a common policy through the concerted exercise of voting rights at Shareholders' Meetings, or which restrict or condition the unrestricted transfer of their shares.

State whether the Company is aware of the existence of concerted actions among its shareholders. If so, provide a brief description:

YES  NO

At 2011 year-end, there was no record at the Company of any agreements or accords between shareholders requiring the concerted exercise of their voting rights, or a common policy on the management of the Company, or having the aim of materially influencing the Company.

Parties involved in concerted action	% of capital affected	Brief description of the concerted action

Expressly state whether any of the above agreements or covenants or concerted actions have been amended or terminated during the year.

**A.7.** Indicate whether there is any individual or legal entity that exercises or may exercise control over the Company, in accordance with Article 4 of the Securities Market Law:

YES  NO

Name

#### Comments

SEPI was the direct owner, at 2011 year-end, of a significant interest in the Company, holding 27,054,000 shares that represent 20% of capital. All of the foregoing is for the purposes contemplated in Royal Decree 1362/2007 of October 19, 2007.

There are no individuals or legal entities that exercise or may exercise control over the Company, as provided in Article 4 of the Securities Market Law.

**A.8.** Complete the following tables on the Company's treasury stock:

At year-end:

Number of direct shares	Number of indirect shares <sup>(**)</sup>	Total % of capital
667,511	—	0.493%



(\*) Through:

Name of direct owner of holding	Number of direct shares
Total	—

Give details of any significant variations during the year, in accordance with Royal Decree 1362/2007:

Date of notice	Total shares acquired directly	Total shares acquired indirectly	Total % of capital
01/14/2011	1,356,827	—	1.003%
05/26/2011	1,357,715	—	1.004%
08/16/2011	1,420,221	—	1.049%
12/12/2011	1,356,920	—	1.003%

#### Gain/(Loss) on treasury stock disposed of during the period (€ Thousand)

762.3

**A.9.** State the conditions and term of the current authority conferred by the Shareholders' Meeting on the Board of Directors for acquisitions or transfers of treasury stock:

The Corporate Enterprises Law (LSC) has consolidated the legal regime applicable to the treasury stock of companies established in Law 3/2009, of April 3, 2009, on Structural Modifications to Commercial Companies, without introducing any material amendments to the regime.

In light of the foregoing, and although the authorization approved by the Shareholders' Meeting on May 20, 2010, in relation to the award of treasury shares, as compensation, to employees of the Company and of the RED ELÉCTRICA Group, was still in force, pursuant to the law, for another four years, it was submitted for approval by the Shareholders' Meeting held on April 13, 2011. It was intended that the shareholders renew the authorization granted last year, in accordance with the most recent corporate governance practices. As a separate item on the agenda, it was also intended to establish a Compensation Plan for members of Senior Management and the Executive Directors of Red Eléctrica Corporación, S.A., which may be extended to companies in its Consolidated Group, allowing part of their compensation to be awarded in the form of Company shares, on the same terms as last year and always within the maximum annual legal limit of €12,000 per participant, which enables certain tax advantages to be enjoyed (which are applied equally to all employees of the Company within their relevant Plan). This Plan requires a resolution with certain legally established conditions.

Accordingly, the Shareholders' Meeting of the Company held on April 13, 2011, gave an authorization to the Board of Directors, pursuant to the provisions of Article 146 and related provisions of the Corporate Enterprises

Law and other applicable legislation, for the derivative acquisition of treasury stock in Red Eléctrica Corporación, S.A. by the Company itself and by companies of the Red Eléctrica Group directly or indirectly and insofar as the Board of Directors considers that the circumstances so dictate, subject to the following conditions:

- ◆ The maximum number of shares to be acquired must not exceed the established legal limit, provided that the other applicable legal requirements can also be fulfilled.
- ◆ Acquisitions cannot be made for a consideration higher than the market value of the shares at the time of acquisition, or for a consideration lower than 50% of the market price at that time.
- ◆ The methods of acquisition may consist of sale and purchase, swap or any other type of transaction for consideration or for no consideration, as the circumstances so dictate. In the case of acquisition for no consideration, pursuant to the provisions of Article 146.4 of the Corporate Enterprises Law, the shares acquired may be partially paid-in.
- ◆ Pursuant to the provisions of Article 146.1 b) of the Corporate Enterprises Law, the acquisition, including any shares previously acquired by the Company and held as treasury stock, may not have the effect of leaving net worth below the amount of capital stock plus legal reserves or restricted reserves pursuant to the bylaws.

For these purposes, 'net worth' will be considered the amount classed as such pursuant to the criteria used to prepare the financial statements, reduced by the amount of income attributed directly to same and increased by the amount of uncalled subscribed capital stock, as well as by the nominal amount and the subscribed additional paid-in capital recorded for accounting purposes as shareholders' equity.

In accordance with paragraph three of Article 146.1 a) of the Corporate Enterprises Law, the Board of Directors of the Company may use some or all of the treasury stock acquired under this authorization and the treasury stock already owned by the Company on the date of approval of the resolution to implement compensation programs consisting of the direct award of shares to employees and Executive Directors of the Company and of the companies belonging to the RED ELÉCTRICA Group.

For all of the foregoing, an authorization as broad as may be necessary is granted to the Board of Directors to request all such authorizations and adopt all such resolutions as may be necessary or appropriate for compliance with the legislation in force, and the implementation and successful outcome of this resolution.

The term of this authorization will be five (5) years as from the date of this Shareholders' Meeting.

The Shareholders' Meeting expressly revoked and, therefore, rendered ineffective the authorization for the derivative acquisition of treasury stock given to the Board of Directors by the Shareholders' Meeting held on May 20, 2010.

**A.10.** Indicate, as appropriate, any statutory or bylaw restrictions on the exercise of voting rights, and any statutory restrictions on the acquisition or transfer of holdings in the capital:

State whether there are statutory restrictions on the exercise of voting rights: YES  NO

**Maximum percentage of voting rights that may be exercised by  
one shareholder due to special statutory restrictions (Electricity Industry Law)**

3 %  
1 % (electricity industry)

**Maximum percentage of voting rights that may  
be exercised by a shareholder due to bylaw restrictions**

3 %  
1 % (electricity industry)

State whether there are bylaw restrictions on the exercise of voting rights: YES  NO

**Description of the statutory and bylaw restrictions on the exercise of voting rights**

Each share gives the right to one vote and all shareholders are entitled to attend Shareholders' Meetings, without any required minimum number of shares, as was the case until the Special Shareholders' Meeting of July 17, 2003, which removed the bylaw requirement to hold at least 50 shares in order to attend Shareholders' Meetings.

Various amendments to Electricity Industry Law 54/1997 of November 27, 1997, affecting restrictions on voting rights were introduced with the entry into force of Law 17/2007 of July 4, 2007, amending Electricity Industry Law 54/1997 to adapt it to the provisions of Directive 2003/54/EC of the European Parliament and of the Council of June 26, 2003 concerning common rules for the internal market in electricity, a Community provision that has been superseded by Directive 2009/72/EC of July 13, 2009, which proclaims the mandatory independence of transmission companies and operators of European electricity systems.

Specifically, Subprovision Two of Additional Provision Three of Law 17/2007 established maximum limits on the exercise of voting rights, in order to guarantee the independence of a company engaging in regulated activities in the electricity industry which, as provided in Electricity Industry Law 54/1997 of November 27, 1997, constitute an essential service.

As a result, the Corporate Bylaws were adapted to such legislation. The literal wording of the Articles referring to restrictions on the exercise of voting rights is as follows:

*«Article 5.- Capital*

1. *The capital of the Company stands at two hundred and seventy million five hundred and forty thousand euros (€270,540,000), and is divided into one hundred and thirty-five million two hundred and seventy thousand (135,270,000) shares, of a single class and series, each with par value of two euros (€2), fully subscribed and paid in, and represented by book entries.*
2. *In accordance with the provisions of the Additional Provision Three of Law 17/2007 and the Electricity Industry Law:*
  1. *Unless otherwise permitted by law, the sum of the direct and indirect interests in the Company's capital held by any individual or legal entity may not at any time exceed five percent of the Company's capital. These shares may not be pooled for any purpose whatsoever. No shareholder may exercise more than three percent of voting rights. Parties that engage in activities in the electricity industry and those individuals or legal entities that directly or indirectly hold more than five percent of their capital, may not exercise more than one percent of voting rights. Furthermore, the sum of the direct or indirect interests held by parties that pursue activities in the electricity industry must not exceed forty percent.*
  2. *For the purposes of calculating the holding of each shareholder, a specific individual or legal entity shall be deemed to own, in addition to the shares and other securities owned or acquired by entities belonging to its group, as this term is defined in Article 4 of Securities Market Law 24/1988 of July 28, 1988, the shares or securities owned:*
    - a) *By persons acting in their own name but for the account of the former, on a concerted basis or as a part of a decision-making unit, the members of a legal entity's Board of Directors being deemed, unless proven otherwise, to act for the account of or on a concerted basis with such entity.*
    - b) *By shareholders with whom it exercises control over a controlled entity.*

*In any event, regard shall be had both to the nominee ownership of the shares and other securities and to the voting rights enjoyed by any means.*
3. *Without prejudice to the provisions of Article 6.2 of these Corporate Bylaws, the breach of the limits indicated in Article 5.2 or of those established at any time by the legislation in force shall entail the legal consequences specified therein, including, as*

the case may be, the imposition of the appropriate penalties and the provisions of these Bylaws.

The voting rights corresponding to the shares or other securities which, pursuant to the provisions of the legislation in force from time to time, exceed the limit specified in this Article shall be held in abeyance until such time as they comply with the limit.

4. As an exception to the general rule, and by reason of the special regime applied by the Electricity Industry Law to SEPI, the holding and voting rights of that company shall be governed by the provisions of these Corporate Bylaws, except as provided for in the Sole Additional Provision thereof.

*Sole Additional Provision.- Special Regime for SEPI*

1. By virtue of the provisions of the Electricity Industry Law, neither the limitations stipulated in Subprovision 2 of Additional Provision Three of Law 17/2007, nor the limitations stipulated in these Bylaws on the holding of shares in the Company and on voting rights shall apply to the State-owned Industrial Holdings Company. The State-owned Industrial Holdings Company will in all cases have a holding of not less than 10%.
2. Where a Director who is an individual holds office on behalf of the shareholder referred to in Transitional Provision Nine in relation to Article 34.1 of the Electricity Industry Law, his compensation must be in keeping with the applicable provisions on incompatibility in the public sector, notwithstanding any compensation that may accrue to such public shareholder, either because it has been directly appointed as a member of the Board of Directors or because of the services provided to the Board or its delegated Committees by the individuals representing such public holder of shares in the capital of the Company, and which exceed any compensation to which he may be personally entitled under such legislation, all of the foregoing, pursuant to Transitional Provision Nine, while such ownership situation is maintained».

There are no other additional bylaw restrictions differing from purely legal restrictions.

In turn, the National Energy Commission is authorized to take legal action to enforce the aforementioned statutory limits. Breach of the established shareholding limits constitutes a very serious infringement under the Electricity Industry Law and the individuals or legal entities that own the securities or to whom the excess shareholding is attributable will be liable.

The legal regime established by Directive 2009/72/EC, of July 13, 2009, which proclaims the mandatory independence of transmission companies and operators of European electricity systems, has endorsed the legal limitations on shareholders established in Law 17/2007.

Indicate whether there are statutory restrictions on the acquisition or transfer of holdings in the capital:

YES  NO

#### Description of statutory restrictions on the acquisition or transfer of holdings in the capital

The transfer of the shares representing the capital of Red Eléctrica Corporación, S.A. is free and is not subject to any restriction. Electricity industry legislation establishes certain limits on shareholdings, in the terms set out above.

As for all listed entities, the acquisition of certain significant holdings must be notified to the issuer and to the CNMV, as provided in Article 53 of Securities Market Law 24/1988 of July 28, 1988, in Royal Decree 1362/2007 of October 19, 2007, and in CNMV Circular 2/2007 of December 19, 2007, which establish the first notification threshold at 3% of capital or voting rights.

**A.11.** Indicate whether the Shareholders' Meeting has resolved to adopt countermeasures in the event of a tender offer pursuant to the provisions of Law 6/2007

YES  NO

If so, explain the measures approved and the circumstances in which the restrictions would be ineffective.

## B Management Structure of the Company

### B.1. Board of Directors

**B.1.1.** Give details of the maximum and minimum number of Directors provided for in the Corporate Bylaws:

#### Maximum number of Directors

13

#### Minimum number of Directors

9

**B.1.2.** Complete the following table indicating the particulars of the Board members:

Name of Director	Representative	Position on the Board	Date of first appointment	Date of last appointment	Appointment procedure
Luis María Atienza Serna		Chairman	07.08.04	05.21.09	Shareholders' Meeting
Antonio Garamendi Lecanda		Member	07.20.99	05.22.08	Shareholders' Meeting
Manuel Alves Torres		Member	10.26.99	05.22.08	Shareholders' Meeting
Rafael Suñol Trepát		Member	12.16.04	05.21.09	Shareholders' Meeting
María Ángeles Amador Millán		Member	05.26.05	05.21.09	Shareholders' Meeting
Francisco Javier Salas Collantes		Member	06.28.05	05.20.10	Shareholders' Meeting
José Folgado Blanco		Member	05.22.08	05.22.08	Shareholders' Meeting
Arantza Mendizábal Gorostiaga		Member	05.22.08	05.22.08	Shareholders' Meeting
María Jesús Alvarez González		Member	05.22.08	05.22.08	Shareholders' Meeting
Rui Manuel Janes Cartaxo		Member	05.20.10	05.20.10	Shareholders' Meeting
Miguel Boyer Salvador		Member	05.20.10	05.20.10	Shareholders' Meeting

#### Total number of Directors

11

Indicate any Board members who vacated their office during the year:

Name of Director	Type of departing Director	Departure date

**B.1.3.** Complete the following tables on the Board members and their status:

#### EXECUTIVE DIRECTORS

Name of Director	Nominated by (Committee)	Position in Company organizational chart
Luis M <sup>a</sup> Atienza Serna	Corporate Responsibility and Governance Committee	Chairman

#### Total number of Executive Directors

1
<b>% Total of Board</b>
9.1

#### EXTERNAL NOMINEE DIRECTORS

Name of Director	Nominated by (Committee)	Name of significant shareholder represented or that nominated the Director
Manuel Alves Torres	Board of Directors since, at the time, the Appointments, Compensation and Corporate Governance Committee did not exist <sup>(3)</sup>	State-owned Industrial Holdings Company (SEPI)
Raïael Suñol Trepal	Appointments and Compensation Committee	State-owned Industrial Holdings Company (SEPI)
María Jesús Álvarez González	Appointments, Compensation and Corporate Governance Committee	State-owned Industrial Holdings Company (SEPI)

(3) Today, the Corporate Responsibility and Governance Committee.

#### Total number of Nominee Directors

3
<b>% Total of Board</b>
27.3

## EXTERNAL INDEPENDENT DIRECTORS

**Antonio Garamendi Lecanda****Profile**

February 8, 1958.

Entrepreneur. Law Degree, Universidad de Deusto.

**Professional Career****Formerly:**

General Representative of La Equitativa, S.A. in Vizcaya.

Managing Director of Bankoa, S.A. Correduría de Seguros.

Chairman, Handyman, S.L.

Chairman of the "Negocios de Comunicación" Group (*La Gaceta de los Negocios*, Dinero, Radio Intereconomía and OTR News Agency).

Director, Babcock & Wilcox Española, S.A.

Director, Albura, S.A. (Red Eléctrica de Telecomunicaciones).

Director, Tubos Reunidos, S.A.

Member, Strategic Committee, Grupo Alta Gestión, S.A.

Chairman, Spanish Confederation of Young Entrepreneurs (CEAJE).

Chairman, Business Creation Commission, CEOE.

Member, Vizcaya Chamber of Real Estate.

Member, Board of Trustees, Guggenheim Museum.

Deputy Chairman, Entel Ibai, S.A.

Member of the Strategic Committee of Sodexo Pass, S.A. Group.

Member, Managing Board of Vizcaya Business Confederation (CEBEK).

**Currently:**

Chairman, Galea Empresarial, S.L.

Chairman, Palacio de Moronati, S.L.

Managing Director, Iniciativas de Comunicación Económica, S.A. (ICESA).

Insurance Broker. Willis Iberia, S.A.

Chairman, Fundación AYUDARÉ.

Chairman, Energy Committee, CEOE. Member, CEOE Executive Committee and Managing Board.

First Deputy Chairman, Spanish Confederation of Small and Medium-Sized Enterprises (CEPYME).

Member and Treasurer, Confemetal and Fundación Formetal.

Committee Member, Institute for Economic Studies (IEE).

Member of the Executive Committee of the Vizcaya Federation of Metal Companies.

Member, Vizcaya Chamber of Commerce.

## M<sup>a</sup> Ángeles Amador Millán

### Profile

October 10, 1949.

Law Degree, Universidad Complutense de Madrid.

### Professional Career

#### Formerly:

Technical General Secretary, Ministry of Public Works and Urban Development.

Undersecretary, Ministry of Health and Consumer Affairs.

Minister for Health and Consumer Affairs.

Member of Parliament for Segovia.

Member of Parliament for Madrid.

Deputy Chairwoman, Constitutional Committee, Lower House of Parliament.

#### Currently:

Practicing attorney.

Member, Governing Board of the Madrid Bar Association.

Board member, Fundación Arte y Derecho.

Member, Advisory Board, Accenture.

## Francisco Javier Salas Collantes

### Profile

March 6, 1948.

Degree in Economics, specializing in Business Economics.

### Professional Career

#### Formerly:

Specialist in credit analysis activities, International Division, Manufacturers Hanover Trust Co. (New York).

Director of Economic and Financial Planning and Director of Economy and Finance, Empresa Nacional del Uranio (ENUSA).

Finance Director, National Industry Institute (I.N.I.).

Director-General of Corporate Management, responsible for the following INI offices: Finance, Planning and Control, Technology and Investment.

Chairman, INI and Teneo.

Chairman, Iberia, Líneas Aéreas de España, while also Chairman of INI and Teneo.

#### Currently:

Founding Member and Manager of SAGA Servicios Financieros (Management and M&A Consultants).

Director of GED CAPITAL DEVELOPMENT, S.A., SGEGR and of GED IBERIAN PRIVATE EQUITY, S.A., SGEGR.

Chairman of Bloqmarine Internacional, S.L.

Member, Advisory Board, YOUNG & RUBICAM, S.L.



Chairman of Fundación Entorno, Empresa y Medioambiente.  
 Trustee, Instituto de Cuestiones Internacionales y Política Exterior (INCIPE).  
 Trustee, APMIB Foundation (Deputy Chairman).  
 Member of the Advisory Board of the Fundación de Estudios Financieros.  
 Director of Abengoa Solar.

## José Folgado Blanco

### Profile

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

### Professional Career

#### Formerly:

Head of the economics department of the CEOE.  
 Member of the Economic and Social Board representing business organizations.  
 Secretary of State for Budgets and Expenditure. Ministry of Economy and Finance, since May 1996.  
 Secretary of State for Economy, Energy and Small and Medium-Sized Enterprises. Ministry of Economy since April 2000.  
 Secretary of State for Energy, Industrial Development and Small- and Medium-Sized Enterprises. Ministry of Economy, since July 2002.  
 Parliamentary representative of the province of Zamora and Deputy Chairman of the Economy and Finance Committee, since March 2004.

#### Currently:

Tenured Professor of Public Finance and Tax Systems, Universidad Autónoma de Madrid.  
 Mayor of Tres Cantos (Madrid) since June 2007.  
 Member of the Social Board, Universidad Autónoma de Madrid.

## Arantza Mendizábal Gorostiaga

### Profile

February 22, 1950.  
 Degree in Economics.  
 Doctorate in Economics.  
 Professor of Applied Economics.

## Professional Career

### Formerly:

Professor and researcher, industrial and technological policy.  
 Acting Rector, Universidad del País Vasco (UPV-EHU).  
 Visiting fellow at St. Anthony's College (Oxford).  
 Member of Parliament.  
 Spokeswoman, Industry, Tourism and Trade Committee, Lower House of Parliament.  
 MP member, Economy and Finance Committee, Lower House of Parliament.  
 MP member, Budget Committee, Lower House of Parliament.

### Currently:

Professor of Applied Economics at the School of Economics and Business Studies and Director of the European Documentation Center, Universidad del País Vasco.

## Miguel Boyer Salvador

### Profile

February 5, 1939.  
 Degree in Physical Science and Economics, with special distinction, Universidad de Madrid.

## Professional Career

### Formerly:

Director of Studies, Instituto Nacional Industria (I.N.I.).  
 Head of Strategic Planning, Explosivos Río Tinto.  
 Member of Parliament for Jaén.  
 Director of Planning and Studies, Instituto Nacional de Hidrocarburos.  
 Minister for Economy, Finance and Trade.  
 Chairman, Banco Exterior de España.  
 Member of the Review Committee, European Organization for Nuclear Research (CERN, Geneva).  
 Member – as one of two experts – of the Expert Group on the Economic and Monetary Union of the European Union ("Delors Commission").  
 Chairman, Cartera Central.  
 Chairman and Managing Director, Grucyrsa.  
 Deputy Chairman, FCC Construcción.  
 Chairman, Compañía Logística de Hidrocarburos (CLH).

### Currently:

Representative of Corporación Financiera Issos, on the Board of Directors of Reyal-Urbis, S.A.

## Rui Manuel Janes Cartaxo

### Profile

July 9, 1952.

Degree in Economics, Universidad Técnica de Lisboa.

### Professional Career

#### Formerly:

Lecturer, Instituto Superior de Economía y Gestión (ISEG).

Economist, research area, Banco de Portugal.

Consultant, OECD Department of Research (Paris).

Financial Director, Ministry of Finance.

Executive Director, CN-Comunicações Nacionais, SGPS, S.A.

Executive Director, TRANSGÁS, S.A.

CEO of GALP POWER.

Executive Director, GALP ENERGÍA SGPS.

Assistant to the Portuguese Minister of Economy and Innovation.

CFO of REN-REDES ENERGÉTICAS NACIONAIS, SGPS.

#### Currently:

Chairman and CEO of REN-REDES ENERGÉTICAS NACIONAIS, SGPS.

#### Total number of Independent Directors

7

#### % Total of Board

63.6

Antonio Garamendi Lecanda has completed the maximum term of 12 years as an Independent Director of RED ELÉCTRICA. According to the provisions of Article 7.2 c) of the Board Regulations, the Unified Good Governance Code and international corporate governance best practices, this is the maximum period for which he may be treated as an Independent Director and, therefore, if a proposal is made for his reappointment at the next Annual Shareholders' Meeting, he will be classed the category of "other External Directors."

If the Annual Shareholders' Meeting approves the reappointment of Mr. Garamendi as a Company Director, he must immediately be replaced as Chairman of the Corporate Responsibility and Governance Committee, a position which must be occupied by an Independent Director, in accordance with the Corporate Bylaws and the Board Regulations.

## OTHER EXTERNAL DIRECTORS

Name of Director

Nominated by (Committee)

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Total number of External Directors

% Total of Board

--

Give details of the reasons why they cannot be considered Nominee or Independent Directors and their relationships, either with the Company or its executives, or with Company shareholders:

Name of Director

Reasons

Company, executive or shareholder with which the relationship is held

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Indicate any variations in the status of each Director that may have occurred during the year:

Name of Director

Date of change

Previous status

Current status

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**B.1.4.** Explain, where applicable, the reasons why Nominee Directors have been appointed at the request of shareholders whose holdings are less than 5% of capital:

Name of shareholder

Justification

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Indicate whether any formal requests for presence on the Board have not been honored from shareholders whose shareholdings are greater than or equal to those of others upon whose request Nominee Directors have been appointed. Explain, where applicable, why the requests have not been honored:

YES  NO 

Name of Director

Explanation

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**B.1.5.** State whether any Director has resigned his position before the end of his term of office, whether that Director explained his reasons to the Board and, if so, in what way, and, where he did so in writing to the entire Board, explain at least the reasons given by that Director:

Name of Director	Reason for resignation

**B.1.6.** Indicate what powers, if any, have been delegated to the Managing Director(s):

Name of Director	Brief description
Luis M <sup>a</sup> Atienza Serna	The Board meeting held on June 25, 2009 unanimously resolved, as proposed by the Appointments, Compensation and Corporate Governance Committee (currently called the Corporate Responsibility and Governance Committee):  «To delegate to the Chairman of the Board of Directors of RED ELÉCTRICA CORPORACIÓN, S.A., Mr. Luis M <sup>a</sup> Atienza Serna, pursuant to the provisions of Article 141 of the current Corporations Law, Article 149 of the Mercantile Registry Regulations, Article 22 of the Corporate Bylaws and Article 5 of the Board Regulations, all powers of the Board of Directors that may be delegated by law and pursuant to the Bylaws».

**B.1.7.** Identify, as appropriate, which members of the Board hold office as Directors or executives at other companies forming part of the listed Company's Group:

Name of Director	Name of Group entity	Position
Luis M <sup>a</sup> Atienza Serna	Red Eléctrica Internacional, S.A. (Sole-Shareholder Company)	Joint Director
Luis M <sup>a</sup> Atienza Serna	Red Eléctrica del Sur, S.A. (REDESUR)	Chairman of the Board of Directors
Luis M <sup>a</sup> Atienza Serna	Transportadora de Electricidad, S.A. (TDE)	Chairman of the Board of Directors

**B.1.8.** Give details, as appropriate, of any Company Directors who are members of the boards of directors of other entities outside the Group that are listed on official securities markets in Spain, as disclosed to the Company:

Name of Director	Name of listed entity	Position
Rafael Suñol Trepal	INYPSA Informes y Proyectos, S.A.	Director

**B.1.9.** Indicate and explain, as appropriate, whether the Company has established rules on the number of Committees of which its Directors may be members:

YES  NO

**Explanation of the rules**

As part of the basic duties of the Corporate Responsibility and Governance Committee in respect of the appointment and removal of directors, Article 16.1 f) of the Regulations of the Board of Directors provides for the evaluation of the time and dedication necessary for directors to perform their work with due quality and efficiency, evaluating for these purposes whether their position as a director is compatible with membership of other managing bodies of companies.

In this regard, the Corporate Responsibility and Governance Committee has the power to analyze and authorize, as the case may be, the members of the Board of Directors of Red Eléctrica to join the boards of directors of other companies.

Article 7.3 of the Board Regulations limits the maximum number of boards of other listed companies on which an Independent Director may sit to two.

**B.1.10.** Regarding Recommendation 8 of the Unified Code, state the general policies and strategies of the Company reserved for approval to the plenary session of the Board:

	Yes	No
Investment and financing policy	X	
Definition of the structure of the corporate group	X	
Corporate governance policy	X	
Corporate social responsibility policy	X	
The strategic or business plan, as well as annual management objectives and budget	X	
Policy regarding compensation and performance evaluation of senior executives	X	
Risk control and management policy, as well as periodic monitoring of internal reporting and control systems	X	
Dividend and treasury stock policy and, in particular, their limits	X	

**B.1.11.** Complete the following tables on the aggregate compensation of Directors during the year:

a) At the Company to which this report relates <sup>(4)</sup>:

Compensation Item	€ Thousand
Fixed compensation (note b)	404
Variable compensation	1,286
Attendance fees (note c)	819
Bylaw-stipulated fees	
Stock options and/or other financial instruments	
Other (note b) <sup>(5)</sup>	17
<b>TOTAL (nota a):</b>	<b>2,526</b>

<sup>(4)</sup> At the Company to which this report relates.

<sup>(5)</sup> This section is broken down in the following table under "Other benefits".

(note a): The compensation of the Board of Directors, without taking into account the compensation of the Chairman in his capacity as Executive Director, amounted to €1,886,000, the same amount as in 2010. This compensation has remained unaltered since 2007.

(note b): The fixed compensation of the Chairman, in his capacity as Executive Director, amounted to €429,000, the same amount as in 2010. This fixed compensation has remained unaltered since 2008. In his capacity as member of the Board of Directors of REN, the Executive Director received compensation of €8,000 in 2011 (€29,000 in 2010) which, as in previous years, has been discounted from the fixed compensation. As of April 2011, REC holds the status of corporate Director on the Board of Directors of REN and the Company has therefore received the compensation directly since that date. Accordingly, for the Executive Director, the sum of the fixed compensation, life insurance and pension plan contributions, together with the compensation received in his capacity as member of the Board of Directors of REN, amounted to €429,000.

(note c): Eleven Board meetings were held in 2011, two less than in 2010.

Other benefits	€ Thousand
Advances	
Loans granted	
Pension funds and plans: contributions	6
Pension funds and plans: agreed obligations	
Life insurance premiums	11
Guarantees provided by the Company for Directors	
<b>TOTAL</b>	<b>17</b>

b) Due to membership of the Company's Directors of other boards of directors and/or senior management of Group companies:

Compensation Item	€ Thousand
Fixed compensation	
Variable compensation	
Attendance fees	
Bylaw-stipulated fees	
Stock options and/or other financial instruments	
Other	
<b>TOTAL</b>	

Other benefits	€ Thousand
Advances	
Loans granted	
Pension funds and plans: contributions	
Pension funds and plans: agreed obligations	
Life insurance premiums	
Guarantees provided by the Company for Directors	
<b>TOTAL</b>	

## c) Total compensation by type of Director:

Type of Director	By company	By Group
Executive	822	
External Nominee	517	
External Independent	1,187	
Other External		
<b>TOTAL</b>	<b>2,526</b>	

The compensation of the Executive Director, including the compensation received from REN, amounts to €831,000 in 2011 (€825,000 in 2010). The variation in compensation in 2011 compared to 2010 is fundamentally due to variable compensation.

d) With respect to income attributed to the parent company <sup>(6)</sup>:

Total Directors' compensation (€ thousand)	2,526
Total Directors' compensation / Income allocated to parent company (as a %)	0.54

**B.1.12.** Identify the members of senior management who are not, in turn, Executive Directors, and indicate the total compensation paid to them during the year <sup>(7)</sup>:

Set forth below is the information regarding the members of senior management that provide services within the Red Eléctrica Group:

Name	Position
Carlos Collantes Pérez-Ardá	Director-General of Transmission
Esther María Rituerto Martínez	Director-General of Finance and Administration
Alberto Carbajo Josa	Director-General of System Operation

<b>Total senior management compensation (€ Thousand)</b>	<b>1,023 <sup>(8)</sup></b>
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(6) The income obtained by the RED ELÉCTRICA Group and attributed to the parent company in 2011 amounted to €460,348,000 (€390,150,000 in 2010).

(7) Exclusively for the purposes of CNMV Circular 4/2007 of March 27, 2007, members of senior management are those individuals who manage the Company at the highest level (excluding the CEO) and, consequently, independently of their legal employment relationship with the Company.

(8) This amount includes €57,000 of life insurance and pension plan contributions.



**B.1.13.** Identify, in aggregate terms, whether there are any safeguard or golden parachute clauses for members of senior management, including the Executive Directors of the Company or of its Group, in the event of dismissal or changes in control. Indicate whether these contracts have to be disclosed to and/or approved by the bodies of the Company or of its Group:

<b>Number of beneficiaries</b>	3	
<b>Body authorizing the clauses</b>	<b>Board of Directors</b>	<b>Shareholders' Meeting</b>
	X	
<b>Is the Shareholders' Meeting informed of the clauses?</b>	<b>YES</b>	<b>NO</b>
	X	

There are safeguard or golden parachute clauses in favor of the Executive Director to cover dismissal or changes in control. These clauses were proposed by the Appointments, Compensation and Corporate Governance Committee (now called the Corporate Responsibility and Governance Committee) and approved by the Board of Directors. These clauses are in line with standard market practices and cover the termination of the employment relationship, providing for indemnification of one year's salary, unless the applicable legislation provides for a higher amount.

In 2011, there are also safeguard or golden parachute clauses for dismissal in favor of two executives. These clauses are in line with standard market practices and cover the termination of the employment relationship, providing for indemnification of up to two years' salary, unless the applicable legislation provides for a higher amount. The contracts containing these clauses were approved by the Appointments, Compensation and Corporate Governance Committee and they were duly notified to the Board of Directors.

**B.1.14.** Indicate the process for establishing the compensation of the members of the Board and the relevant Bylaw provisions:

#### Process for establishing the compensation of Board members and Bylaw clauses

Provisions regarding the compensation of the members of the Board of Directors are currently contained in Article 20 and in the Sole Additional Provision of the Bylaws, as well as in Article 27 of the Board Regulations. These provisions are set forth below:

##### I. Corporate Bylaws:

###### Article 20:

«...The compensation of the Board of Directors shall consist of a fixed monthly fee for the attendance of Board meetings and a share in the Company's income. Overall annual compensation for the entire Board and for the above items shall be 1.5 percent of the Company's net income, approved by the Shareholders' Meeting. The above compensation is, in all cases, a maximum figure and the Board itself shall be in charge of allocating the amount among the aforesaid items and among the Directors in such manner, at such time and in such proportion as it freely determines. Pursuant to Article 218.2 of the Corporate Enterprises Law, compensation in the form of a share in income may only be received by Directors after the provisions to the legal and bylaw reserves have been covered and the shareholders have been recognized a dividend of not less than 4%.

Compensation consisting of the award of shares or stock options or compensation linked to share value shall require a resolution

of the Shareholders' Meeting, which must state the number of shares to be awarded, the price for exercising the options, the share value taken as a reference and the term of this compensation system.

The compensation stipulated in this Article shall be compatible with and independent of salaries, wages, severance pay, pensions or compensation of any kind established generally or individually for members of the Board of Directors who hold an ordinary or special senior management employment relationship or an independent professional relationship with the Company, which relationships shall be compatible with the status of member of the Board of Directors».

**Sole Additional Provision, second paragraph:**

«Where a Director who is an individual holds office on behalf of the shareholder referred to in Transitional Provision Nine in relation to Article 34.1 of the Electricity Industry Law —the State-owned Industrial Holdings Company—, his compensation must be in keeping with the applicable provisions on incompatibility in the public sector, notwithstanding any compensation that may accrue to such public shareholder, either because it has been directly appointed as a member of the Board of Directors or because of the services provided to the Board or its delegated Committees by the individuals representing such public holder of shares in the capital of the Company, and which exceed any compensation to which he may be personally entitled under such legislation, all of the foregoing, pursuant to Transitional Provision Nine, while such ownership situation is maintained».

**II. Board Regulations (Article 27):**

1. Directors shall be entitled to obtain such compensation as is established by the Shareholders' Meeting and by the Board of Directors in accordance with the provisions of the Corporate Bylaws and those contained in these Regulations.

2. The compensation policy approved by the Board of Directors shall cover at least the following matters:

- a) The amount of the fixed compensation items, itemizing any fees for attending Board and Committee meetings, with an estimate of the annual fixed compensation to which they give rise.
- b) Variable compensation items, including, in particular:
  - i) The types of Director to which they apply, with an explanation of the relative weighting of variable to fixed compensation items.
  - ii) Criteria for evaluating results on which any right to compensation is based.
  - iii) Fundamental parameters and the basis for any system of annual bonuses or other benefits not paid in cash.
  - iv) An estimate of the absolute amount of the variable compensation arising from the proposed compensation plan, depending on the degree of compliance with the assumptions or objectives taken as a reference.

This shall also include the technical safeguards necessary to ensure that such variable compensation is in line with the professional performance of its beneficiaries and is not merely the result of the general performance of the markets or of the industry in which the Company operates, or other similar circumstances.

- c) The principal characteristics of the corporate welfare systems, with an estimate of their amount or equivalent annual cost.
- d) Conditions that must be observed in the contracts of those exercising senior management functions as Executive Directors, including term, advance notice periods and any other clauses relating to signing bonuses, as well as indemnification for early termination or termination of the contractual relationship between the Company and the Executive Director.

3. Compensation by way of the award of Company shares, on the terms authorized by the Shareholders' Meeting, variable compensation linked to the Company performance and corporate welfare systems shall be reserved to Executive Directors.

4. Compensation linked to the Company's earnings shall take into account any qualifications stated in the external auditor's report that reduce such income.

5. Directors' compensation shall be transparent. For such purpose, the Corporate Responsibility and Governance Committee shall prepare an annual report on Directors' compensation, which shall include:

- a) An individual breakdown of the compensation obtained by each Director, to include, where appropriate:
  - i) Any attendance fees and other fixed compensation as Director.
  - ii) Additional compensation as a member of any Board Committee.
  - iii) Any compensation in the form of a share in income or premiums, and the reason for which it is granted.
  - iv) Contributions on behalf of Executive Directors to fixed-contribution pension plans, or any increase in the vested rights of Executive Directors in the case of contributions to fixed-benefit plans.
  - v) Any severance agreed or paid in the event of termination of their functions.
  - vi) Any compensation received as a Director of other Group companies.
  - vii) Compensation for the performance of senior management functions by Executive Directors.

viii) Any other compensation item other than those listed above, regardless of its nature or the Group company that pays it, especially where it is deemed a related-party transaction or where its omission distorts the true and fair view of the compensation received by the Director.

b) An individual breakdown of any award of shares to Executive Directors, on the terms authorized by the Shareholders' Meeting.

c) Information on the relationship, in the preceding year, between the compensation obtained by Executive Directors and the earnings or other performance indicators of the Company.

Indicate whether approval of the following decisions is reserved to the plenary session of the Board:

	YES	NO
At the proposal of the Company's Chief Executive, the appointment and removal of senior executives and their indemnification clauses.	X	
Directors' compensation and, in the case of Executive Directors, the additional consideration for their executive functions and other contractual conditions that must be observed.	X	

**B.1.15.** Indicate whether the Board of Directors approves a detailed compensation policy and specify the matters addressed by it:

YES  NO

	YES	NO
The amount of the fixed compensation items, broken down, where necessary, into attendance fees for Board and Board Committee meetings, and an estimate of the fixed annual compensation to which they give rise.	X	
Variable compensation items.	X	
The principal characteristics of corporate welfare systems, with an estimate of their amount or equivalent annual cost.	X	
Conditions to be respected in the contracts of those individuals exercising senior management functions as Executive Directors.	X	

**B.1.16.** Indicate whether the Board submits a report on the Directors' compensation policy to the advisory vote of the Shareholders' Meeting, as a separate item on the agenda. As appropriate, explain the aspects of the report on the compensation policy approved by the Board for future years, the most significant changes in that policy by comparison with the policy applied during the year, and an overall summary of how the compensation policy was applied during the year. Describe the role of the Compensation Committee and, where external advisers have been used, identify the external consultants engaged:

YES  NO

### Matters addressed by the compensation policy report

The report on Red Eléctrica's compensation policy is prepared following the recommendations of the Conthe Code (section 40), the European Commission Recommendation of December 14, 2004 and the European Commission Recommendation of April 30, 2009 as regards the regime for the remuneration of Directors of listed companies, which has been incorporated into Sustainable Economy Law 2/2011, of March 4, 2011, which added Article 61 ter to the Securities Market Law. This Article introduces the obligation of the boards of directors of listed companies to prepare an annual report on directors' compensation, to include complete, clear and understandable information on the compensation policy of the company approved by the board for the year in question and, as the case may be, the policy envisaged for future years. It also establishes that the report shall also include an overall summary of how the compensation policy was applied during the year, and a breakdown of the individual compensation earned by each Director, which shall be disclosed and submitted to the advisory vote of the Annual Shareholders' Meeting, as a separate item on the agenda.

Over and above the requirements of Article 61 ter of the Securities Market Law, for several years now Red Eléctrica has been voluntarily submitting the compensation of the Board of Directors of the Company for approval by the Annual Shareholders' Meeting. Both the report on director's compensation and the resolution to be proposed to the Shareholders' Meeting regarding Board compensation will be submitted by the Board — as separate items on the Agenda for the Shareholders' Meeting— to the Annual Shareholders' Meeting.

This year, the report on directors' compensation has been prepared by taking into account not only the requirements of the new Article 61 ter of the Securities Market Law but also the requests for information from foreign international investors and their advisers, as well the most advanced national and international corporate governance practices in this area.

For further information, please see the 2011 Annual Report on Directors' Compensation.

### Role of the Corporate Responsibility and Governance Committee

The policy for applying the bylaw compensation criteria was proposed by the Corporate Responsibility and Governance Committee and approved by the Board of Directors, without prejudice to its subsequent submission to the Shareholders' Meeting for approval.

The Committee met on 11 occasions in 2011, for the most part to address compensation matters relating to the Company's Board and senior management.

	YES	NO
Was external advice sought?	X	
Identity of external consultants	J&A Garrigues, S.L.P. <sup>(9)</sup>	

(9) Legal advisers for the preparation of the 2011 Annual Report on Directors' Compensation.

**B.1.17.** Indicate, as appropriate, which members of the Board are, in turn, members of the boards of directors, executives or employees of companies that own significant holdings in the listed Company and/or in entities of its Group:

Name of Director	Name of significant shareholder	Position
Manuel Alves Torres	State-owned Industrial Holdings Company (SEPI)	Director of Planning and Control and member of the Management Committee
María Jesús Álvarez González	State-owned Industrial Holdings Company (SEPI)	Director of Economy and Finance and member of the Management Committee

Give details, as appropriate, of any material relationships, other than those envisaged under the preceding heading, of the members of the Board of Directors with significant shareholders and/or entities in its Group:

Name of related Director	Name of related significant shareholder	Description of relationship

**B.1.18.** Indicate whether there have been any amendments to the Board Regulations during the year:

YES  NO

#### Description of amendments

**B.1.19.** Indicate the procedures for the appointment, reappointment, evaluation and removal of Directors. Give details of the competent bodies, the formalities to be fulfilled and the criteria to be used in each of the procedures.

##### 1. Appointment and reappointment

Article 19 of the Board Regulations provides that Directors will be appointed by the Shareholders' Meeting or by the Board of Directors by way of co-optation. The Corporate Responsibility and Governance Committee must report in advance on the proposed appointment of Directors, including by way of co-optation. Within the scope of its powers, the Board of Directors will procure that the candidates appointed are of good standing, competence and experience, as provided in Article 20 of the Regulations.

As provided in Article 21 of the Regulations, Directors will hold office for the period stipulated in the Corporate Bylaws. Proposals submitted by the Board to the Shareholders' Meeting for the appointment or reappointment of Directors, as well their provisional appointment by co-optation, will be approved by the Board:

- i) At the proposal of the Corporate Responsibility and Governance Committee, in the case of Independent Directors.
- ii) Following a report by the Corporate Responsibility and Governance Committee in the case of all other Directors.

Article 20 of the Corporate Bylaws establishes a four-year term of office for Directors, who may be reappointed indefinitely. As provided in Article 7 of the Board Regulations, Independent Directors may not remain in office for a continuous period of more than twelve years.

In October 2011, the Board of Directors approved a Board Chairman Succession Plan, in accordance with the most recent international corporate governance practices. More information on this is set forth in section G) of this Report.

## 2. Evaluation of Directors

As in every year, the Board has begun the yearly self-evaluation of the Board, its Committees and its Chairman.

After the consideration given in 2010 to the possibility of having the self-evaluation process reviewed by external advisers with a view to optimizing the methodology used and aligning it with the best practices in this area, the 2011 self-evaluation is being carried out with the support of expert external advisers (KPMG).

The conclusions of the KPMG report on the findings of the evaluation highlight the high level of commitment of the Directors, their pride in belonging to the Company, their commitment to excellence in the management of the company and the continuous incorporation of corporate governance best practices. The report also contemplates certain ways of improving Board practices, including strengthening communications with shareholders and investors in general, reinforcing the role of Independent Directors in Board tasks or the role of the Board in defining and monitoring the risk control policy.

## 3. Removal

Article 22 of the Board Regulations provides that Directors will cease to hold office at the end of the term for which they were appointed or when so decided by the Shareholders' Meeting in exercise of the authority conferred upon it by law or the Bylaws. The Board of Directors must not propose the removal of an Independent Director prior to the completion of the term of office specified in the bylaws for which the Director was appointed, unless there is just cause and subject to a report from the Corporate Responsibility and Governance Committee.

Directors must tender their resignation to the Board of Directors and, if the Board deems it appropriate, formally resign in the cases contemplated in Article 22.2 of the Board Regulations and listed in section B.1.20 below.

Article 22.3 of the Board Regulations provides that Committee members will vacate their office when they relinquish their directorships.

When a Director vacates his office before the end of his term, by reason of resignation or otherwise, he will explain the reasons in a letter to be sent to all members of the Board, the matter being reported in the Annual Corporate Governance Report, as provided in Article 22.4 of the Board Regulations.

### **B.1.20.** Indicate the cases in which Directors must resign:

Article 22.2 of the Board Regulations provides that Directors must tender their resignation to the Board of Directors and, if the Board deems it appropriate, formally resign, in the following cases:

- a) Upon reaching 70 years of age.*
- b) When they are subject to any of the grounds of incompatibility or prohibition provided for by law.*
- c) When they are convicted of an offense or penalized for a serious or very serious infringement in disciplinary proceedings conducted by the supervisory authorities of the securities, energy and telecommunications markets.*
- d) When they have seriously breached their obligations as Directors.*
- e) When they stand down from the executive positions with which their appointment as Director was associated.*

- f) When their continued presence on the Board jeopardizes the Company's interests, in particular, in relation to Article 30.4 of these Regulations, and the Board deems this to be the case with the affirmative vote of two-thirds of its members.
- g) In the case of a Nominee Director, when the shareholder whose shareholding interests he represents on the Board disposes of its shareholding in the Company or reduces it below the level which reasonably justified his appointment as such».

**B.1.21.** Explain whether the function of Company Chief Executive falls to the Chairman of the Board. As appropriate, indicate what measures have been taken to limit the risks of power being concentrated in the hands of one person:

YES  NO

#### Measures to limit risks

Article 25 of the Corporate Bylaws states that the Chairman of the Board is the Chairman of the Company and of its governing and management bodies.

Furthermore, he is the person responsible for senior management and full representation of same in all matters, acting with the powers delegated by the Board.

The Chairman has the power to adopt, for reasons of urgency, the measures he deems appropriate in the interests of the Company, but must immediately report on such measures to the Board of Directors. All of the foregoing is without prejudice to regular reporting to ordinary Board meetings on the corporate management of the different areas of the Company, requesting, as the case may be, approval of the resolutions submitted.

In particular, pursuant to the provisions of Article 5.6 of the Board Regulations, the Board is reserved «*the direct exercise of the following responsibilities that cannot be delegated, except for those contemplated in letters b) and c) below, which may be adopted for reasons of urgency by the Chairman of the Company and subsequently ratified by the Board:*

a) Approval of the general policies and strategies of the Company and, in particular:

- i) Approval of the strategic or business plan of the Company and its Group, as well as the annual budget and management objectives.
- ii) Approval of the investment and financing policy.
- iii) Approval of the definition of the structure of the corporate Group.
- iv) Approval of the corporate governance policy.
- v) Approval of the corporate responsibility policy.
- vi) Approval of the policy regarding compensation and evaluation of senior executives.
- vii) Approval of the policy for control and management of the principal risks of the Company and of the Group, and knowledge and periodic monitoring of internal control, prevention and reporting systems.

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

- The different kinds of risk (operating, technological, financial, legal, reputational, etc.) the Company is exposed to, including contingent liabilities and other off-balance-sheet risks among the financial or economic risks.
- The determination of the risk level the Company deems to be acceptable.
- The measures envisaged to mitigate the impact of the identified risks, should they materialize.
- The internal reporting and control systems to be used to control and manage the above risks, including contingent liabilities and off-balance-sheet risks.

viii) Approval and, if applicable, proposal to the Shareholders' Meeting of the dividend and treasury stock policies, in particular, the limits thereof.

ix) Those specifically stipulated in these Regulations.

b) The following decisions:

- i) Directors' compensation and, in the case of Executive Directors, the additional consideration for their executive functions and other contractual conditions that must be observed.
- ii) Financial information that the Company must periodically disclose as a listed company.
- iii) Investments or transactions deemed to be strategic by virtue of their high amount or special characteristics, unless their approval corresponds to the Shareholders' Meeting.
- iv) The creation or acquisition of holdings in special-purpose vehicles or entities domiciled in countries or territories that are considered tax havens, and any other transactions and operations that could impair the transparency of the Group.

c) Related-party transactions, as defined by the legislation in force from time to time, that are material or outside the ordinary course of business of the Company and must be reported obligatorily to the securities markets, pursuant to the aforementioned legislation, following a report by the Audit Committee.

Where a related-party transaction involves a Director, in addition to not exercising or delegating his right to vote, the Director shall leave the meeting while the Board of Directors deliberates and votes on the transaction, after having informed the Board of the transaction.

d) The annual evaluation of:

- i) The quality and efficiency of the functioning of the Board and the performance by the Chairman of his functions, based on a report referred thereto by the Corporate Responsibility and Governance Committee.
- ii) The functioning of its Committees, based on the reports referred thereto by them».

To all of the foregoing it should be added that the existence of the Audit Committee and of the Corporate Responsibility and Governance Committee, entirely composed of members of the Board of Directors specializing in matters within their sphere of responsibility, reinforces the specific control exercised over the basic and strategic responsibilities of the Board of Directors, which in no event will be performed exclusively by the Chairman.

Indicate and, as appropriate, explain whether rules have been established allowing Independent Directors to request the call of Board meetings or the inclusion of new items on the agenda in order to coordinate and give voice to the concerns of External Directors and to lead the evaluation by the Board of Directors.

YES  NO

#### Explanation of the rules

Directors may request the inclusion of new items on the agenda for Board meetings without limitation. In this regard, pursuant to Article 17 of the Board Regulations, a Board meeting may be called by three Directors.

Therefore, any Director may request a Board meeting to be called, and, where jointly requested in writing by three Directors, independently of the type of Director, the Corporate Bylaws and the Board Regulations establish that the Board must meet, thus providing greater flexibility for calling Board meetings.

Management of the evaluation process is expressly delegated to the Corporate Responsibility and Governance Committee.

The Board Regulations attribute to the Chairman of the Corporate Responsibility and Governance Committee, who is an Independent Director, the function of communication and coordination between External and/or Independent Directors in the discharge of their duties, and include the possibility of requesting a Board meeting to be called or the inclusion of new items on the agenda at the request of any Director, as well as the coordination of the concerns of External Directors.

Law 25/2011, of August 1, 2011, partially reforming the Corporate Enterprises Law, establishes the possibility that Directors making up less than one-third of the members of the Board may call a Board meeting, setting the agenda, to be held in the municipality of the registered office, if, after making a request to the Chairman, the Chairman fails to call the meeting within one month without just cause.

**B.1.22.** Are qualified majorities, other than the statutory majorities, required for any type of decision?

YES  NO

Article 3.4 of the Board Regulations provides that, in order to be valid, any amendment of the Regulations will require a resolution adopted by a two-thirds majority of the Directors present.



Indicate how resolutions are adopted on the Board of Directors and specify, at least, the minimum attendance quorum and the type of majority for adopting resolutions:

Adoption of resolutions		
Type of resolution	Quorum	Type of majority
Any resolution, with the exception of amendments to the Board Regulations	Half plus one of the Directors present in person or by proxy	Simple

No provision is made for resolutions that require a qualified majority for their adoption, apart from those specifically contemplated in the applicable legislation and those relating to amendments to the Board Regulations.

Except in cases where other quorum requirements have been specifically established, the Board will be validly constituted where at least half plus one of its members are present, in person or by proxy. Where an odd number of Directors are present, a sufficient quorum will be deemed to exist if the next whole number immediately exceeding half of the Directors is present.

Article 21 of the Corporate Bylaws establishes that any Director may grant a proxy to another Director, in writing and specifically for each meeting, to attend and vote on his behalf at meetings of the Board of Directors, procuring that the proxy is granted to a Director of the same type as the Director represented (Article 28.2 b of the Board Regulations).

The Chairman will be tasked with organizing the debate, ensuring and encouraging the participation of all Directors in Board deliberations, and putting the items to a vote once he deems them to have been sufficiently debated. Each Director, present in person or by proxy, will have one vote.

Article 21 of the Bylaws and Article 18 of the Board Regulations establish that resolutions will be adopted by majority vote, unless the law requires that resolutions be adopted by a higher majority or in the aforesaid case of amendment of the Regulations of the Board of Directors, as specified in Article 3.4 thereof.

**B.1.23.** Explain whether there are any specific requirements, apart from those relating to the Directors, to be appointed Chairman:

YES  NO

**Description of requirements**

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**B.1.24.** Indicate whether the Chairman has a casting vote:

YES  NO

### Matters on which there is a casting vote

In the event of a tied vote, the Chairman will have the casting vote and will decide upon the issue independently of the subject matter of the resolution being voted on (Article 21 of the Corporate Bylaws and Article 18.3 of the Board Regulations).

**B.1.25.** Indicate whether the Bylaws or the Board Regulations impose any limit on the age of Directors:

YES  NO

**Age limit for Chairman** 70      **Age limit for Managing Director** —      **Age limit for Director** 70

Article 22 of the Board Regulations provides that Directors must tender their resignation to the Board of Directors and, where the Board deems it appropriate, formally resign once they reach seventy (70) years of age.

**B.1.26.** Indicate whether the Bylaws or Board Regulations establish any limit on the term of office of Independent Directors:

YES  NO

**Maximum number of years in office** 12

As with all other Company Directors, Independent Directors will hold office for four years and may be reappointed indefinitely.

Notwithstanding the foregoing, as provided in Article 7.2 c) in fine of the Board Regulations, Independent Directors may not remain in office for a continuous period of more than twelve years.

Antonio Garamendi Lecanda has completed the maximum term of 12 years as an Independent Director of RED ELÉCTRICA. According to the provisions of Article 7.2 c) of the Board Regulations, the Unified Good Governance Code and international corporate governance best practices, this is the maximum period for which he may be treated as an Independent Director and, therefore, if a proposal is made for his reappointment at the next Annual Shareholders' Meeting, he will be classed the category of "other External Directors."

If the Annual Shareholders' Meeting approves the reappointment of Mr. Garamendi as a Company Director, he must immediately be replaced as Chairman of the Corporate Responsibility and Governance Committee, a position which must be occupied by an Independent Director, in accordance with the Corporate Bylaws and the Board Regulations.

As already indicated in Section B.1.19 above, unless there is sufficient cause and subject to a report by the Corporate Responsibility and Governance Committee, the Board of Directors may not propose the removal of any External Directors before the end of the term for which they were appointed.

**B.1.27.** Where female Directors are few or non-existent, explain the reasons why and the initiatives adopted to correct the situation.

#### Explanation of reasons and initiatives

In line with Recommendation 15 of the Conthe Code, the aim of gradually adding female Directors with the appropriate qualifications and experience to the Board served as a guide for the reports and proposals of the Corporate Responsibility and Governance Committee and of the Board of Directors. As a result, two female Directors were appointed by the Annual Shareholders' Meeting held on May 22, 2008.

At 2011 year-end, the Board of Directors of Red Eléctrica Corporación S.A. had the same number of female Directors as at 2010 year-end, that is, 3 female Directors (2 Independent and 1 Nominee) out of a total of 11 Directors, meaning that women represented 27.3% of the Board.

The commitment of the Board of Directors of Red Eléctrica to strengthening the presence of women is an objective of good corporate governance policies, both on the Board of Directors and in Company Management and the rest of the organization of the main companies of the Red Eléctrica Group. Its pursuit must be ongoing in order to consolidate a responsible corporate management model based, among other aspects, on active management of the principles of equality and non-discrimination.

As part of its ongoing commitment to adopt corporate governance best practices, the Board of Directors assumed the obligation of approving an annual report on gender diversity matters at the proposal of the Corporate Responsibility and Governance Committee, and the first edition of the report was approved at the end of 2008.

In line with this commitment, the Board meeting held on July 27, 2011 approved the Report on Gender Diversity, which was referred to it by the Corporate Responsibility and Governance Committee, and was notably granted the *Igualdad en la Empresa* (Equality in Enterprise) distinction by the Ministry of Health, Social Policy and Equality. This Report has been published on the Company's website.

The same Board meeting of July 27, 2011 also analyzed the content of a Company Equality Policy, which was approved following a favorable report by the Corporate Responsibility and Governance Committee.

The Red Eléctrica Equality Policy will be implemented by setting up the relevant internal procedures at the Company and establishing an Integral Equality Plan, which shall be subject to continuous monitoring and evaluation by the Corporate Responsibility and Governance Committee and by the Board of Directors.

In particular, indicate whether the Appointments and Compensation Committee has established procedures so that selection processes do not suffer from implicit bias preventing the selection of female Directors and consciously seek candidates that meet the required profile:

YES  NO

#### Identify the main procedures

As stated, the measures put in place by the Company are aimed at actively promoting the selection of female Directors and their incorporation onto the Board of Directors, on the terms provided in Recommendation 15 of the Conthe Code and in accordance with Article 16.1 of the Board Regulations.

**B.1.28.** Indicate whether there are any formal procedures for granting proxies to vote at Board meetings. If so, give brief details:

Each Director may grant a proxy to another Director, in writing and specifically for each meeting, to represent him/her and vote on his/her behalf at the meetings of the Board of Directors. This is provided in Article 21 of the Corporate Bylaws.

Where a Director cannot, with just cause, attend the Board meeting(s) to which he has been called, he must give instructions to the Director that is to represent him, procuring that he is represented by a Director of the same type, as provided in Article 28.2 b) of the Board Regulations.

**B.1.29.** Indicate the number of Board meetings held during the year. Also indicate, as appropriate, how often the Board met without the Chairman's attendance:

Number of Board meetings	11
Number of Board meetings not attended by the Chairman	0

Indicate how many meetings of the various Board Committees were held during the year:

Number of Executive or Delegated Committee meetings	—
Number of Audit Committee meetings	10
Number of Appointments and Compensation Committee meetings	11
Number of Appointments Committee meetings	—
Number of Compensation Committee meetings	—

**B.1.30.** Indicate how many Board meetings held during the year were not attended by all members. Proxies granted with no specific instructions will be treated as absences:

Number of Director absences during the year	7
Absences as a percentage of total number of votes during the year	6%

**B.1.31.** Indicate whether the individual and consolidated financial statements submitted for approval by the Board are certified beforehand:

YES  NO

Indicate, as appropriate, the person(s) who certified the Company's individual and consolidated financial statements for their preparation by the Board:

Name	Position

**B.1.32.** Explain the mechanisms, if any, established by the Board of Directors to prevent the individual and consolidated financial statements prepared by it from being submitted at the Shareholders' Meeting with a qualified auditors' report:

The Board Regulations expressly establish that the Company's Board of Directors will formulate the definitive financial statements, procuring that they do not give rise to any qualifications by the auditor. Nevertheless, where the Board considers that it must maintain its policy, it will publicly explain the substance and scope of the discrepancy.

In this regard, the Audit Committee plays a particularly important role, as it continuously monitors the process of preparing the economic and financial information sent to the market supervisory bodies, thereby increasing the likelihood that there will be no qualifications in the annual auditors' reports.

Since the formation of the Company in 1985, it has not been subject to any qualifications in the audits of its financial statements. This demonstrates the utmost accuracy, reliability and sufficiency of the financial statements of the Company and its consolidated Group since its formation, guaranteeing at all times the maximum transparency in its reporting.

**B.1.33. Is the Board Secretary a Director?**

YES  NO

**B.1.34. Explain the procedures for appointment and removal of the Board Secretary, indicating whether his/her appointment and removal were reported to the Appointments Committee and approved by the plenary session of the Board.**

**Procedure for appointment and removal**

As provided in Article 10.4 of the Board Regulations, the Corporate Responsibility and Governance Committee will report on proposals for the appointment and removal of the Board Secretary, prior to their submission to the Board.

The Secretary of the Board of Directors is Mr. Rafael García de Diego Barber, a member of the Madrid Bar Association. He is not a Company Director and has served as Secretary since May 4, 1995, for which reason the Committee could not report on his appointment, since it did not exist at that time.

	YES	NO
Does the Appointments Committee report on the appointment?	X	
Does the Appointments Committee report on removal?	X	
Does the plenary session of the Board approve the appointment?	X	
Does the plenary session of the Board approve the removal?	X	

Is the Board Secretary specifically tasked with monitoring good governance recommendations?

YES  NO

**Comments**

As provided in Article 26 e) of the Bylaws and Article 10.3 b) of the Board Regulations, the duties of the Secretary of the Board of Directors include ensuring compliance by the Board of Directors and its Committees with the Corporate Bylaws, the Shareholders' Meeting Regulations, the Board Regulations, and other corporate governance rules at the Company.

In addition, Article 26 f) of the Corporate Bylaws and the corresponding Article 10.3 c) of the Board Regulations provide that the Secretary of the Board of Directors is responsible for *«ensuring that the Company's corporate governance rules and the actions of the Board of Directors are in line with the good corporate governance recommendations in force from time to time»*.

**B.1.35.** Indicate the mechanisms, if any, established by the Company to preserve the independence of the auditors, of financial analysts, of investment banks, and of rating agencies:

The Audit Committee is the body within the Board of Directors that is responsible for the relationship with external auditors. In this regard, the Audit Committee assists the Board of Directors in monitoring the independence of the Company's external auditor.

Pursuant to the power contemplated in Article 23.2 of the Corporate Bylaws, Article 14.3 b) of the Board Regulations, in relation to the independence of external auditors, tasks the Audit Committee with establishing procedures to ensure the independence and professionalism of the external auditors and receiving information regarding matters that might jeopardize their independence and professionalism.

In this regard, the Audit Committee must ensure that the Company (i) discloses any change of auditor to the CNMV as a material event and, if applicable, any disagreements with the outgoing auditor; and (ii) complies with the rules in force regarding the provision of non-audit services, limits on concentration of the auditor's business and, in general, all other rules established to safeguard the independence of the auditor. In the event of resignation of the auditor, the Audit Committee must examine the underlying circumstances.

Moreover, Article 37 of the Board Regulations imposes the duty on the Board to refrain from engaging audit firms whose envisaged fees for all items exceed 10% of their total revenues in the preceding year.

In addition, Article 37 of the Board Regulations imposes the obligation on the Board of Directors to provide yearly information on the overall fees paid by the Company to the audit firm for non-audit services. The Company frequently makes all manner of presentations to financial analysts and investment banks to report on the key economic and financial highlights of the Group, and on its business performance.

These presentations are regularly attended by the most prominent industry professionals and experts. After these presentations, all participants are offered the opportunity to be included on a list of entities that periodically receive the most relevant Company information of interest to them.

All presentations to analysts are sent to the Spanish CNMV beforehand so that they may be consulted by the markets on its website. The presentations are also posted immediately on the Company website.

The main purpose of the Investor Relations Department, which reports to the Company's Directorate-General of Administration and Finance, is to act as a channel for communications with financial professionals and institutional investors, and to handle their inquiries.

**B.1.36.** Indicate whether the Company changed external auditors in the year. If so, identify the new and outgoing auditors:

YES  NO

**Outgoing auditor**

**New auditor**

--	--

If there were any disagreements with the outgoing auditor, explain the substance thereof:

YES  NO

**Explanation of disagreements**

**B.1.37.** Indicate whether the audit firm performs any non-audit work for the Company and/or its Group, and if so, state the amount of fees received for such work and the percentage they represent of the fees billed to the Company and/or its Group:

YES  NO

	Sociedad	Grupo	Total
Fees for non-audit work (€ thousand)	-	110	110
Fees for non-audit work / Total fees billed by audit firm (as a %)	0%	48%	48%

**B.1.38.** Indicate whether the audit report on the financial statements for the preceding year contains any reservations or qualifications. If so, state the reasons given by the Chairman of the Audit Committee to explain the substance and scope of such reservations or qualifications

YES  NO

**Explanation**

**B.1.39.** Indicate the number of consecutive years the current audit firm has audited the financial statements of the Company and/or its Group. Indicate the number of years the current audit firm has audited the Company's financial statements as a percentage of the total number of years during which the Company's financial statements have been audited:

	Company	Group
Number of consecutive years	6	6
Number of years audited by current audit firm/ Number of years the company has been audited (as a %)	23.1%	54.5%

**B.1.40.** Indicate any holdings, as disclosed to the Company, owned by the members of the Company's Board of Directors in the capital of entities engaging in business of a kind identical, similar or complementary to the business constituting the corporate purpose of the Company or of its Group. Also indicate the offices they hold or the functions they perform at these companies:

Name of Director	Name of company in which shares are held	% Holding	Office or functions
Luis M <sup>a</sup> Atienza Serna	CFO of REN-REDES ENERGÉTICAS NACIONAIS, SGPS	—	Individual representative of the corporate Director Red Eléctrica Corporación, S.A., on the Board of Directors of Portuguese company REN-REDES ENERGÉTICAS NACIONAIS, SGPS
Rui Manuel Janes Cartaxo	CFO of REN-REDES ENERGÉTICAS NACIONAIS, SGPS	0.0036 %	Chairman and CEO of REN-REDES ENERGÉTICAS NACIONAIS, SGPS

**B.1.41.** Indicate whether there is a procedure to allow Directors to seek external professional advice? If so, give details:

YES  NO

#### Details of the procedure

There is a specific procedure in place at the Company to allow Directors to seek external advice.

In order to receive assistance in exercising their functions, Article 26 of the Board Regulations establishes that External Directors may request that the Board of Directors engage legal, accounting, financial or other expert advisers, at the expense of the Company.

The engagement must refer to specific problems of a certain scale and complexity arising in the discharge of their office.

The engagement request must be addressed to the Chairman. The request may be rejected by the Board of Directors if it transpires or can be inferred that:

- a) it is not necessary for the proper performance of the functions entrusted to the Directors;
- b) the cost thereof is not reasonable in view of the significance of the problem and the assets and revenues of the Company; or
- c) the technical assistance sought may be adequately provided by Company experts or technical personnel, or has been entrusted to other external experts.

Articles 13.5 and 15.7 of the Board Regulations provide that the Audit Committee and the Corporate Responsibility and Governance Committee may propose that the Board of Directors seek independent professional advice.

Furthermore, those Committees may access any type of Company information or documentation necessary for the better performance of their duties, pursuant to the provisions of the aforementioned Articles of the Board Regulations.

**B.1.42.** Indicate whether there is a procedure to ensure that Directors have the necessary information in order to prepare for meetings of the management bodies sufficiently in advance. If so, give details:

YES  NO

#### Details of the procedure

Board meetings are called at least six (6) days in advance and all relevant information is sent out with the call notice. The call notice always includes the agenda for the meeting and, in general, except where it is not possible, the relevant information, duly summarized and prepared.

Notwithstanding the foregoing, Article 17.3 of the Board Regulations establishes that the call notice for Board meetings will be sent at least three (3) days prior to the date of the meeting. As an exception and for reasons of urgency, the Board may be called by telephone and the advance notice period will not apply where the Chairman deems that the circumstances justify it. The reasons of urgency will be explained in the Minutes of the meeting.



Article 25 of the Board Regulations provides that Directors have the broadest rights to be informed of and to inspect any aspect of the Company. In this regard, Directors may, at any time, examine the books, registers, documents and other background information on corporate transactions and may even inspect all Company facilities. The right to information extends to subsidiary companies, both domestic and foreign.

In accordance with Article 25 of the Board Regulations and so as not to disturb the ordinary management of the Company, the exercise of the right to information will be channeled through the Chairman of the Board of Directors, who will handle all requests from Directors, providing the information directly to them. The Chairman will also offer the appropriate contact persons at the relevant level within the organization or make arrangements to allow Directors to conduct the desired examination and inspection *in situ*.

Article 25 of the Board Regulations provides that the Chairman of the Company may restrict access to certain information on an exceptional and temporary basis, informing the Board of Directors of this decision at its next meeting.

Both the Audit Committee and the Corporate Responsibility and Governance Committee may access any kind of Company information or documentation that they may need for the better performance of their duties, as indicated in section B.1.41 above.

**B.1.43.** Indicate whether the Company has established rules requiring Directors to report on and, as the case may be, resign in cases that could harm the credit and reputation of the Company. If so, give details:

YES  NO

#### Details of rules

Article 30 of the Board Regulations provides, among the disclosure obligations of Directors, that Directors must inform the Company of all judicial, administrative and other claims that by reason of their significance could harm the credit and reputation of the Company and, in particular, of any criminal proceedings in which they appear as an accused party, and of subsequent progress in the case.

Furthermore, pursuant to Article 22.2 f) of the Board Regulations, Directors must tender their resignation to the Board of Directors and, where the Board deems it appropriate, formally resign where their continued presence on the Board may jeopardize the interests of the Company, as envisaged above, and where the Board deems this to be the case with the affirmative vote of two-thirds of its members.

If a Director is indicted or a decision is rendered to bring him to trial for any of the crimes referred to in Article 213 of the Corporate Enterprises Law, the Board shall review the matter as soon as possible and, in light of the specific circumstances, shall decide, as provided for in the preceding paragraph, whether or not it is appropriate for the Director to remain in office. All of the foregoing will be reported on in the Annual Corporate Governance Report.

**B.1.44.** Indicate whether any member of the Board of Directors has informed the Company that he has been indicted or that a decision has been rendered to bring him to trial for any of the crimes stated in Article 213 of the Corporate Enterprises Law:

YES  NO

Name of Director

Criminal proceeding

Comments



Indicate whether the Board of Directors has reviewed the case. If yes, give a reasoned explanation of the decision adopted as to whether or not it is appropriate for the Director to remain in office:

YES  NO

**Decision adopted**

**Reasoned explanation**

## B.2. Committees of the Board of Directors

**B.2.1.** List all of the Committees of the Board of Directors and their members:

### EXECUTIVE OR DELEGATED COMMITTEE

Name	Position	Type

### AUDIT COMMITTEE

Name	Position	Type
Arantza Mendizábal Gorostiaga	Chairwoman	Independent
José Folgado Blanco	Member	Independent
María Jesús Alvarez González	Member	Nominee

### APPOINTMENTS AND COMPENSATION COMMITTEE

Name	Position	Type
Antonio Garamendi Lecanda	Chairman	Independent
María Ángeles Amador Millán	Member	Independent
Luis María Atienza Serna	Member	Executive
Manuel Alves Torres	Member	Nominee

### APPOINTMENTS COMMITTEE

Name	Position	Type

### COMPENSATION COMMITTEE

Name	Position	Type

### \_\_\_\_\_ COMMITTEE

Name	Position	Type

#### B.2.2. State whether the Audit Committee performs the following functions:

	YES	NO
Supervises the preparation and integrity of the financial information relating to the Company and, as the case may be, the Group, reviewing compliance with legal provisions, the appropriate definition of the consolidated group, and the correct application of accounting principles.	X	
Reviews internal control and risk management systems on a regular basis, so that the main risks are adequately identified, managed and disclosed.	X	
Ensures the independence and efficacy of the internal audit function; proposes the selection, appointment, reappointment and removal of the head of the internal audit service; proposes the budget for this service; receives regular reports on its activities; and verifies that senior management is acting on the conclusions and recommendations contained in its reports.	X	
Establishes and supervises a mechanism to enable staff to report, on a confidential and, if appropriate, anonymous basis, any potentially significant irregularities, particularly financial or accounting irregularities, they may detect at the Company.	X	
Makes recommendations to the Board for the selection, appointment, reappointment and removal of the external auditor, and the terms and conditions of its engagement.	X	
Receives regular information from the external auditor on the progress and findings of the audit plan, and verifies that senior management is acting on its recommendations.	X	
Ensures the independence of the external auditor.	X	
In the case of groups, the group auditor should be encouraged to take responsibility for auditing all the companies in the Group.	X	

#### B.2.3. Describe the rules of organization and functioning, and the responsibilities attributed to each of the Board Committees:

##### I. AUDIT COMMITTEE

###### a) Background

At the meeting held on November 18, 2003, the Board of Directors of Red Eléctrica created the Audit Committee to replace the former Audit and Compliance Committee, pursuant to the provisions of Article 23 of the Corporate Bylaws and Chapter V, Articles 15 and 16 of the Board Regulations, approved at that meeting. The foregoing was also consistent with the provisions of Article 47 of Law 44/2002 of November 22, 2002 on Measures to Reform the Financial System.

Specifically, the Audit Committee was created by a resolution adopted by the Board of Directors of Red Eléctrica on November 30, 1999, under the name of the Audit and Compliance Committee. This Committee was created as part of the process to adapt the Company's governance rules to the new situation resulting from the tender offer made by the State-Owned Industrial Holdings Company (SEPI) and from the Company's listing on the stock markets on July 7, 1999.

The Annual Shareholders' Meeting of the Company on May 31, 2007, approved an amendment to the Corporate Bylaws to bring them into line with the Single Text of Corporate Governance Recommendations, known as the Unified Good Governance Code, approved by the CNMV under a Decision dated May 19, 2006.

The Annual Shareholders' Meeting amended Article 23 of the Corporate Bylaws to bring it into line with Recommendation 22 of the Unified Good Governance Code, regarding the composition of the Audit Committee, and changed the name of the Audit Committee from Audit Commission to Audit Committee, more in keeping with commercial practices.

The Shareholders' Meeting held on April 13, 2011, approved an amendment to the Corporate Bylaws and to the Shareholders' Meeting Regulations in order to adapt them to the new legal requirements established in Law 12/2010, of June 30, 2010 (basically affecting the composition, structure and functions of the Audit Committee) and Legislative Royal Decree 1/2010, of July 2, 2010, approving the Revised Corporate Enterprises Law (fully repealing the Corporations Law and partially repealing the Securities Market Law).

All of the approved amendments have been notified to the CNMV and registered at the Mercantile Registry.

#### b) Composition

Article 13 of the Board Regulations provides that the Committee will be comprised of a minimum of three (3) and a maximum of five (5) members, as determined by the Board, the majority being External Directors and appointed by the Board of Directors, and reasonably endeavoring to reflect the composition of the Board.

Following a report by the Corporate Responsibility and Governance Committee, the Board meeting held on July 27, 2011, approved the reappointment for a period of 3 years of two of its members (Ms. Arantza Mendizábal Gorostiaga and Ms. María Jesús Álvarez González) and appointed Mr. José Folgado Blanco as a new member for a period of 3 years following the expiration of the term for which Mr. Francisco Javier Salas Collantes was appointed.

As already mentioned, the Directors on the Audit Committee are particularly qualified to hold their positions, with lengthy professional experience in positions of the highest responsibility outside the RED ELÉCTRICA Group, in functions similar to those entrusted to the Committee. A brief description is given below of each member's professional career (further details are provided in Section B.1.3 above):

- ◆ Ms. Arantza Mendizábal Gorostiaga holds a Doctorate in Economics and is Professor of Applied Economics at the Faculty of Economics of Universidad del País Vasco. She has been a distinguished researcher in the areas of industrial and technological policy, an MP member of the Economy and Finance Committee, the Budget Committee and Spokeswoman for the Industry, Trade and Tourism Committee of the Lower House of Parliament. In addition to her duties as Professor, she is currently the Director of the European Documentation Center of Universidad del País Vasco. She was appointed Chairwoman of the Audit Committee on July 20, 2009, for a period of three years.
- ◆ Ms. María Jesús Álvarez González holds degrees in Law, and in Economics and Business Studies. She has

held various executive positions within SEPI and engaged in various activities in the banking and industrial sectors. She has also been a member of the board of directors of Enusa Industrias Avanzadas, S.A., Equipos Nucleares, S.A., Clínica Castelló, S.A., Indra Sistemas, S.A., Infoinvest, S.A., Infoleasing, S.A., Empresa Nacional de Residuos Radioactivos, S.A. (ENRESA), Aluminio Español, S.A. and Agencia Efe, S.A. She is currently the Economic and Financial Director of SEPI, a member of the Management Committee of SEPI and a member of the Board of Trustees of Fundación SEPI and of Fundación Laboral SEPI.

- ◆ Mr. José Folgado Blanco holds a Degree in Economics (and final-year award with special distinction) and a Doctorate in Economics, Universidad Autónoma de Madrid. He has been Head of the Economics Department of the CEOE, Member of the Economic and Social Board representing business organizations and Secretary of State for Budgets and Expenditure. Ministry of Economy and Finance, since May 1996, Secretary of State for Economy, Energy and Small and Medium-Sized Enterprises of the Ministry of Economy, since April 2000, Secretary of State for Energy, Industrial Development and Small and Medium-Sized Enterprises of the Ministry of Economy, since July 2002, Parliamentary representative of the province of Zamora and Deputy Chairman of the Economy and Finance Committee, since March 2004. He is currently a Tenured Professor of Public Finance and Tax Systems at Universidad Autónoma de Madrid (on extended leave of absence), the Mayor of Tres Cantos (Madrid) since June 2007 and a Member of the Social Board of Universidad Autónoma de Madrid.

The members of the Committee hold office for a term of not more than three years, may be reappointed indefinitely and stand down on expiration of that term, when they cease to be Directors, or when so resolved by the Board of Directors, in the latter case following a report by the Corporate Responsibility Governance Committee. The Chairman of the Committee is an Independent Director elected by its members and the Committee Secretary is the Secretary of the Board of Directors. The Chairman must be substituted every three years and may be reappointed after one year has elapsed since he left office. Committee members are appointed and removed by the Board of Directors at the proposal of the Board Chairman following a report from the Corporate Responsibility and Governance Committee.

### c) Organization and functioning

The Audit Committee meets at least once every quarter and any time it is called by its Chairman or two of its members so request, and whenever the Board or its Chairman requests that it issue a report. The Committee met ten (10) times in 2011.

Article 13.4 of the Board Regulations establishes that meetings may be called, and the associated documentation sent, by telematic means that guarantee due security and confidentiality for the call notice and the related documentation.

The call notice, including the agenda, will be sent by the Committee Chairman or Secretary to each of its members at least three days in advance of the date scheduled for the meeting, unless the meeting needs to be called sooner for reasons of urgency.

Article 13.4 also allows Committee meetings to be held for reasons of urgency and on an exceptional basis by conference call, videoconferencing or any other remote means of communication that enables them to be held, provided that all Committee members can have access thereto.

The Committee may be constituted with the attendance of the majority of its members and will adopt decisions or recommendations by a majority vote, which decisions or recommendations must be recorded in the Minutes at the end of the meeting. Members of the management team or Company personnel who are

requested by the Chairman of the Audit Committee will be obliged to attend Committee meetings and must provide assistance and allow access to any information they have, in relation to the matters discussed.

In order to better perform its functions, the Committee may propose to the Board of Directors that advice be sought from independent professionals and may access any type of Company information or documentation it may require.

#### d) Powers

The basic powers of the Committee are set out in Article 14 of the Board Regulations and can be summarized in six major groups: i) economic and financial information; ii) internal control and risk management systems; iii) external auditors; iv) compliance with legal provisions and internal rules; v) Company shareholders; and vi) other general powers.

The Committee, composed entirely of External Directors, formally met with the external auditor on various occasions in 2011, whenever it deemed it appropriate for the better performance of its functions, passing on the questions, clarification and comments it saw fit.

Its remit includes most notably the procedure for fulfilling the functions assigned in relation to the financial statements. Since its creation in 1999, the Audit and Compliance Committee has been responsible for reviewing the Company's financial statements, monitoring compliance with legal requirements and the correct application of generally accepted accounting principles, and reporting on any amendments to the accounting principles and methods proposed by Company Management.

When the Committee became the Audit Committee in November 2003, with the functions and responsibilities established by law and the Bylaws, it also assumed responsibility for approving the accounting principles and methods to be used in preparing the Company's financial statements and those of its consolidated Group, and for verifying their accuracy, reliability and sufficiency.

Also notable is the specific procedure for supervision by the Committee of any financial information sent on a periodic or *ad hoc* basis to the market supervisory bodies. The Committee is also responsible for ensuring that Company's financial documentation complies with legal accounting standards and, in particular, with any applicable EU recommendations and obligations on bookkeeping by electric utilities.

All of the foregoing leads to more direct control over the preparation of the Company's economic and financial information. Since this control is carried out by a collective body consisting of Directors with the highest professional qualifications in relation to the matters falling under the Committee's jurisdiction (as can be seen from the professional careers of Directors as described above), the accounting principles of reliability, certainty, accuracy and sufficiency are reinforced, as is the transparency of the process for the preparation of corporate economic information.

The Regulations of the Board of Directors approved on January 28, 2010 gave the Audit Committee the following new responsibilities:

- ◆ To report previously to the Board of Directors on material transactions or operations for the financing of the companies of the Red Eléctrica Group.
- ◆ To report to the Board of Directors on related-party transactions, as defined in the legislation in force from time to time, that are material or fall outside the ordinary course of business of the Company, that must be reported obligatorily to the securities markets pursuant to the aforementioned legislation, and that require the Board's approval.

## II. CORPORATE RESPONSIBILITY AND GOVERNANCE COMMITTEE

### a) Background

Following the listing of Red Eléctrica on the stock exchange in 1999, an Appointments Committee was created within the Board of Directors and began to perform functions as regards the appointment of Directors and senior executives. Following the recommendations of the Aldama Report of November 18, 2003, the Company's Board of Directors converted this Committee into the Appointments and Compensation Committee. The Committee's initial powers regarding appointments were expanded and it assumed new functions in relation to the compensation of the Board of Directors and the management team of the Company and of its Group.

In accordance with corporate governance recommendations and particularly those set out in the Conthe Code, pursuant to the amendments made by the Shareholders' Meeting held on May 31, 2007, the Company's Board of Directors changed the name of the Committee in 2007 to the Appointments, Compensation and Corporate Governance Committee and extended its powers. Particularly noteworthy among the powers expressly attributed to this Committee are those relating to corporate governance.

At the meeting held on January 28, 2010, the Board of Directors amended the Board Regulations by renaming the Appointments, Compensation and Corporate Governance Committee as the Corporate Responsibility and Governance Committee. The change of name of this Committee was accompanied by broad powers granted in the area of corporate responsibility.

### b) Structure

Article 24.2 of the Corporate Bylaws and Article 15 and 16 of the Board Regulations govern the structure, composition and functions of the Corporate Responsibility and Governance Committee.

The Committee must consider the suggestions made by the Chairman, the members of the Board, and Company executives or shareholders in matters affecting the appointment of Directors, including Managing or Executive Directors, and compliance with corporate governance principles, the Corporate Bylaws and the Board Regulations.

The Committee meets as often as is appropriate for the sound performance of its functions. In any event, the Committee must meet at least once every quarter, whenever called by its Chairman or so requested by two of its members, and whenever the Board of Directors or its Chairman requests that a report be issued or proposals be adopted.

As in the case of the Audit Committee, Article 15.5 of the Regulations of the Board of Directors provides, for the first time, that meetings may be called, and the associated documentation sent, by telematic means that guarantee due security and confidentiality for the call notice and the related documentation.

The call notice, which must include the agenda, is sent by the Committee Chairman or Secretary to each Committee member at least three days in advance of the date scheduled for the meeting, unless the meeting needs to be held sooner for reasons of urgency.

Also with respect to this Committee, Article 15.5 of the Board Regulations allows Committee meetings to be held for reasons of urgency and on an exceptional basis by conference call, videoconferencing or any other remote means of communication that enables them to be held, provided that all Committee members can have access thereto.

The Committee met eleven (11) times in 2011.

The Committee may be constituted with the attendance of the majority of its members and adopt decisions or recommendations by a majority vote, which decisions or recommendations must be recorded in the Minutes at the end of the meeting. In order to better perform its functions, the Committee may propose to the Board of Directors that advice be sought from independent professionals and may access any type of Company information or documentation it may require to perform its functions.

Article 15 of the Board Regulations provides that the Corporate Responsibility and Governance Committee will be comprised of a minimum of three and a maximum of five members, as determined by the Board, with a majority of External Directors and at least half of its members must be Independent Directors. The Chairman of the Committee is an Independent Director elected by its members and the Committee Secretary is the Secretary of the Board of Directors.

Committee members are appointed and removed by the Board of Directors at the proposal of the Board Chairman following a report from the Corporate Responsibility and Governance Committee. Committee members hold office for a maximum period of three years, may be reappointed and stand down when they cease to be Directors or when so resolved by the Board of Directors, following a report by the Corporate Responsibility and Governance Committee. The Chairman must be substituted every three years and may be reappointed after one year has elapsed since he vacated office, as in the case of the Audit Committee.

### c) Composition

Following a report by the Corporate Responsibility and Governance Committee, the Board meeting held on July 27, 2011, approved the reappointment of two of its members (Mr. Luis María Atienza Serna and Mr. Manuel Alves Torres) for a period of 3 years.

At 2011 year-end and at the date of approval of this Report, the Corporate Responsibility and Governance Committee was composed of four Directors: three External Directors and one Executive Director. Two of the External Directors were Independent Directors and one of them was the Chairman of the Committee, who has the casting vote in the event of a tie.

At 2011 year-end and at the date of approval of this Report, the composition of the Committee was as follows:

Director	Position	Type of Director
Antonio Garamendi Lecanda	Chairman	Independent
María Ángeles Amador Millán	Member	Independent
Luis María Atienza Serna	Member	Executive
Manuel Alves Torres	Member	Nominee

The Chairman of the Committee, who must be an Independent Director, is elected by its members and the Committee Secretary is the Secretary of the Board of Directors, Mr. Rafael García de Diego Barber. Committee members are appointed and removed by the Board of Directors at the proposal of the Board Chairman.



Antonio Garamendi Lecanda has completed the maximum term of 12 years as an Independent Director of RED ELÉCTRICA. According to the provisions of Article 7.2 c) of the Board Regulations, the Unified Good Governance Code and international corporate governance best practices, this is the maximum period for which he may be treated as an Independent Director and, therefore, if a proposal is made for his reappointment at the next Annual Shareholders' Meeting, he will be classed the category of "other External Directors."

If the Annual Shareholders' Meeting approves the reappointment of Mr. Garamendi as a Company Director, he must immediately be replaced as Chairman of the Corporate Responsibility and Governance Committee, a position which must be occupied by an Independent Director, in accordance with the Corporate Bylaws and the Board Regulations.

#### d) Powers

The basic responsibilities of the Corporate Responsibility and Governance Committee are regulated in Article 24 of the Corporate Bylaws and Articles 15 and 16 of the Board Regulations.

Pursuant to the authorization contained in Article 24.2 of the Corporate Bylaws, the Corporate Responsibility and Governance Committee has basic responsibilities concerning appointments and removals, compensation, fulfillment of Director duties, corporate governance rules and other generic functions.

The Board Regulations approved on January 28, 2010 established a specific section on the powers of this Committee in the area of corporate responsibility.

#### **B.2.4.** Indicate the advisory and consultative powers and any delegated powers held by each of the Committees:

Name of Committee: AUDIT

#### Brief description

The basic responsibilities of this Committee, pursuant to Article 23 of the Corporate Bylaws, are as follows:

- (i) To report at Shareholders' Meetings on matters falling within its jurisdiction which are raised in the course of such Meetings.
- (ii) To supervise the efficacy of the Company's internal control, any internal audit, and risk management systems, as well as discuss with the auditors any significant weaknesses of the internal control system detected in the course of the audit.
- (iii) To supervise the process of preparing and filing regulated financial information.
- (iv) To propose to the Board of Directors the appointment of auditors for submission to the Shareholders' Meeting.
- (v) To duly engage with the auditors in order to receive information on any issues that may jeopardize their independence, for their examination by the Committee, and any other issues relating to the audit process, as well as other communications provided for in audit legislation and audit standards. In any case, they must receive each year from the auditors written confirmation of their independence from the Company or from entities related to the Company directly or indirectly, as well as information on additional services of any kind provided to such entities by those auditors or by persons or entities related to those auditors in accordance with the provisions of the legislation in force.

- (vi) Before the auditors' report is issued, to issue a report each year expressing an opinion on the independence of the auditors or audit firms. This report must, in any case, make a pronouncement on the provision of the additional services referred to in the preceding letter.
- (vii) Any other powers attributed to it by the Board, whether generally in the Board Regulations or by specific assignment.

The above basic responsibilities are detailed in Article 14 of the Board Regulations, which establishes the following:

**As regards economic and financial information:**

- a) To approve the accounting principles and methods to be used in the preparation of the financial statements of the Company and of its consolidated Group, and to verify their accuracy, reliability and sufficiency.
- b) To supervise the preparation and integrity of the financial information of the Company and, as appropriate, of the Group, ensuring that legislative requirements are taken into account, the consolidated group is adequately defined, and the applicable accounting principles and methods are correctly applied.
- c) To review and report to the Board in advance on the economic and financial information the Company must disclose and send to the market supervisory bodies. The Committee must ensure that any interim financial statements are prepared using the same accounting methods as annual financial statements and, where it sees fit, it may ask the external auditor to conduct a limited review.
- d) To report previously to the Board of Directors on material transactions or operations for the financing of companies in the Red Eléctrica Group.

**As regards internal control and risk management systems:**

- a) To approve the Company's internal control procedures in the areas of expenditure and investment, making the appropriate amendments, as the case may be.
- b) To supervise the internal audit function, which will ensure the sound functioning of the internal reporting and control systems and must address requests for information from the Audit Committee in the performance of its functions.
- c) To ensure the independence and efficacy of the internal audit function; to supervise and control the process for selection, appointment, reappointment and removal of the head of the internal audit function, and its action plans; to supervise and control the media and resources assigned to the internal audit function, including its budget; to receive periodic information on its activities; and to verify that senior management of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company is acting on the conclusions and recommendations of its reports.

The head of internal audit must present an annual work program to the Committee, directly report on any incidents arising during its implementation and submit an activities report at the end of each year.

- d) To periodically supervise the internal control and risk management systems, so that the main risks are identified, managed and appropriately disclosed.

- e) To supervise the procedure established by the Board to enable staff to report any potentially significant irregularities, particularly financial or accounting irregularities, they may detect at the Company.

The persons in charge of internal control must inform the Committee when they detect irregularities or breaches that may significantly impact or harm the net worth, earnings or image of the Company or of its Group.

**As regards the external auditor:**

- a) To propose the appointment of external auditors to the Board of Directors for submission to the Shareholders' Meeting, procuring that it be the same audit firm for all Group companies, and the terms of the audit contract, the scope of the professional mandate and the renewal or termination thereof.
- b) To establish procedures to ensure the independence and professionalism of the external auditors and to receive information regarding matters that might jeopardize their independence and professionalism. To that end:
  - i) It will ensure that any change of auditor and, if applicable, any disagreements with the outgoing auditor are disclosed by the Company to the CNMV as material events.
  - ii) It will ensure that the Company, within the scope of its responsibilities, complies with the rules in force regarding the provision of non-audit services, limits on concentration of the auditor's business and, in general, all other rules established to safeguard the independence of the auditor.
  - iii) The Committee will investigate the circumstances giving rise to the resignation of any external auditor.
- c) To receive any relevant information relating to the Audit Plan, the process and results of its implementation, as well as any other information provided for in the accounting standards.
- d) To act as a communication channel between the Board and the external auditor; to evaluate the results of each audit and verify that senior management of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company acts on its recommendations, mediating in the event of discrepancies between the former and the latter in relation to the principles and methods applicable in the preparation of the financial statements.
- e) To supervise compliance with the audit contract, seeking to ensure that the principal contents of the audit report are drafted clearly and precisely.
- f) To be informed of the material situations detected by the external auditor, in the same way as information from the internal control systems is received, which may adversely affect the net worth, earnings, or image of the Group.
- g) To periodically request from the external auditors, and at least once a year, an evaluation of the quality of the Group's internal control procedures.

**As regards compliance with legal provisions and internal regulations:**

- a) To supervise compliance with the Internal Code of Conduct on the Securities Market and with the functions of the Oversight Body provided in the Code, reporting periodically to the Corporate Responsibility and Governance Committee on the degree of compliance with the Code and on any incidents that occur.
- b) To resolve doubts and conflicts raised by parties affected by the Internal Code of Conduct on the Securities Market and submitted to the Committee by the Oversight Body over compliance with the Code.

- c) To annually evaluate compliance with the rules of the Internal Code of Conduct on the Securities Market and, as the case may be, adopt the appropriate measures for its optimum implementation and improvement; in this connection, the Committee is also responsible for submitting to the Corporate Responsibility and Governance Committee for referral to the Board of Directors any proposed amendments to the Code it may consider necessary.
- d) To review compliance with the actions and measures resulting from reports or inspections by the supervisory and control authorities of the securities market.

**As regards the Company's shareholders:**

- a) To entertain and, as appropriate, respond to the initiatives, suggestions or complaints that may be made by shareholders in respect of the scope of the Committee's functions.
- b) To report, as appropriate, to the Shareholders' Meeting on issues raised at the meeting by shareholders in relation to matters falling within its jurisdiction.

**Other:**

- a) To keep the Board of Directors duly informed of its activities and to prepare an annual report to be included in the Annual Corporate Governance Report and an Action Plan for each year.
- b) To report to the Board on extraordinary investment transactions when so requested by the Board and, in all cases, on transactions for the creation or acquisition of holdings in special-purpose vehicles or entities domiciled in countries or territories that are considered tax havens, as well as any transactions and operations that could impair the transparency of the Group.
- c) To report to the Board in advance on related-party transactions requiring authorization from the Board of Directors, as provided in Article 5.6 c) of the Regulations.  
To also report to the Board on other related-party transactions not requiring Board authorization but which the Committee considers the Board should be made aware of.
- d) To propose and report on any other matter related to the foregoing that may be requested by the Chairman or by the Board of Directors.
- e) Any other powers attributed to it by the Board.

**Name of Committee:** CORPORATE RESPONSIBILITY AND GOVERNANCE

**Brief description**

The basic responsibilities of this Committee, pursuant to Article 24 of the Corporate Bylaws, are as follows:

- a) To report on (and, in the case of Independent Directors, make) any proposals to be submitted by the Board of Directors to the Shareholders' Meeting for the appointment or removal of Directors, including in cases of co-optation.
- b) To propose the compensation policy for Directors and senior executives to the Board of Directors and ensure its observance.
- c) To assume such reporting, supervising and proposing functions in the area of corporate governance as may be determined by the Board of Directors, as long as no *ad hoc* Committee has been set up for those functions.

The above basic responsibilities are detailed in Article 16 of the Board Regulations, which establishes the following:

**In relation to appointments and removals:**

- a) To report in advance on (and, in the case of Independent Directors, make) any proposals to be submitted by the Board of Directors to the Shareholders' Meeting for the appointment or removal of Directors, including in cases of co-optation.
- b) To report, prior to their submission to the Board of Directors, on proposals for the appointment or removal of the Secretary and the Deputy Secretary of the Board of Directors.
- c) To propose the system for selecting Independent Directors to the Board of Directors.
- d) To ensure that the candidates for filling a vacant directorship meet all of the requirements imposed in the legal provisions and in these Regulations.
- e) To evaluate the skills, knowledge and experience required on the Board and consequently define the functions and skills required of the candidates for each vacancy.
- f) To evaluate the time and dedication necessary for Directors to be able to perform their duties with due quality and efficiency, evaluating for these purposes whether their position as a Director is compatible with membership on other management bodies of companies.
- g) To report on such appointments and removals of senior executives of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company as the Chairman may propose to the Board of Directors.
- h) To examine or organize, in the manner deemed appropriate, the process for succession of the Chairman and, as appropriate, to make proposals to the Board so the handover takes place in a planned and orderly fashion.
- i) To ensure that gender diversity is taken into account when filling vacancies.
- j) To consult with the Chairman, particularly when dealing with matters relating to Executive Directors.

**In relation to compensation:**

- a) To propose to the Board:
  - the compensation policy for the Directors and senior executives of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company;
  - the individual compensation and other contractual conditions of Executive Directors;
  - the basic terms and conditions of the contracts of senior executives of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company.
- b) To consult with the Chairman of the Company, particularly when dealing with matters relating to Executive Directors and senior executives of the Company and of Red Eléctrica de España, S.A. Sole-Shareholder Company.
- c) To ensure compliance with the compensation policy established by the Company.

**In relation to fulfillment of Director duties:**

- a) To ensure the fulfillment by the Directors of the obligations established in these Regulations, to report to the Board on their fulfillment, and to issue the relevant reports and proposals and, as applicable, on the measures to be adopted in the event of breach.
- b) To authorize Directors to use corporate assets.

**In relation to the corporate governance rules:**

- a) To supervise compliance with the corporate governance rules, making proposals for improvement to the Board of Directors, and to receive information in this respect and, as appropriate, issue an annual report on the measures to be implemented and submit it to the Board.
- b) To refer to the Board of Directors the proposals of the Audit Committee on the amendment of the Internal Code of Conduct on the Securities Markets.

**In relation to the corporate responsibility policy** (section introduced in the January 2010 reform of the Regulations of the Board of Directors):

- a) To propose and promote the Company's policy on corporate responsibility.
- b) To report on and supervise corporate responsibility initiatives and proposals made or decided on by the organizational units responsible, and, as appropriate, refer the relevant report or proposal to the Board of Directors.
- c) To annually prepare a report on corporate responsibility policy.

**Other functions:**

- a) To keep the Board informed of its activities and to prepare an annual report to be included in the Annual Corporate Governance Report and an Action Plan for each year.
- b) To propose and report on any other matter related to the foregoing that may be requested by the Chairman or by the Board of Directors.
- c) To report to the Board on the performance of their duties by the Chairman and the plenary session of the Board.
- d) To verify the type of each Director for the purposes of the pertinent explanations by the Board to the Shareholders' Meeting that is to make or ratify the Director's appointment, and for the recording of the appointment in the Annual Corporate Governance Report.
- e) Any other powers attributed to it by the Board.

**B.2.5.** Indicate, as appropriate, whether there are any regulations for the Board Committees, where they can be consulted, and whether any amendments have been made during the year. Also indicate whether any annual report on the activities of each Committee has been prepared voluntarily:

There are no specific internal regulations for the Committees, the preference having been for comprehensive regulation in the Board Regulations.

The Regulations may be consulted on the Company website, [www.ree.es](http://www.ree.es), in the Corporate Governance area of the Shareholders and Investors section, without prejudice to the fact they are registered at the CNMV and the Madrid Mercantile Registry and are therefore generally available to investors.

Each of the Board Committees prepares an annual report on their activities. These reports are published on the Company's website.

The Shareholders' Meeting held on April 13, 2011, approved an amendment to the Corporate Bylaws and to the Shareholders' Meeting Regulations in order to adapt them to the new legal requirements established

in Law 12/2010, of June 30, 2010 (basically affecting the composition, structure and functions of the Audit Committee) and Legislative Royal Decree 1/2010, of July 2, 2010, approving the Revised Corporate Enterprises Law (fully repealing the Corporations Law and partially repealing the Securities Market Law).

During 2011, the Corporate Responsibility and Governance Committee carried out an in-depth review of the Board Regulations in order to adapt them to the legislative amendments approved in 2010 and 2011 mentioned in Chapter I of this Section, following the approval by the Shareholders' Meeting held on April 13, 2011 of the amendment to the Corporate Bylaws and to the Shareholders' Meeting Regulations in order to adapt them to Law 12/2010, of June 30, 2010 and Legislative Royal Decree 1/2010, of July 2, 2010. The Corporate Responsibility and Governance Committee has prepared a proposed amendment to the Board Regulations that will be submitted to the Board for approval, subject to the necessary technical adjustments, once the regulations implementing the new rules governing the Annual Corporate Governance Report and the new Annual Report on Directors' Compensation are published.

The legislative amendments approved in the area of corporate governance in 2011, in particular, Law 25/2011, of August 1, 2011, have led to the commencement of a new review of the Corporate Bylaws and the Shareholders' Meeting Regulations in order to adapt them to the new legal requirements and this review is expected to conclude with a proposal by the Corporate Responsibility and Governance Committee to the Board of Directors, for referral to the next Shareholders' Meeting.

For further details of the content of the above reforms of the Corporate Bylaws and the Shareholders' Meeting Regulations, please consult the relevant explanatory reports, which will be published together with the call notice for the Annual Shareholders' Meeting.

**B.2.6.** Indicate whether the composition of the Executive Committee reflects the participation of the various Directors on the Board according to their status:

YES  NO

**If no, explain the composition of the Executive Committee**

Not applicable as there is no Executive Committee.

## C Related-Party Transactions

**C.1.** State whether the plenary session of the Board has reserved approval, subject to a favorable report by the Audit Committee or any other Committee to which that function has been delegated, of any transactions performed by the Company with Directors, significant shareholders or shareholders represented on the Board, or persons related to them:

YES  NO

**C.2.** Give details of material transactions entailing a transfer of funds or obligations between the Company or entities of its Group and the significant shareholders of the Company:

Name of significant shareholder	Name of Group company	Nature of the relationship	Type of transaction	Amount (€ Thousand)

**C.3.** Give details of material transactions entailing a transfer of funds or obligations between the Company or entities of its Group and the Company's Directors or executives:

Name of Director or executive	Name of Group company	Nature of the relationship	Type of transaction	Amount (€ Thousand)

There are no material transactions with Company Directors or executives.

At December 31, 2011, there were no loans, advances or guarantees established by the Company in favor of members of the Board of Directors of the Company. There were also no pension liabilities incurred vis-à-vis the members of the Company's Board of Directors at that date.

**C.4.** Give details of material transactions by the Company with other companies of the same Group, where such transactions are not eliminated in the process of preparing the consolidated financial statements and do not fall within the course of the Company's business, as regards their subject matter or terms and conditions:

Name of Group company	Brief description of the transaction	Amount (€ Thousand)
Red Eléctrica del Sur (REDESUR)	Transactions of no material significance, carried out in the ordinary course of the business between enterprises, which are included merely for informational purposes.	980



**C.5.** Indicate whether any members of the Board of Directors were subject to any conflict of interest during the year, as provided for in Article 229 of the Corporate Enterprises Law:

YES  NO

**Name of Director**

**Description of conflict of interest**

**C.6.** Give details of the mechanisms in place for detecting, identifying and resolving any potential conflicts of interest between the Company and/or its Group and its Directors, executives or significant shareholders:

In relation to the Directors, Article 29.3 a) of the Board Regulations establishes that Directors must notify the Board of Directors, through the Chairman or the Secretary, of any conflict of interest to which they are subject and refrain from attending and participating in deliberations affecting matters in which they have a direct or indirect personal interest or in which there is any sign of a conflict of interest. Pursuant to that Article, a personal interest will also be considered to exist when the matter affects a person related to the Director or to a company with which he has an employment or professional relationship or at which he has an executive position or a significant shareholding.

For the purposes of the preceding paragraph, 'related persons' are those defined as such from time to time in the applicable legislation.

In accordance with the provisions of Article 29.3 b) of the Board Regulations, Nominee Directors must disclose to the Board of Directors any conflict of interest between the Company and the shareholder that proposed their appointment where said conflict affects matters submitted to the Board and they must refrain from participating in the adoption of the corresponding resolutions.

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

Under Article 7 of the Internal Code of Conduct on the Securities Market, persons subject or temporarily subject thereto must generally attempt to avoid situations of direct conflict of interest or conflicts concerning persons related to them and must inform the Oversight Body of any situations of conflict of interest that may reasonably arise within fifteen (15) days of such situations coming to their attention, so that the Oversight Body may adopt the corresponding decisions in advance. Directors must give notice of the situations described in the preceding paragraph through the Office of the Secretary of the Board of Directors.

Persons subject or temporarily subject to the Code must keep up to date the information regarding conflicts of interest they have disclosed, reporting any such changes as may occur. Without prejudice to the obligations specified in the preceding paragraph as regards conflicts of interest, Directors must comply with the requirements contained in the Corporate Bylaws and in the Board Regulations and, in general, with all requirements arising from the corporate/commercial legislation on corporations.

The Oversight Body will keep an up-to-date itemized Register of the conflicts of interest disclosed by the various persons subject or temporarily subject to the Code, and will adopt the appropriate security measures for its safekeeping and storage. In any event, access to the Register will be restricted.

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

The Audit Committee is responsible for supervising compliance with the Internal Code of Conduct and the performance of the functions of the Oversight Body, the person responsible for the material transaction and the Office of the Secretary of the Board of Directors contemplated therein, as well as the internal resolution of any such questions and conflicts raised by parties subject or temporarily subject to the Code as may be submitted to the Committee by the Oversight Body. The Audit Committee will evaluate compliance with the Internal Code of Conduct on an annual basis and will adopt any appropriate measures for its optimum implementation and improvement. It is also responsible for proposing to the Corporate Responsibility and Governance Committee, for referral to the Board of Directors, any amendments it deems necessary in light of the Board's commitment to continuous adaptation, as well as the adoption of corporate governance best practices in the area and of the applicable legislation.

In relation to Company executives, Article 2.1.3 of the Internal Code of Conduct on the Securities Market establishes that Company executives, as defined in Chapter 1, are deemed to be subject to the Code and, accordingly, will be subject to potential conflicts of interest. Article 5.2.2 of the Internal Code provides that, when circumstances so require, the Oversight Body may decide to include as persons subject to the Code, on a temporary basis, any persons participating in a material transaction that have access to inside information. The parties affected will be given individual written notice of their inclusion on or exclusion from those lists.

In accordance with the provisions of Article 31 of the Board Regulations, the Board of Directors formally reserves the right to be informed of any material transaction of the Company with a significant shareholder, unless as a result of its nature and conditions it falls within the jurisdiction of the Shareholders' Meeting.

In 2010, at the proposal of the Audit Committee, the Board of Directors approved a policy on controlling related-party transactions and defined objective parameters for controlling related-party transactions, material or otherwise, recurring annual related-party transactions, and related-party transactions requiring mandatory notification to the markets.

**C.7.** Is more than one Group company listed in Spain?

YES  NO

List the subsidiaries listed in Spain:

**Listed subsidiaries**

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Indicate whether the areas of activity they engage in and any business dealings between them, and between the listed subsidiary and other Group companies, have been publicly and precisely defined:

YES  NO

**Define any business dealings between the parent company and the listed subsidiary, and between the listed subsidiary and other Group companies**

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Identify the mechanisms envisaged for the resolution of potential conflicts of interest between the listed subsidiary and other Group companies:

**Mechanisms for the resolution of any conflicts of interest**

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## D Risk Control Systems

**D.1.** General description of the risk policy of the Company and/or its Group, giving details and evaluating the risks covered by the system, together with evidence that the system is appropriate for the profile of each type of risk:

The purpose of the Risk Policy of the Red Eléctrica Group, approved by the Board of Directors on July 24, 2008, is to establish principles and guidelines to ensure the systematic identification, analysis, assessment, management and control of material risks that may affect the Red Eléctrica Group's objectives and activities, applying uniform criteria, within the established risk limits.

Material risks of the Red Eléctrica Group are those that may significantly affect the overall objectives of the Red Eléctrica Group, related to:

- ◆ Sustained creation of value over time.

Sustained profit growth, which must allow appropriate returns for investors and enable the company to implement its strategy.

- ◆ The continuity and quality of the energy supply in the electricity systems.

The achievement of this objective involves the management by the Spanish System Operator and is dependent on the reliability and availability of the transmission network.

- ◆ The construction of the electricity transmission infrastructure network necessary to meet future needs.

Red Eléctrica, as the sole transmission company of the Spanish electricity system, must design, fulfill the formalities for and construct the facilities specified by energy planning. This overall objective must be achieved on a cost-effective basis.

- ◆ The compatibility of the above objectives with social and environmental concerns.

This Policy establishes criteria on the acceptable level of risk for each of the overall objectives, which may be summarized as follows: all material risks that could jeopardize achievement of the overall objectives must have a low probability/impact value. Steps must be taken to ensure that any risks that do not meet this value are lowered to such level.

The general guidelines contained in the Risk Policy are as follows:

- ◆ Risk management must be fundamentally proactive and also geared towards the medium and long term, taking into account possible scenarios in an ever more globalized environment.
- ◆ In general, risks must be managed according to the relationship between the importance of the risk (probability/impact) and the investment and resources necessary to reduce it.
- ◆ Notwithstanding the above, the impact the risks may have on the electricity system itself must also be taken into account with respect to activities relating to the electricity system.
- ◆ Processes must be designed with efficiency and efficacy in mind and contemplate controls to mitigate risks, taking the form of systems based on international standards (good practices) that are periodically verified and improved.

- ◆ Contingency plans must be established to reduce the impact of material risks.
- ◆ The insurance necessary to cover any losses that may occur must be arranged.

The most significant risks to which the Group is exposed, and which form part of the risk control system, are:

- a) **Regulatory**, since the principal business activities of the Group are subject to regulation.
- b) **Operational**, basically arising from its assigned activities within the electricity system and the requirement to care for and protect the natural environment.
- c) **Market**, since most revenues, as well as certain expenses, may be influenced by variables such as inflation and interest rates.
- d) **Business and Credit (or counterparty)**, albeit to a lesser extent due to the lesser weight of the subsidiaries in the overall Group and the existing regulation regarding invoicing and collection for transmission and operation activities.

The risk control system covers both risks from internal processes and risks from the environment in which it operates, covering all activities performed by the Group, evaluating the impact of each risk on four aspects: strategy, the income statement, the electricity system and reputation.

Of all risks monitored by the system, 11% relate to regulatory risks, 75% to operational risks and 14% to business, market or credit risks. These figures are consistent with a Group whose fundamental mission is to ensure the functioning of the electricity system as a whole in a heavily regulated environment and with the level of solvency supported by the ratings given to it by international rating agencies.

An independent review of the design of the risk control system was carried out in 2011 by specialist consultant Ernst & Young, based on the ISO 31000 Standard (Risk Management. Principles and Guidelines). The conclusion issued by the firm on January 14, 2012, is as follows:

“As a result of our review, we can conclude that the design of the Risk Management System of Red Eléctrica Corporación applicable to its different activities is in line with the principles established in the ISO 31000 Standard on Principles and Guidelines.”

Furthermore, it should be noted that in 2007 Red Eléctrica embarked on a project to align, review and improve its System for Internal Control over Financial Reporting (ICFR), with the basic aim of improving the efficiency and security of processes for preparing economic and financial information on the Company, adopting international best practices early on, on a voluntary basis. The ICFR is detailed in one of the sections of Annex II to this Annual Corporate Governance Report, which Annex includes additional information to the current Annual Corporate Governance Report in accordance with Article 61 bis of Securities Market Law 24/1998, of July 29, 1988, as amended by Sustainable Economy Law 2/2011, of March 4, 2011.

**D.2.** Indicate whether any of the various kinds of risk (operating, technological, financial, legal, reputational, tax, etc.) to which the Company and/or its Group are exposed arose during the year:

YES  NO

If yes, describe the underlying circumstances and whether the established control systems functioned:

Risk materializing during the year	Underlying circumstances	Functioning of the control systems
The transmission network facilities are constantly exposed to operating events that may affect the continuity and security of the electricity supply.	In general, these events were caused by third parties and meteorological phenomena.	The control systems functioned adequately, as shown by the transmission network availability index, which reached 97.65% in 2011 (compared with 97.92% in 2010).  The Company has insurance policies that limit the potential impact of these events on the income statement.

**D.3.** Indicate whether any Committee or other governing body is responsible for establishing and supervising those control mechanisms:

YES  NO

If yes, give details of their functions

Name of Committee or body	Description of functions

As expressly recognized in the Board regulations, the **Board of Directors** is responsible for approval of the integral risk management policy of the Company and of the Group, and knowledge and periodic monitoring of internal control, prevention and reporting systems.

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

The **Audit Committee** is responsible for the periodic supervision of the risk management system, to ensure that the main risks are adequately identified, managed and disclosed.

The **Management Committee**, comprised of executives from the key strategic areas of the Company, is responsible for:

- ◆ Promoting implementation of the integral risk management policy.
- ◆ Monitoring the Risk Map, and agreeing on the appropriate actions to facilitate the achievement of the global objectives.

The risk control function is performed on a centralized basis by the **Regulation Office**, which reports to the Office of the Chairman.

#### **D.4. Identification and description of the procedures for compliance with the various regulations affecting the Company and/or its Group:**

##### **Procedures**

The RED ELÉCTRICA Group constantly designs and implements processes to ensure its compliance with the various regulations and to mitigate or reduce the related risks.

These processes have been integrated into systems structured according to a set of internal standards and procedures based on international standards (ISO 9001, ISO 14001 and OHSAS 18001), which are subject to systematic audits of the adequacy of their design and compliance, and include mechanisms for controlling the objectives that they must meet.

##### **Projects**

All proposals for significant projects from an economic or strategic point of view include the corresponding risk analysis, allowing risks to be evaluated when the related decisions are to be made. These decisions are made by the competent corporate body according to the established limits, with the most important projects requiring the approval of the Board of Directors.

##### **Verification**

The design and adaptation to existing regulations of, and correct compliance with, the internal rules and procedures is systematically reviewed by the Internal Audit and Risk Management functions, which form an integral part of the Regulation Office, and these procedures are also supervised by the Audit Committee.

Internal rules and their compliance are also subject to external audits on a periodic basis, by international ISO and OHSAS standards certification bodies.

##### **Self-evaluation of legal compliance**

An internal rule was approved and implemented in 2011 which obliges all units of the organization to establish mechanisms for the identification, dissemination and updating of the legislation applicable to them, and to carry out a yearly self-evaluation of their compliance.

## E Shareholders' Meeting

**E.1.** Indicate and, as appropriate, give details of any differences between the minimum quorum requirements provided for in the Corporate Enterprises Law (LSC) and the quorum required for the Shareholders' Meeting.

YES  NO

Percentage quorum other than as provided in Art. 193 LSC for general matters

Percentage quorum other than as provided in Art. 194 LSC for general matters

Quorum required on first call

Quorum required on second call

**E.2.** Indicate and, as appropriate, give details of any differences between the regime provided for in the Corporate Enterprises Law (LSC) and the regime for adopting corporate resolutions:

YES  NO

Describe how it differs from the regime provided for in the LSC.

Qualified majority other than as provided in Art. 194.1 and 194.2 LSC

Other instances of qualified majority

Percentage established by the Company for adoption of resolutions

Describe the differences

**E.3.** List any shareholder rights in connection with Shareholders' Meetings that differ from those established in the Corporate Enterprises Law (LSC).

Shareholder rights in relation to Shareholders' Meetings are regulated in Article 15 of the Corporate Bylaws, which expressly refer to the right to information and the right to attend Meetings, and in Articles 6 to 10 of the Shareholders' Meeting Regulations.

In accordance with the corporate legislation currently in force, Article 6 of the Shareholders' Meeting Regulations sets out the rights of shareholders, introducing, over and above the provisions of the LSC, a new right to participate in company matters on the terms established in Article 7 of the Shareholders' Meeting Regulations.

### Right to Information

The Company pays particular attention to the shareholders' right to information, as reflected in Article 15 of the Corporate Bylaws and Article 8 of the Shareholders' Meeting Regulations. Thus, Article 8 of the Shareholders' Meeting Regulations establishes an obligation to make available to shareholders, free of



charge, both through the Shareholder Information Office and on the Company website, the documentation and information relating to the agenda for the Shareholders' Meeting, including the following:

- ◆ The call notice of the Shareholders' Meeting, containing the proposed resolutions and the corresponding reports by the Board of Directors.
- ◆ The Company's individual and consolidated financial statements and the proposed distribution of income for the year.
- ◆ The Company's individual and consolidated management reports for the year.
- ◆ The audit reports for the consolidated financial statements and the Company's financial statements.
- ◆ The Annual Corporate Governance Report.
- ◆ The Corporate Responsibility Report.
- ◆ The Environmental Report.
- ◆ The report on the compensation policy for the Board of Directors, included in the annual public documentation submitted to the Annual Shareholders' Meeting.
- ◆ Any other report the inclusion of which is obligatory or is determined by the Board of Directors.

In order to reinforce the shareholders' right to information, shareholders may request the pertinent documentation, reports or clarification from the Company on the items included on the agenda, as well as request any information or clarification or ask questions in writing regarding any information provided by the Company to the CNMV since the date of the last Shareholders' Meeting.

The Shareholder Information Office specifically deals with requests made by Company shareholders. Shareholders may also submit questions in writing regarding any information available to the public or communicated to the competent authorities, and make inquiries through the Shareholder Information Office.

In addition, Article 15.4 of the Shareholders' Meeting Regulations establishes that shareholders may orally request any reports or clarification during the Meeting that they consider appropriate regarding items on the agenda. If this right cannot be satisfied at that time, the Board of Directors must provide the information in writing within seven days after the holding of the Shareholders' Meeting.

Law 25/2011, of August 1, 2011, precisely establishes certain information that is to be published on the website at the time of calling the Shareholders' Meeting, the scope of which is covered by the current Shareholders' Meeting Regulations.

Under Law 25/2011 more prominence is given to company websites, since it introduces a new Article 11 bis to the Corporate Enterprises Law regulating the online site or corporate website. The Law also incorporates an obligation under Article 516 of the Corporate Enterprises Law for listed companies to use the website to disseminate the call notice for the Shareholders' Meeting, something which Red Eléctrica Corporación, S.A. has been doing for a number of years.

The Law also introduces amendments to the call notice for the Shareholders' Meeting, mainly to reinforce the shareholders' right to information.

### Right to attend

Article 15 of the Corporate Bylaws and Article 9 of the Shareholders' Meeting Regulations establish that shareholders may attend the Shareholders' Meeting if they are up to date in the payment of capital calls and evidence their share ownership, by way of certification in their name, in the accounting register of book entries five days before the meeting is due to be held.

Company Directors and Executives must attend Shareholders' Meetings. As a general rule and in order for the proceedings of meetings and the resolutions adopted to reach the widest audience, the media are allowed access to Shareholders' Meetings. In order to facilitate such dissemination, Meetings may be filmed.

The Corporate Bylaws and the Shareholders' Meeting Regulations establish specific conditions for the representation of shareholders at Shareholders' Meetings, but there is no specific policy established by the Company regarding proxies for Shareholders' Meetings.

In this regard, Article 15 of the Corporate Bylaws and Article 10 of the Shareholders' Meeting Regulations provide that shareholders with the right to attend may confer a proxy for the Shareholders' Meeting on another shareholder with the right to attend, in the manner established in Article 184 of the LSC and in accordance with the provisions of the Corporate Bylaws. Proxies must be conferred in writing and specifically for each Meeting.

With the entry into force of Law 25/2011, the bylaw restrictions on attendance at Shareholders' Meetings have been eliminated and therefore it should be understood that the bylaw provision that proxies may only be conferred on another shareholder no longer applies and that proxies may be conferred on any individual. All of the above is notwithstanding the necessary adaptation of the relevant articles of the Corporate Bylaws and the Shareholders' Meeting Regulations, which are expected to be proposed to the next Shareholders' Meeting.

Except for cases of public proxies, which are subject to the legal provisions in force, no person may accumulate proxy votes that, together with their own votes, give them voting rights exceeding 3% of capital, as indicated in this Report (Section A.10).

Law 17/2007 amended Article 34 of Electricity Industry Law 54/1997, of November 27, 1997, by establishing various limits on shareholdings. Law 17/2007 provides that the voting rights corresponding to shares that exceed the maximum percentage established by law will be held in abeyance until the amount of shareholdings or voting rights is adjusted, establishing certain limits on shareholdings and voting rights at the Company.

Consequently, according to Article 5 (Capital Stock), Article 14 (Quorum) and the Sole Additional Provision (Special Regime for the State-Owned Industrial Holdings Company) of the Corporate Bylaws, and Article 6.3 (Limitations) and Article 15.8 (Vote) of the Shareholders' Meeting Regulations, the sum of the direct or indirect holdings in the Company's capital of any individual or legal entity may not exceed five percent of the Company's capital stock at any time, unless otherwise authorized by law. These shares may not be pooled for any purpose whatsoever. No shareholder may exercise more than three percent of voting rights. Parties that engage in activities in the electricity industry and those individuals or legal entities that directly or indirectly hold more than five percent of their capital, may not exercise more than one percent of voting rights. Furthermore, the sum of the direct or indirect interests held by parties that pursue activities in the electricity industry must not exceed forty percent.

As an exception to the above general rule, a special regime is applicable to the State-Owned Industrial Holdings Company (SEPI) pursuant to the new Sole Additional Provision of the Corporate Bylaws, according to which, in line with the provisions of the Electricity Industry Law, the limitations established in Subprovision 2 of Additional Provision Three of Law 17/2007 and those established in the Corporate Bylaws on shareholdings in the Company and voting rights do not apply to SEPI. The State-Owned Industrial Holdings Company will in all cases have a holding of not less than 10%.

Article 14 of the Corporate Bylaws provides that shares or other securities the non-economic rights of which exceed the limits recognized in Article 5 shall not be taken into account when calculating the quorum required to convene the relevant Shareholders' Meetings, or when calculating the majorities for the adoption of resolutions.

Moreover, in accordance with Article 15 of the Corporate Bylaws and Article 10 of the Shareholders' Meeting Regulations, as required by Law 17/2007, except in cases of public proxies, which are subject to the legal provisions in force in each case, no person may accumulate proxy votes that, together with their own votes, give them voting rights exceeding 3% of capital.

The special legal regime limiting holdings and voting rights in the Company's capital stock must be regarded as endorsed by Directive 2009/72/EC, of July 13, 2009, applying to transmission companies and operators of European electricity systems.

#### Right to Participate and New Technologies

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

In line with the most well-known recommendations in this area, the Shareholders' Meeting Regulations are in line with the regime established by Law 26/2003 of July 17, 2003 regarding the development of shareholder rights and the rules regarding the organization and functioning of the Shareholders' Meeting.

Thus it is provided that shareholders owning 5% of capital may request that the Board, prior to issuing the call, include any item on the agenda for the next Shareholders' Meeting. The Board of Directors must include the items requested in the manner that best suits the Company's interests, provided that they refer to matters falling within the scope of the powers of the Shareholders' Meeting.

Shareholders may also make proposals regarding items on the agenda and suggestions regarding any activities and interests of the Company that, in their opinion, should be discussed at the Shareholders' Meeting. In both cases, shareholders may make proposals and suggestions through the Shareholder Information Office.

Law 25/2011 has introduced a number of adjustments and provisions aimed at reinforcing the shareholders' right to participate in the Shareholders' Meeting, which will require the necessary adaptations to be made to the Corporate Bylaws and to the Shareholders' Meeting Regulations, and these are expected to be submitted for approval to the Annual Shareholders' Meeting.

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

Following the ongoing policy of providing shareholders with advanced telematic means of exercising their rights, the Board meeting held on February 24, 2011 approved the rules regarding voting and proxies by remote means and the exercise of the right to information by electronic means for the Annual Shareholders' Meeting held on April 13, 2011. The procedure was very satisfactory yet again: 664 shareholders holding 208,839 shares voted and/or delegated their vote electronically. This meant that 14% of the 4,788 shareholders present in person or by proxy at the Meeting participated in the Meeting by electronic means. This was another success as it equaled the percentage obtained at the 2010 Shareholders' Meeting and almost doubled the number of shareholders that voted and/or delegated their vote electronically at the 2009 Shareholders' Meeting, when 379 shareholders holding 133,711 shares used the electronic voting procedure.

Presentations to analysts and the Shareholders' Meeting are broadcast in real time on the Company website. Webcasts of presentations are available on the Company website. In 2007, 2008, 2009, 2010 and 2011 the Shareholders' Meeting was broadcast via live video webcast, with simultaneous translation into English.

Particularly noteworthy in 2011, as mentioned previously, was the implementation of the Shareholders' Electronic Forum at the Shareholders' Meeting held on April 13, 2011, with the aim of meeting the legislative requirements envisaged in Article 528.2 of the Corporate Enterprises Law. The purpose of the Forum is to facilitate communication among the shareholders of Red Eléctrica with a view to publishing proposals to supplement the agenda contained in the call notice, issuing requests for adherence to such proposals, presenting initiatives in order to reach the percentage to exercise the minority right envisaged in the law or making offers or requests for voluntary representation.

This tool has been incorporated into Article 8.4 of the Shareholders' Meeting Regulations, following its approval by the Shareholders' Meeting held on April 13, 2011.

The Company has also used certain social networking sites (Facebook and Twitter) in 2011 to publicize and provide information on the Annual Shareholders' Meeting.

It is worth mentioning that the amendment of the Corporate Bylaws and the Shareholders' Meeting Regulations approved at the Annual Shareholders' Meeting held on April 13, 2011, included a new duty for the company: equal treatment of shareholders, a provision that was already contained in the Board Regulations (Article 35).

As indicated previously, Law 25/2011 established the obligation on corporate enterprises to have a website, which must be approved by the Shareholders' Meeting and registered at the Mercantile Registry. The creation of the RED ELÉCTRICA website is expected to be submitted for approval or ratification to the next Annual Shareholders' Meeting.

#### **E.4. Indicate, as appropriate, the measures adopted to encourage participation by shareholders at Shareholders' Meetings:**

The Shareholders' Meeting Regulations pay particular attention to the right to participate, as developed upon in Article 7 and explained in detail in Section E.3 above, which should be consulted for further information.

Regarding the use of electronic voting, please see section E.3 above.

Law 25/2011, of August 1, 2011, partially reforming the Corporate Enterprises Law, has established provisions in this regard, leading to the need to adapt the Corporate Bylaws and Shareholders' Meeting Regulations.

**E.5.** Indicate whether the Chairman of the Board of Directors chairs Shareholders' Meetings. Give details, as appropriate, of what measures are adopted to ensure the independence and sound functioning of the Shareholders' Meeting:

YES  NO

#### Details of measures

As provided in the Company's regulations, the office of Chairman of the Shareholders' Meeting falls to the Chairman of the Board of Directors.

Article 12 of the Shareholders' Meeting Regulations establishes that the Shareholders' Meeting will be chaired by the Chairman of the Board of Directors and, in his absence, by the corresponding Deputy Chairman, either by rank or longest time in office. Failing that, it will be chaired by the person appointed by the Board of Directors and, if no appointment has been made, by the Director or shareholder freely chosen by the shareholders attending each meeting.

The Secretary or, as the case may be, Deputy Secretary of the Board of Directors will act as Secretary of the Shareholders' Meeting. If both are absent, the Secretary of the Shareholders' Meeting will be the Director or shareholder freely chosen by the shareholders attending each meeting.

The Chairman is tasked with chairing the meeting and establishing the order of deliberations and speeches; deciding on the method of voting on resolutions; handling any questions, clarification or claims arising in relation to the agenda, the list of attendees, share ownership, delegations or proxies, quorum requirements for the valid constitution of the Shareholders' Meeting and the adoption of resolutions, or the Bylaws limit on voting rights; and granting the floor to the shareholders who so request, withdrawing or refusing the floor when he deems the matter in question have been sufficiently debated.

The new contents of Article 5 of the Shareholders' Meeting Regulations and Article 13 of the Corporate Bylaws, both amended by the Shareholders' meeting held on April 13, 2011, establish measures aimed at ensuring the independence and sound functioning of the Shareholders' Meeting. These Articles provide that the Board of Directors will call annual and special Shareholders' Meetings by publishing a notice in the Official Mercantile Registry Gazette and on the Company's website at least one month before the date scheduled for the Shareholders' Meeting.

Royal Decree-Law 13/2010, of December 3, 2010, introduced the possibility of the Company website substituting the call notice published in the press, a possibility which the Company has included in the amendments to the Corporate Bylaws and the Shareholders' Meeting Regulations which, as previously mentioned, were approved by the Annual Shareholders' Meeting held on April 13, 2011.

The call notice shall state the name of the Company, the date and time of the Meeting on first call and the agenda on which the business to be transacted shall appear. The date for the second call may also be set. A minimum period of twenty-four hours must elapse between the two calls. Where a second call is not provided for and the Shareholders' Meeting cannot be held, the Meeting must be announced in the same way as the first call, within fifteen days from the date on which it was not held and at all times eight days prior to holding the second meeting. In the call notice the Board will endeavor to state the likely date for the meeting on first or second call.

Shareholders' Meetings shall be held in Spain at such venue as may be decided in each case by the Board of Directors, and as shall be duly indicated in the call notice.

It is worth noting here, in view of its importance to the Company, that pursuant to the new LSC, the Corporate Bylaws can, for the first time, expressly establish a venue for the Shareholders' Meeting outside the municipality where the registered office is located, an option which has been included in Article 13 of the Corporate Bylaws and Article 5 of the Shareholders' Meeting Regulations.

The Board must call a Special Shareholders' Meeting when shareholders holding five percent of the capital stock send a request stating the reasons and describing the business to be transacted, which must relate to matters falling within the jurisdiction of the Shareholders' Meeting. In this case the Shareholders' Meeting must be called to be held within thirty days from the date on which the Board of Directors was asked by way of a notary to call it and it shall fall to the Board of Directors to draw up the agenda, including the items indicated in the request in the manner which best suits the interests of the Company.

Shareholders representing at least five percent of the capital stock may request the publication of a supplement to the call notice for a Shareholders' Meeting, including one or more items on the agenda. This right must be exercised by giving duly authenticated notice which must be received at the registered office within five days after the publication of the call notice.

The supplement to the call notice must be published at least fifteen days prior to the date set for holding the Shareholders' Meeting. If included by the aforesaid shareholders in their request, the Board shall make available to the shareholders the complete wording of the resolutions proposed on the same terms as indicated above.

Failure to publish the supplement to the call notice by the statutory deadline shall be a ground for rendering the Shareholders' Meeting void.

If the Shareholders' Meeting is not called by the Board of Directors despite it being required to do so, it may be called, at the request of the shareholders and with the Board having been given the opportunity to be heard, by the judge having jurisdiction over the Company's registered office who, if applicable, will appoint the person to chair the Meeting.

The quorum necessary for constitution of the Shareholders' Meeting is established in Article 14 of the Corporate Bylaws and in Article 11 of the Shareholders' Meeting Regulations. The Corporate Bylaws and the Shareholders' Meeting Regulations do not differ from the provisions established in Articles 193 and 194 LSC. As already indicated, the minimum share requirement (50) in order to be able to attend Shareholders' Meetings was eliminated from the Corporate Bylaws in 2003.

Article 15 of the Shareholders' Meeting Regulations contains detailed rules for the sound functioning of the Shareholders' Meeting. This Article provides that, prior to addressing the items on the agenda, a list of attendees will be drawn up, detailing the status or representative authority of each attendee and the number of shares with which they attend, whether in person or by proxy. The number of shareholders present in person or by proxy and the amount of capital held by them will be stated at the bottom of the list, summarizing the capital corresponding to shareholders with the right to vote, and all such data will be verified by the Secretary.

Once the meeting has been called to order, the Secretary will read the call and attendance data based on the list of attendees. Based on the list of attendees, the Chairman will declare the meeting to be validly constituted, if appropriate. If a notary is present at the request of the Company to draw up the Minutes of the meeting, he will ask those attending if there are any reservations or objections to the shareholder attendance and capital data stated by the Chairman.

At the Annual Shareholders' Meeting the Chairman will inform the meeting of the most significant matters in the year and the proposals of the Board, and his presentation may be completed by the individuals authorized by him.

The Chairman of the Audit Committee will be available to the Shareholders' Meeting to respond to any questions raised by the shareholders on matters falling within its jurisdiction.

When the appropriate presentations have been concluded, the Chairman shall grant the floor to shareholders who have so requested, directing and coordinating the debate, and seeking to follow the established agenda.

Article 15.8 of the Shareholders' Meeting Regulations establishes that each share gives the right to one vote on the terms established in the Corporate Bylaws, with the limits set out therein as required by the Electricity Industry Law.

The Chairman will also decide on the most suitable method for voting in each case, announcing it publicly at the Shareholders' Meeting sufficiently in advance and prior to the vote.

Article 15 of the Shareholders' Meeting Regulations allows for the possibility of establishing electronic voting systems, provided that the identity of the voter and his status as shareholder or proxyholder are evidenced and that the number of shares with which he votes, as well as the direction of the vote or, as the case may be, his abstention, are stated clearly and unequivocally.

Article 17 of the Corporate Bylaws and Article 15.9 of the Shareholders' Meeting Regulations do not differ from the provisions established in the legislation in force, since they simply establish that resolutions will be adopted by majority vote, except where a higher majority is required by law.

All the above is also without prejudice to the rights to participate, to information and to attend, which are described in sufficient detail in Section E.3 of this Report.

**E.6.** Indicate, as appropriate, any amendments made to the Shareholders' Meeting Regulations during the year:

The Shareholders' Meeting held on April 13, 2011 approved the amendment of certain articles of the Shareholders' Meeting Regulations in order to update their provisions in light of certain legislative reforms (principally, Law 2/2010, of June 30, 2010 and Legislative Royal Decree 1/2010, of July 2, 2010, approved the Revised Corporate Enterprises Law) which have affected the legal regime governing corporations, in line with the reform of the Corporate Bylaws, also approved at the same meeting.

The reform consists of the deletion of the introductory paragraph and the amendment of Articles 1 ("Purpose and entry into force of the Regulations"), Article 2 ("Company website"), Article 3 ("Powers of the Shareholders' Meeting"), Article 5 ("Call"), Article 6 ("Shareholders' rights"), Article 8 ("A shareholder's right to information"), Article 9 ("Right to attend"), Article 11 ("Quorum"), Article 15 ("Constitution, deliberation and adoption of resolutions" in relation to Article 15.5 "Debate"), and Article 16 ("Minutes of the Shareholders' Meeting and certificate") of the Shareholders' Meeting Regulations.

The approved amendments to the Shareholders' Meeting Regulations have been notified to the CNMV, registered at the Mercantile Registry and published on the Company's website.

Following the approval of Law 25/2011, of August 1, 2011, it is necessary to carry out a new review of the Shareholders' Meeting Regulations and, subject to a report by the Corporate Responsibility and Governance Committee, it is expected that the Board of Directors will submit the proposed amendment to the next Annual Shareholders' Meeting.

For further details of the content of this proposed amendment to the Shareholders' Meeting Regulations, please consult the explanatory report prepared by the Board of Directors, which will be published together with the call notice for the Shareholders' Meeting.

**E.7.** Indicate the data on attendance at the Shareholders' Meetings held in the year to which this Report refers:

Date of Shareholders' Meeting	ATTENDANCE DATA				Total
	% Attendance in person	% Attendance by proxy	% Remote voting Electronic voting	Other	
04.13.11	20.5 %	45.4%	0.15%	--	66.05 %

**E.8.** Briefly indicate the resolutions adopted at the Shareholders' Meetings held in the year to which this Report refers and the percentage of votes with which each resolution was adopted:

**Resolutions adopted**

1. Examination and approval, as the case may be, of the Financial Statements (balance sheet, income statement, statement of changes in equity, cash flow statement, and notes to financial statements) and the Management Report of Red Eléctrica Corporación, S.A. for the year ended December 31, 2010.

For	Against	Abstentions
99.95%	0.03%	0.02%

<b>Resolutions adopted</b>	<b>For</b>	<b>Against</b>	<b>Abstentions</b>
2. Examination and approval, as the case may be, of the Consolidated Financial Statements (consolidated balance sheet, consolidated income statement, consolidated overall income statement, consolidated statement of changes in equity, consolidated cash flow statement, and notes to the consolidated financial statements) and the Consolidated Management Report of the Consolidated Group of Red Eléctrica Corporación, S.A. for the year ended December 31, 2010.	99.95%	0.03%	0.02%
3. Examination and approval, as the case may be, of the proposed distribution of income of Red Eléctrica Corporación, S.A. for the year ended December 31, 2010.	99.95%	0.03%	0.02%
4. Examination and approval, as the case may be, of the conduct of management by the Board of Directors of Red Eléctrica Corporación, S.A. in 2010.	99.92%	0.04%	0.04%
5. Appointment of the auditors of the Parent Company and of the Consolidated Group.	99.95%	0.03%	0.02%
6. Amendment of the Corporate Bylaws to update their provisions as a result of various legislative reforms relating to corporations:			
6.1 Amendments for adaptation to the latest legislative reforms and other formal or stylistic amendments to make the wording of the Corporate Bylaws more precise: amendment of Article 1 ("Name and legal regime"), Article 6 ("Accounting record of shares"), Article 7 ("Rights attaching to shares"), Article 8 ("Increase and reduction of capital stock"), Article 11 ("Shareholders' Meeting"), Article 12 ("Types of Shareholders' Meetings"), Article 14 ("Quorum"), Article 15 ("Right to information and attendance of Shareholders' Meetings"), Article 17 ("Presiding Panel, deliberations"), Article 18 ("Minutes"), Article 20 ("Board of Directors"), Article 22 ("Board Committees and delegation of powers"), Article 23 ("Audit Committee"), Article 24 ("Appointments and Compensation Committee"), Article 29 ("Audit"), Article 32 ("Rules and method of liquidation"), and Article 33 ("Scope of these Bylaws") of the Corporate Bylaws.	99.95%	0.03%	0.02%
6.2 Amendment of the Bylaws not only to adapt them to the latest legislative reforms, but also to add flexibility to the venue for holding Shareholders' Meetings: amendment of Article 13 ("Call to the Shareholders' Meeting") of the Corporate Bylaws.	99.95%	0.03%	0.02%
7. Amendment of the Regulations of the Shareholders' Meeting to update their provisions as a result of various legislative reforms relating to corporations:			
7.1 Amendments for adaptation to the latest legislative reforms and other amendments of a formal or stylistic nature to make the wording of the Shareholders' Meeting Regulations more precise: deletion of the introductory paragraph. Amendment of Article 1 ("Purpose and entry into force of the Regulations"), Article 2 ("Company website"), Article 3 ("Powers of the Shareholders' Meeting"), Article 6 ("Shareholders' rights"), Article 8 ("Shareholders' right to information"), Article 9 ("Right to attend"), Article 11 ("Quorum"), Article 15 ("Constitution, deliberation and adoption of resolutions"), and Article 16 ("Minutes of the Shareholders' Meeting and certificate") of the Regulations of the Shareholders' Meeting.	99.95%	0.03%	0.02%
7.2 Amendment of the Shareholders' Meeting Regulations not only to adapt them to the latest legislative reforms, but also to add flexibility to the venue for holding Shareholders' Meetings: amendment of Article 5 ("Call") of the Regulations of the Shareholders' Meeting.	99.95%	0.03%	0.02%



<b>Resolutions adopted</b>	<b>For</b>	<b>Against</b>	<b>Abstentions</b>
8. Authorizations granted to Board of Directors for the derivative acquisition of treasury stock:			
8.1 Authorization for the derivative acquisition of treasury stock by the Company or by companies of the Red Eléctrica Group, and for the direct award of treasury stock to employees and Executive Directors of the Company and of the companies of the Red Eléctrica Group, as compensation.	98.92%	1.07%	0.01%
8.2 Approval of a Compensation Plan for members of Management and the Executive Directors of the Company and of the companies of the Red Eléctrica Group.	99.65%	0.32%	0.03%
8.3 Revocation of previous authorizations.	99.93 %	0.04 %	0.03 %
9. Compensation of the Board of Directors.			
9.1 Approval of the report on the compensation policy for the Board of Directors of Red Eléctrica Corporación, S.A.	68.68%	30.60%	0.72%
9.2 Approval of the compensation of the Board of Directors of Red Eléctrica Corporación, S.A. for 2010.	96.54%	2.96%	0.50%
10. Delegation of authority to fully implement the resolutions adopted at the Shareholders' Meeting.	99.51%	0.47%	0.02%
11. Information to the Shareholders' Meeting on the 2010 Annual Corporate Governance Report of Red Eléctrica Corporación, S.A.	For information	For information	For information
12. Information to the Shareholders' Meeting on the elements contained in the Management Report relating to Article 116 bis of the Securities Market Law.	For information	For information	For information

**E.9.** Indicate whether there is any restriction in the Bylaws regarding the minimum number of shares necessary to attend the Shareholders' Meeting:

YES  NO

**Number of shares necessary to attend the Shareholders' Meeting**

1

**E.10.** Indicate and provide support for the policies followed by the Company with respect to proxy voting at Shareholders' Meetings:

The Company has no specific policy for granting proxies to vote at Shareholders' Meetings. Notwithstanding the above, the Corporate Bylaws and the Shareholders' Meeting Regulations establish specific conditions for the representation of shareholders at Shareholders' Meetings.

In this regard, Article 15 of the Corporate Bylaws and Article 10 of the Shareholders' Meeting Regulations provide that shareholders with the right to attend may confer a proxy for the Shareholders' Meeting on another shareholder with the right to attend, in the manner established in Articles 185 through 187 of the LSC respecting the provisions of the Corporate Bylaws. Proxies must be conferred in writing and specifically for each Meeting.

With the entry into force of Law 25/2011, the bylaw restrictions on attendance at Shareholders' Meetings have been eliminated and therefore it should be understood that the bylaw provision that proxies for the Shareholders' Meeting may only be conferred on another shareholder no longer applies and that

proxies may be conferred on any individual. All of the above is notwithstanding the necessary adaptation of the relevant articles of the Corporate Bylaws and the Shareholders' Meeting Regulations, which are expected to be proposed to the next Shareholders' Meeting.

Except for cases of public proxies, which are subject to the legal provisions in force, no person can accumulate proxy votes that, together with their votes, give them voting rights exceeding 3% of capital. In addition, shares may not be pooled for any purpose.

As already discussed in this Report (section A), Law 17/2007 amended Article 34 of Electricity Industry Law 54/1997 of November 27, 1997. Specifically, Subprovision two of Additional Provision Three of Law 17/2007 established new maximum limits on the exercise of voting rights, in order to guarantee the independence of a company engaging in regulated activities in the electricity industry which, pursuant to Electricity Industry Law 54/1997 of November 27, 1997, constitute an essential service.

These legal provisions have been included in the Corporate Bylaws and the Shareholders' Meeting Regulations, as indicated in section E.3 above.

Thus, any individual or legal entity may hold shares in the Company, provided that the sum of their direct and indirect interests in the Company's capital does not exceed five percent of capital and they do not exercise more than three percent of voting rights. These shares may not be pooled for any purpose whatsoever.

Parties that pursue activities in the electricity industry, and those individuals or legal entities that directly or indirectly hold more than five percent of their capital, may not exercise more than one percent of voting rights at the company responsible for operation of the system.

The special regime for SEPI, whereby it must hold at least ten percent of capital in all cases, remains unchanged.

The legal regime established by Directive 2009/72/EC, of July 13, 2009, which proclaims the mandatory independence of transmission companies and operators of European electricity systems has endorsed the legal limitations on shareholders established in Law 17/2007.

Also notable are the provisions of the Corporate Bylaws and Shareholders' Meeting Regulations regarding electronic voting and proxies, which have been successfully applied since 2005 and are discussed in detail in section E.3 above.

As is customary, the Company facilitated the use of electronic voting systems and proxies by shareholders for the Annual Shareholders' Meeting held on April 13, 2011, following approval of the corresponding procedure by the Board meeting held on February 24, 2011.

Law 25/2011 has introduced certain amendments to the legal regime applicable to proxies and the relevant amendments will therefore be made to the Corporate Bylaws and Shareholders' Meeting Regulations.

**E.11.** Indicate whether the Company is aware of the policy of institutional investors on whether or not to participate in the Company's decisions:

YES  NO

### Describe the policy

Relations between the Company and institutional investors are general in nature and no specific or special relationships are held with any of them.

The Company regularly organizes road shows at the principal financial centers in Spain and abroad where there is a higher concentration of institutional investors, in order to inform them of its activities and its business performance in an attempt to forge closer ties with this group of investors. In light of the high percentage of foreign institutional investors (close to 70%), in 2011, as in previous years, the Company implemented a program of visits to investors and proxy advisers in order to directly explain the corporate governance practices and initiatives followed by the Company, with a view to consolidating adequate mechanisms for the regular exchange of information with domestic and foreign institutional investors and the most prominent proxy advisers, in order to continue adapting to the most advanced international corporate governance standards.

Under no circumstances does the Company disclose any information to institutional shareholders that might place them in a privileged or advantageous situation vis-à-vis the other shareholders.

#### E.12. Indicate the URL and means of accessing corporate governance content on the website:

Article 2 of the Shareholders' Meeting Regulations establishes the content of the Company website, the purpose of which is to serve as an instrument to ensure transparency in the way the Company conducts itself and, at the same time, to allow shareholders to exercise their rights more effectively, as well as make their dealings with the Company easier. The Company has been using this form of communication since it was listed on the stock markets in 1999. The content of the website is updated regularly and exceeds the requirements of the applicable legislation.

Under Law 25/2011 more prominence is given to company websites, since it introduces a new Article 11 bis to the Corporate Enterprises Law regulating the online site or corporate website. The Law also incorporates an obligation under Article 516 of the Corporate Enterprises Law for listed companies to use the website to disseminate the call notice for the Shareholders' Meeting, something which Red Eléctrica Corporación, S.A. has been doing for a number of years.

As indicated previously, Law 25/2011 established the obligation on corporate enterprises to have a website, which must be approved by the Shareholders' Meeting and registered at the Mercantile Registry. The creation of the RED ELÉCTRICA website is expected to be submitted for approval or ratification to the next Annual Shareholders' Meeting.

The Company's website ([www.ree.es](http://www.ree.es)) includes a "Shareholders and Investors" section accessible from the home page. Among other items, it includes a section specifically entitled "Corporate Governance" containing all information on this matter that may be of interest to shareholders. The website includes the following content, among other items, in accordance with the Shareholders' Meeting Regulations:

- ◆ The Corporate Bylaws.
- ◆ The Shareholders' Meeting Regulations, the Board Regulations and other corporate governance provisions.
- ◆ Quarterly reports for the year and annual reports for the past two years, together with reports by the external auditor.
- ◆ The Annual Corporate Governance Report prepared by the Board.
- ◆ The composition of the Board and its Committees.

- ◆ Details of shareholders with stable holdings, both direct and indirect, and their representation on the Board, as well as any side agreements between shareholders which have been disclosed to the Company and the market.
- ◆ The shareholdings of each of the members of the Board.
- ◆ The report on the compensation policy for the Board of Directors.
- ◆ Information contained in the presentations made to different market operators and analysts, intermediaries and significant shareholders.
- ◆ Material events disclosed to the CNMV.
- ◆ The resolutions adopted at the last Shareholders' Meeting, including details on the composition and result of the vote.
- ◆ The current call for the next Shareholders' Meeting.
- ◆ Any information that must be made available to shareholders along with the call for the Shareholders' Meeting.
- ◆ Responses to proposals and suggestions made by shareholders.
- ◆ Communication channels between the Company and the shareholders and the relevant explanations regarding the exercise of the right to information, indicating the postal and electronic mail addresses to which shareholders may send their questions.
- ◆ The Shareholders' Electronic Forum and its Operating Rules.
- ◆ Means and procedures for granting proxies for Shareholders' Meetings, as well as the means and procedures for casting votes remotely, with the ballots approved for doing so.

As regards the disclosure of resolutions approved by the Shareholders' Meeting, Article 17 of the Shareholders' Meeting Regulations specifies that, without prejudice to the recording of all registrable resolutions at the Mercantile Registry and to any applicable legal provisions regarding disclosure of corporate resolutions, the Company will submit the text of the approved resolutions to the CNMV in a notice disclosing a material event, on the same day the meeting is held or on the immediately following business day. Once it has been reported to the CNMV, the text of the resolutions will also be made available on the Company website.

Work continued in 2011 to improve the content of the Company website as a means of communication with shareholders and investors, pursuant to Order ECO/3772/2003 of December 26, 2003 and CNMV Circular 4/2007. The following steps were particularly noteworthy:

- ◆ The live and simultaneous broadcast, in Spanish and English, of the Annual Shareholders' Meeting held on April 13, 2011.
- ◆ The live and simultaneous broadcast, in Spanish and English, of the presentation of 2010 year-end results and the Company's 2011-2015 Strategic Plan.
- ◆ The publication in English of the call notice, as from the date of its publication in Spanish, and proposed resolutions submitted for approval to the Shareholders' Meeting, as well as all the related documentation, including the Annual Corporate Governance Report.

Particularly noteworthy in 2011 was the implementation of the Shareholders' Electronic Forum at the Shareholders' Meeting held on April 13, 2011. The Operating Rules for the Shareholders' Electronic Forum were approved by the Board of Directors at the meeting held on February 24, 2011.

The Shareholders' Electronic Forum set up by Red Eléctrica Corporación, S.A. on its website ([www.ree.es](http://www.ree.es)) on the occasion of holding its Shareholders' Meetings, responds to the need established in the last paragraph of Article 117.2 of Securities Market Law 24/1988, of July 28, 1988, introduced by Law 12/2010 of June 30, 2010, and in Article 528.2 of the Revised Corporate Enterprises Law, approved by Legislative Royal Decree 1/2010, of July 2, 2010.

The purpose of the Forum is to facilitate communication among the shareholders of Red Eléctrica with a view to publishing proposals to supplement the agenda contained in the call notice, issuing requests for adherence to such proposals, presenting initiatives in order to reach the percentage to exercise the minority right envisaged in the law or making offers or requests for voluntary representation.

This tool has been incorporated into Article 8.4 of the Shareholders' Meeting Regulations, following its approval by the Shareholders' Meeting held on April 13, 2011.

Following the approval of Law 25/2011, it is expected that the Board will propose the incorporation of certain technical amendments to the Shareholders' Meeting Regulations to the Annual Shareholders' Meeting in order to adapt the relevant articles to the literal wording of the Law.

## F Degree of Compliance with Corporate Governance Recommendations

Indicate the degree to which the Company complies with the recommendations of the Unified Good Governance Code.

In the event of noncompliance with any of the recommendations, explain the recommendations, rules, practices or criteria used by the Company.

It is worth noting that the level of compliance with the corporate governance recommendations remains the same as that detailed in the 2010 Annual Corporate Governance Report.

**1.** The bylaws of listed companies should not place an upper limit on the votes that can be cast by a single shareholder, or impose other restrictions that hinder the taking of control at the Company by means of the acquisition of its shares on the market.

See sections: A.9, B.1.22, B.1.23 and E.1, E.2

Complies  Explain

**2.** When a parent company and a subsidiary are listed, the two should provide detailed disclosure on:

a) Their respective areas of activity and any business dealings between them, as well as between the listed subsidiary and other Group companies.

b) The mechanisms in place to resolve possible conflicts of interest.

See sections: C.4 and C.7

Complies  Complies partially  Explain  Not applicable

**3.** Even when not expressly required under corporate/commercial law, any decisions involving a structural change should be submitted to the Shareholders' Meeting for approval or ratification. In particular:

a) The conversion of listed companies into holding companies by way of "subsidiarization", or the transfer to dependent entities of core activities previously pursued by the original company, even where the latter retains full control of the former.

b) Any acquisition or disposal of key operating assets that would effectively alter the company's corporate purpose.

c) Operations the effect of which is equivalent to the company's liquidation.

Complies  Complies partially  Explain

**4.** Detailed proposals of the resolutions to be adopted at the Shareholders' Meeting, including the information stated in Recommendation 28, should be made available at the same time as the publication of the call notice.

Complies

Complies partially

Explain

**5.** Separate votes should be taken at the Shareholders' Meeting on substantially independent items, so that shareholders can express their preferences in each case. This rule will apply in particular to:

- a) The appointment or ratification of Directors, with separate voting on each;
- b) Amendments to the Corporate Bylaws, with votes taken on all articles or groups of articles that are substantially independent.

See section: E.8

Complies

Complies partially

Explain

**6.** Companies should allow split votes, so that financial intermediaries acting as nominees on behalf of different clients can issue their votes according to their client's instructions.

Complies

Explain

**7.** The Board should perform its duties with unity of purpose and independent judgment, treat all shareholders equally and be guided by the interests of the Company, understood to be maximizing the economic value of the Company on a sustained basis.

The Board also should ensure that the Company abides by the laws and regulations in its dealings with stakeholders; fulfils its obligations and agreements in good faith; respects the customs and good practices of the industries and territories where it does business; and upholds any additional social responsibility principles it has subscribed to voluntarily.

Complies

Complies partially

Explain

**8.** The core mission of the Board should be to approve the Company's strategy and authorize the organizational resources to implement it, and ensure that management meets the objectives set while pursuing the Company's interests and corporate purpose. As such, the plenary session of the Board should reserve the right to approve:

- a) The general policies and strategies of the Company, in particular:
  - i) The strategic or business plan, as well as annual management objectives and budgets.
  - ii) The investment and financing policy.
  - iii) Definition of the structure of the corporate group.
  - iv) The corporate governance policy.

- v) The corporate social responsibility policy.
- vi) The policy regarding compensation and evaluation of senior executives.
- vii) The risk control and management policy, as well as periodic monitoring of internal reporting and control systems.
- viii) The dividend and treasury stock policies and, in particular, their limits.

See sections: B.1.10, B.1.13, B.1.14 and D.3

b) The following decisions:

- i) On the proposal of the Company's Chief Executive, the appointment and removal of senior executives, and their indemnification clauses.

See section: B.1.14

- ii) Directors' compensation and, in the case of Executive Directors, the additional consideration for their executive functions and other contractual conditions that must be observed.

See section: B.1.14

- iii) The financial information that the Company must periodically disclose as a listed company.

- iv) Investments or operations considered strategic by virtue of their amount or special characteristics, unless their approval corresponds to the Shareholders' Meeting.

- v) The creation or acquisition of shares in special-purpose vehicles or entities resident in countries or territories that are considered tax havens, and any other transactions or operations of an analogous nature whose complexity could impair the transparency of the Group.

c) Transactions the Company enters into with Directors, significant shareholders, shareholders with Board representation or other persons related thereto ("related-party transactions").

However, Board authorization will not be required for related-party transactions that simultaneously meet the following three conditions:

1. They are governed by standard-form agreements applied on an across-the-board basis to a large number of clients.
2. They are made at prices or rates generally set by the person supplying the goods or services in question;
3. Their amount is no more than 1% of the company's annual revenues.

It is recommended that related-party transactions should only be approved on the basis of a favorable report from the Audit Committee or any other Committee to which this function has been entrusted, and that any Directors involved should not exercise or delegate their votes, and should withdraw from the meeting room while the Board deliberates and votes.

Ideally the powers attributed to the Board in this section should be deemed to be non-delegable with the exception of those mentioned in letters b) and c), which may be delegated to the Delegated Committee for reasons of urgency and later ratified by the plenary session of the Board.

See sections: C.1 and C.6

Complies

Complies partially

Explain



**9.** To operate effectively and encourage participation, the Board of Directors should ideally comprise no less than five and no more than fifteen members.

See section: B.1.1

Complies  Explain

**10.** External Directors, both Nominee and Independent, should occupy an ample majority of Board positions, while the number of Executive Directors should be the minimum necessary, bearing in mind the complexity of the corporate group and the percentage holdings of Executive Directors.

See sections: A.2, A.3 and B.1.3

Complies  Complies partially  Explain

**11.** If any External Director cannot be deemed a Nominee or Independent Director, the Company should disclose this circumstance and the links that person maintains with the Company or its executives, or with its shareholders.

See section: B.1.3

Complies  Complies partially  Explain

Antonio Garamendi Lecanda has completed the maximum term of 12 years as an Independent Director of RED ELÉCTRICA. According to the provisions of Article 7.2 c) of the Board Regulations, the Unified Good Governance Code and international corporate governance best practices, this is the maximum period for which he may be treated as an Independent Director and, therefore, if a proposal is made for his reappointment at the next Annual Shareholders' Meeting, he will be classed the category of "other External Directors."

If the Annual Shareholders' Meeting approves the reappointment of Mr. Garamendi as a Company Director, he must immediately be replaced as Chairman of the Corporate Responsibility and Governance Committee, a position which must be occupied by an Independent Director, in accordance with the Corporate Bylaws and the Board Regulations.

**12.** Among External Directors, the ratio of Nominee Directors to Independent Directors should reflect the proportion between the capital represented on the Board by Nominee Directors and the remainder of the Company's capital.

This proportionality rule may be relaxed so that the weighting of Nominee Directors is greater than would strictly correspond to the total percentage of capital they represent:

1. In large cap companies where few or no shareholdings are legally deemed significant shareholdings, but there are shareholders whose shareholdings have a high absolute value.

2. In companies with numerous shareholders represented on the Board but not otherwise related.

See sections: A.2, A.3 and B.1.3

Complies  Explain

**13.** The number of Independent Directors should represent at least one-third of all Directors.

See section: B.1.3

Complies  Explain

**14.** The category of each Director should be explained by the Board to the Shareholders' Meeting which is to make or ratify his/her appointment and should subsequently be confirmed or reviewed annually in the Annual Corporate Governance Report, after verification by the Appointments Committee. The report should also disclose the reasons for the appointment of Nominee Directors proposed by shareholders with shareholdings of less than 5% of capital, and explain why formal requests for presence on the Board have not been honored from shareholders whose holdings are greater than or equal to those of others upon whose request Nominee Directors have been appointed.

See sections: B.1.3 and B.1.4

Complies  Complies partially  Explain

As indicated in Recommendation no. 11, Antonio Garamendi Lecanda has completed the maximum term of 12 years as an Independent Director of RED ELÉCTRICA. According to the provisions of Article 7.2 c) of the Board Regulations, the Unified Good Governance Code and international corporate governance best practices, this is the maximum period for which he may be treated as an Independent Director and, therefore, if a proposal is made for his reappointment at the next Annual Shareholders' Meeting, he will be classed the category of "other External Directors."

If the Annual Shareholders' Meeting approves the reappointment of Mr. Garamendi as a Company Director, he must immediately be replaced as Chairman of the Corporate Responsibility and Governance Committee, a position which must be occupied by an Independent Director, in accordance with the Corporate Bylaws and the Board Regulations.

**15.** When female Directors are few or nonexistent, the Board should state the reasons why and the initiatives adopted to correct the situation; in particular, with respect to vacancies, the Appointments Committee should take steps to ensure that:

- a) Selection processes do not suffer from implicit bias preventing the selection of female Directors;
- b) The Company makes a conscious effort to include women with the target profile among the candidates for Board positions.

See sections: B.1.2, B.1.27 and B.2.3

Complies  Complies partially  Explain  Not applicable

**16.** The Chairman, as the person responsible for the sound functioning of the Board, should ensure that Directors are supplied with sufficient information in advance of Board meetings, and prompt debate and encourage the active involvement of all members, safeguarding their rights to freely express and adopt positions; and organize and coordinate regular evaluations of the Board and, where appropriate, the Company's Chief Executive, along with the Chairmen of the relevant Committees.

See section: B.1.42

Complies

Complies partially

Explain

**17.** Where the Board Chairman is also the Company's Chief Executive, an Independent Director should be empowered to request the call of Board meetings or the inclusion of new items on the agenda in order to coordinate and give voice to the concerns of External Directors and to lead the Board's evaluation of the Chairman.

See section: B.1.21

Complies

Complies partially

Explain

Not applicable

Thus any Director may request that a Board meeting be called and, if so requested in writing jointly by three Directors (regardless of their category), the Corporate Bylaws and the Board Regulations provide that the Board must meet. Accordingly, it may be concluded that Red Eléctrica's internal regulations not only fulfill the aim of the Unified Code, but also offer greater flexibility when calling Board meetings.

The process of evaluation of the Board and its Chairman is expressly assigned to the Corporate Responsibility and Governance Committee.

The Board Regulations attribute to the Chairman of the Corporate Responsibility and Governance Committee the function of communication and coordination between and among External and/or Independent Directors in the performance of their functions, and include the possibility of requesting the calling of a Board meeting or the inclusion of new items on the agenda at the request of any Director, as well as the coordination of the concerns of External Directors and management of the evaluation by the Board of its Chairman.

**18.** The Board Secretary should take special care to ensure that the Board's actions:

- a) Adhere to the spirit and letter of laws and their implementing regulations, including those approved by regulatory agencies;
- b) Comply with the Corporate Bylaws, the Shareholders' Meeting Regulations, the Board Regulations and other regulations at the Company;
- c) Are informed by the good governance recommendations of the Unified Code that the Company has subscribed to.

In order to safeguard the independence, impartiality and professionalism of the Secretary, his/her appointment and removal should be proposed by the Appointments Committee and approved by the plenary session of the Board and the relevant appointment and removal procedures should be stipulated in the Board Regulations.

See section: B.1.34

Complies

Complies partially

Explain

**19.** The Board should meet as often as needed to effectively perform its functions, in accordance with the schedule of dates and matters established at the beginning of the year, and each Director may propose other items not initially included on the agenda.

See section: B.1.29

Complies

Complies partially

Explain

**20.** Director absences should be kept to the bare minimum and quantified in the Annual Corporate Governance Report. When Directors have no choice but to delegate their vote, they should do so with instructions.

See sections: B.1.29 and B.1.30

Complies

Complies partially

Explain

**21.** When Directors or the Secretary express concerns about any proposal or, in the case of Directors, about the Company's performance, and such concerns are not resolved at the Board, the person expressing them can request that they be recorded in the Minutes.

Complies

Complies partially

Explain

Not applicable

**22.** The plenary session of the Board should evaluate the following each year:

- a) The quality and efficiency of the functioning of the Board;
- b) Based on the report submitted by the Appointments Committee, the performance of their functions by the Board Chairman and the Company's Chief Executive;
- c) The performance of its Committees on the basis of the reports furnished by them.

See section: B.1.19

Complies

Complies partially

Explain

**23.** All Directors should be able to exercise their rights to receive any additional information they require on matters falling within the Board's jurisdiction. Unless otherwise indicated in the Corporate Bylaws or Board Regulations, such requests should be addressed to the Board Chairman or Board Secretary.

See section: B.1.42

Complies

Explain

**24.** All Directors should be entitled to call on the Company for the advice and guidance they need to perform their functions. The Company should provide suitable channels for the exercise of this right, which may include external advice in special circumstances at the Company's expense.

See section: B.1.41

Complies  Explain

**25.** Companies should organize induction programs for new Directors as a swift means of sufficiently familiarizing them with the workings of the Company and its corporate governance rules. Directors should also be offered refresher programs when circumstances so advise.

Complies  Complies partially  Explain

**26.** Companies should require their Directors to devote sufficient time and effort to perform their functions effectively, and, as such:

- a) Directors should inform the Appointments Committee of any other professional obligations, in case they might affect the level of dedication required;
- b) Companies should establish rules about the number of directorships their Board members can hold.

See sections: B.1.8, B.1.9 and B.1.17

Complies  Complies partially  Explain

**27.** The proposal for the appointment or reappointment of Directors submitted by the Board to the Shareholders' Meeting, as well as provisional appointments by way of co-optation, should be approved by the Board:

- a) On the proposal of the Appointments Committee, in the case of Independent Directors;
- b) Subject to a report from the Appointments Committee in all other cases.

See section: B.1.2 and B.1.3

Complies  Complies partially  Explain

**28.** Companies should post the following Director particulars on their websites, and keep them permanently updated:

- a) Professional profile and background;
- b) Directorships held in other companies, listed or otherwise;
- c) An indication of the Director's category; in the case of Nominee Directors, stating the shareholder they represent or have links with;

- d) The date of their first and subsequent appointments as a Company Director, and;  
e) Shares held in the Company and any share options.

Complies       Complies partially       Explain

**29.** Independent Directors should not remain in office for a continuous period of more than 12 years.

See section: B.1.2 and B.1.26

Complies       Explain

**30.** Nominee Directors should resign when the shareholder they represent fully disposes of their shareholding. The corresponding number of Nominee Directors should also resign if the shareholder they represent reduces its shareholding to such an extent that the number of its Nominee Directors must also be reduced.

See sections: A.2, A.3, B.1.2 and B.1.20

Complies       Complies partially       Explain

**31.** The Board of Directors should not propose the removal of any Independent Director prior to completion of the term of office specified in the Corporate Bylaws for which the Director was appointed, except when the Board finds that there is just cause after a report from the Appointments Committee. In particular, just cause will be deemed to exist when a Director is in breach of the duties inherent in his/her position or is subject to any of the circumstances described in section III.5 (Definitions) of this Code.

The removal of Independent Directors may also be proposed when a tender offer, merger or similar corporate transaction produces changes in the capital structure of the Company, in order to meet the proportionality criterion set out in Recommendation 12.

See sections: B.1.2, B.1.5 and B.1.26

Complies       Explain

**32.** Companies should establish rules obliging Directors to inform the Board of any circumstances that might harm the organization's name or reputation, tendering their resignation as the case may be, and, in particular, to inform the Board of any criminal proceedings in which they appear as an accused party, and of subsequent progress in the case.

Where a Director is indicted or a decision is rendered to bring him to trial for any of the crimes referred to in Article 124 of the Corporations Law, the Board should review the matter as soon as possible and, in light of the specific circumstances, decide whether or not it is appropriate for the Director to remain in office. The Board should give a reasoned account of the matter in the Annual Corporate Governance Report.

See sections: B.1.43, B.1.44

Complies

Complies partially

Explain

**33.** All Directors should express clear opposition when they feel a proposal submitted for the Board's approval could be contrary to the corporate interest. In particular, Independent and other Directors unaffected by the potential conflict of interest should challenge any decision that could harm the interests of shareholders not represented on the Board.

When the Board makes material or reiterated decisions about which a Director has expressed serious reservations, he/she must draw the pertinent conclusions. Directors resigning for such causes should explain their reasons in the letter referred to in the next Recommendation.

This Recommendation should also apply to the Secretary of the Board; Director or otherwise.

Complies

Complies partially

Explain

Not applicable

**34.** Directors who give up their positions before their term of office expires, through resignation or otherwise, should explain their reasons in a letter to be sent to all members of the Board. Regardless of whether such resignation is disclosed as a material event, the reasons for same must be explained in the Annual Corporate Governance Report.

See section: B.1.5

Complies

Complies partially

Explain

Not applicable

**35.** The Company's compensation policy, as approved by its Board of Directors, should specify at least the following items:

- a) The amount of the fixed components, itemized where necessary, of Board and Board Committee attendance fees, with an estimate of the fixed annual payment they give rise to;
- b) Variable components, in particular:
  - i) The types of Director to which they apply, with an explanation of the relative weighting of variable to fixed compensation items;
  - ii) Performance evaluation criteria used to calculate entitlement to the award of shares or share options or any performance-related compensation;
  - iii) The main parameters and grounds for any system of annual bonuses or other, non-cash benefits; and

- iv) An estimate of the absolute amount of the variable compensation arising from the proposed compensation plan, depending on the degree of compliance with the assumptions or objectives taken as a reference.
- c) The principal characteristics of pension systems (for example, supplementary pensions, life insurance and similar arrangements), with an estimate of their amount or annual equivalent cost.
- d) Conditions that must be respected in the contracts of Executive Directors exercising senior management functions. Among them:
  - i) Term;
  - ii) Notice periods; and
  - iii) Any other clauses covering hiring bonuses, as well as indemnities or 'golden parachutes' in the event of early termination of the contractual relationship between the Company and the Executive Director.

See section: B.1.15

Complies

Complies partially

Explain

**36.** Compensation in the form of the delivery of shares in the Company or other companies in the Group, share options or other share value-based instruments, payments linked to the Company's performance or pension plans should be confined to Executive Directors.

The delivery of shares is excluded from this limitation when Directors are required to retain them until they vacate office.

See section: B.1.15

Complies

Explain

**37.** External Directors' compensation should sufficiently compensate them for the dedication, abilities and responsibilities that the position entails, but should not be so high as to compromise their independence.

Complies

Explain

**38.** In the case of compensation linked to Company earnings, any qualifications stated in the external auditor's report that reduce those earnings should be taken into account.

Complies

Explain

Not applicable

**39.** In the case of variable compensation, compensation policies should include technical safeguards to ensure they reflect the professional performance of the beneficiaries and not simply the general progress of the markets or of the industry in which the Company operates, or other similar circumstances.

Complies

Explain

Not applicable



**40.** The Board should submit a report on the Directors' compensation policy to the advisory vote of the Shareholders' Meeting, as a separate item on the agenda. This report can be supplied to shareholders separately or in the manner each Company sees fit.

The report will focus on the compensation policy approved by the Board for the current year with reference, as the case may be, to the policy planned for future years. It will address all the points referred to in Recommendation 35, except those potentially entailing the disclosure of commercially sensitive information. It will also focus on the most significant changes in compensation policy compared with the previous year to which the Shareholders' Meeting refers. It also will include a global summary of how the policy was applied over the previous year.

The role of the Compensation Committee in designing the policy should be reported by the Board, along with the identity of any external advisers engaged.

See section: B.1.16 and E.8

Complies

Complies partially

Explain

**41.** The notes to the financial statements should list individual Directors' compensation in the year, including:

a) A breakdown of the compensation of each Director, to include where appropriate:

- i) Attendance fees and other fixed Director payments;
- ii) Additional compensation for acting as Chairman or a member of any Board Committee;
- iii) Any payments made under profit-sharing or bonus plans, and the reason for their award;
- iv) Contributions made on the Director's behalf to defined-contribution pension plans, or any increase in the Director's vested rights in the case of contributions to defined-benefit plans;
- v) Any severance packages agreed or paid;
- vi) Any compensation they receive as Directors of other companies in the Group;
- vii) The compensation Executive Directors receive in respect of their senior management positions;
- viii) Any compensation item other than those listed above, regardless of its nature and provenance within the Group, especially when it may be considered a related-party transaction or when its omission would detract from a true and fair view of the total compensation received by the Director.

b) An individual breakdown of deliveries to Directors of shares, share options or other share value-based instruments, itemized by:

- i) Number of shares or options awarded in the year, and the terms set for their exercise;
- ii) Number of options exercised in the year, specifying the number of shares involved and the exercise price;
- iii) Number of options outstanding at the end of the year, specifying their price, date and other exercise conditions;
- iv) Any change in the year in the terms of exercise of previously awarded options.

c) Information on the relationship in the past year between the compensation obtained by Executive Directors and the Company's earnings, or other measures of the Company's performance.

Complies

Complies partially

Explain

**42.** When the Company has a Delegated or Executive Committee (hereinafter, the Delegated Committee), the breakdown of its members by Director category should be similar to that of the Board itself. The Secretary of the Board should also act as Secretary of the Delegated Committee.

See sections: B.2.1 and B.2.6

Complies       Complies partially       Explain       Not applicable

**43.** The Board should be kept fully informed of the business transacted and decisions made by the Delegated Committee. To this end, all Board members should receive a copy of the Delegated Committee Minutes.

Complies       Explain       Not applicable

**44.** In addition to the Audit Committee required pursuant to the Securities Market Law, the Board of Directors should form a Committee, or two separate Committees, for Appointments and Compensation.

The rules governing the composition and functioning of the Audit Committee and the Appointments and Compensation Committee(s) should be set forth in the Board Regulations, and include the following:

- a) The Board of Directors should appoint the members of such Committees based on the knowledge, aptitudes and experience of its Directors and the tasks of each Committee; discuss their proposals and reports; and the Committees must report to the Board, at its first plenary session following each Committee meeting, on their activities and answer for their work;
- b) These Committees should be comprised exclusively of External Directors and have a minimum of three members. The above is without prejudice to the attendance at meetings of Executive Directors or senior executives, at the express invitation of Committee members.
- c) Committees should be chaired by Independent Directors.
- d) They may engage external advisors, when they feel this is necessary for the performance of their functions.
- e) Minutes should be drawn up of the proceedings and a copy sent to all Board members.

See sections: B.2.1 and B.2.3

Complies       Complies partially       Explain

The only limitation on full compliance with the Recommendation is the fact that the Executive Director and Chairman of the Company is a member of the Corporate Responsibility and Governance Committee, by unanimous decision of the Board of Directors, which believes it is of interest for him to be a member, so that the Committee functions more effectively, without prejudice to his abstention or absence in all matters that may personally affect him or may lead to a possible conflict of interest.

The above circumstances, their parallel with the contents of Recommendations 56 and 58, which require the broad participation and collaboration of the Chief Executive with the Corporate Responsibility and Governance Committee; the content of Recommendation 45 attributing to the Committee the supervision and submission to the Board of proposals for improvement of the corporate governance rules, a task in which the Chairman

of the Board plays an important role; and finally the fact that the rest of Recommendation 44 is fully complied with, have led to the conclusion that the Company complies with the essence of the Recommendation.

The above reasons were stated to the CNMV in July 2008, in relation to the 2007 Annual Corporate Governance Report, and were reiterated in the Company's 2008, 2009 and 2010 Annual Corporate Governance Reports.

**45.** The job of supervising compliance with internal codes of conduct and corporate governance rules should be entrusted to the Audit Committee, the Appointments Committee or to the Compliance Committee or Corporate Governance Committee, where they exist separately.

Complies  Explain

**46.** All members of the Audit Committee, particularly its Chairman, should be appointed on the basis of their knowledge and expertise in accounting, auditing and risk management matters.

Complies  Explain

**47.** Listed companies should have an internal audit function, under the supervision of the Audit Committee, to ensure the sound functioning of internal reporting and control systems.

Complies  Explain

**48.** The head of the internal audit function should present an annual work program to the Audit Committee; report to it directly on any incidents arising during its implementation; and submit an activities report at the end of each year.

Complies  Complies partially  Explain

**49.** The risk control and management policy should specify at least:

- a) The various types of risk (operating, technological, financial, legal, reputational, etc.) the Company is exposed to, including contingent liabilities and other off-balance-sheet risks among the financial or economic risks;
- b) The determination of the risk level the Company deems to be acceptable;
- c) The measures in place to mitigate the impact of the identified risks, should they occur;
- d) The internal reporting and control systems to be used to control and manage the above risks, including contingent liabilities and off-balance-sheet risks.

See section: D

Complies  Complies partially  Explain

**50.** The Audit Committee's role should be:

1. As regards internal control and reporting systems:

- a) To supervise the preparation and the integrity of the financial information prepared on the Company and, where appropriate, the Group, reviewing compliance with legal provisions, the appropriate definition of the consolidated group, and correct application of accounting principles;
- b) To regularly review internal control and risk management systems, so that the principal risks are adequately identified, managed and disclosed.
- c) To ensure the independence and efficacy of the internal audit function; propose the selection, appointment, reappointment and removal of the head of the internal audit function; propose the department's budget; receive regular information on its activities; and verify that senior management acts on the conclusions and recommendations of its reports.
- d) To establish and supervise a mechanism whereby staff can report, confidentially and, if appropriate, anonymously, any potentially significant irregularities, in particular financial or accounting irregularities, they detect at the Company.

2. As regards the external auditor:

- a) To make recommendations to the Board for the selection, appointment, reappointment and removal of the external auditor, and the terms and conditions of its engagement;
- b) To receive regular information from the external auditor on the audit plan and the results of its implementation, and check that senior management is acting on its recommendations;
- c) To ensure the independence of the external auditor, to which end:
  - i) The Company should disclose any change of auditor to the CNMV as a material event, accompanied by a statement of any disagreements with the outgoing auditor and the reasons for the same.
  - ii) The Committee should ensure that the Company and the auditor adhere to current regulations on the provision of non-audit services, the limits on concentration of the auditor's business and, in general, other requirements designed to safeguard the independence of the auditor;
  - iii) The Committee should investigate the issues giving rise to the resignation of any external auditor.
- d) In the case of groups, the group auditor should be encouraged to take responsibility for auditing all the companies in the Group.

See sections: B.1.35, B.2.2, B.2.3 and D.3

Complies

Complies partially

Explain

The Board of Directors considers it appropriate, as has been the case in the past, for the Audit Committee to supervise and control the process of selection, appointment and removal of the head of the internal audit function, and its action plans, supervising and approving the resources allocated thereto, including its budget.

Nevertheless, the Board of Directors unanimously believes that the powers to appoint and remove the head of the internal audit function and propose its budget should lie with the Company's senior management.

The Board of Directors considers that the power to supervise and control the process, more extensive than that of simply making proposals, strengthens and clarifies the content of the Recommendation itself, ensuring the suitability of the person responsible for the internal audit function and the control by

the Audit Committee of said suitability, at the same time respecting the customary channels for appointing the persons responsible for the various executive areas of the Company.

The above reasons were also stated to the CNMV in July 2008, in relation to the 2007 Annual Corporate Governance Report, and were reiterated in the Company's 2008, 2009 and 2010 Annual Corporate Governance Reports.

**51.** The Audit Committee should be empowered to meet with any Company employee or executive, even ordering their appearance without the presence of any other executive.

Complies  Explain

**52.** The Audit Committee should report to the Board, prior to the adoption by the Board of the corresponding decisions, on the matters indicated in Recommendation 8:

- a) The financial information that the Company must periodically disclose as a listed company. The Committee should ensure that interim statements are prepared using the same accounting principles as the annual statements and, to this end, may ask the external auditor to conduct a limited review.
- b) The creation or acquisition of shares in special-purpose vehicles or entities resident in countries or territories that are considered tax havens, and any other transactions or operations of an analogous nature whose complexity could impair the transparency of the Group.
- c) Related-party transactions, except where the prior reporting function has been entrusted to some other supervision and control committee.

See sections: B.2.2 and B.2.3

Complies  Complies partially  Explain

**53.** The Board of Directors should seek to present the financial statements to the Shareholders' Meeting without reservations or qualifications in the audit report. In the exceptional event that any reservations or qualifications exist, both the Chairman of the Audit Committee and the auditors should give a clear account to shareholders of their scope and content.

See section: B.1.38

Complies  Complies partially  Explain

**54.** The majority of Appointment Committee members (or Appointment and Compensation Committee members, as the case may be) should be Independent Directors.

See section: B.2.1

Complies  Complies partially  Explain

Of the four members of the Corporate Responsibility and Governance Committee, three are External Directors and two of them are Independent Directors, meaning that they constitute a relative but not absolute majority.

Further to the comments on Recommendation 44, it must again be stated that Independent Directors have a voting majority on the Corporate Responsibility and Governance Committee, since in the hypothetical event of a tie between Independent and other Directors, the Chairman, who must be an Independent Director, has a casting vote.

**55.** The Appointments Committee should have the following functions in addition to those stated in earlier Recommendations:

- a) To evaluate the balance of skills, knowledge and experience on the Board, define the roles and capabilities required of the candidates to fill each vacancy, and decide the time and dedication necessary for them to properly perform their duties.
- b) To examine or organize, in appropriate form, the process for succession of the Chairman and Chief Executive, making recommendations to the Board so the handover proceeds in a planned and orderly manner.
- c) To report on the appointment and removal of senior executives proposed by the Chief Executive to the Board;
- d) To report to the Board on the gender diversity issues discussed in Recommendation 14 of this Code.

See section: B.2.3

Complies       Complies partially       Explain       Not applicable

**56.** The Appointments Committee should consult with the Company's Chairman and Chief Executive, especially on matters relating to Executive Directors.

Any Board member may request that the Appointments Committee take into consideration, if it deems them suitable, potential candidates for any vacant directorships.

Complies       Complies partially       Explain       Not applicable

**57.** The Compensation Committee should have the following functions in addition to those stated in earlier Recommendations:

- a) To make proposals to the Board of Directors regarding:
  - i) The compensation policy for Directors and senior executives;
  - ii) The individual compensation and other contractual conditions of Executive Directors.
  - iii) The standard conditions for senior executive contracts.
- b) To ensure compliance with the compensation policy set by the Company.

See sections: B.1.14, B.1.15 and B.2.3

Complies       Complies partially       Explain       Not applicable

**58.** The Compensation Committee should consult with the Chairman and Chief Executive, especially on matters relating to Executive Directors and senior executives.

Complies       Explain       Not applicable



## G Other Information of Interest

If there is deemed to be any material aspect or principle relating to the corporate governance practices followed by the Company that has not been addressed in this report, please give details.

This section can include any other information, clarification or qualification relating to the previous sections of the Report.

In particular, indicate whether the Company is subject to any legislation other than Spanish legislation on corporate governance, and if so, include any information that it is required to furnish, where such information differs from that required in this Report.

Binding definition of Independent Director:

State whether any of the Independent Directors has or has had any relationship with the Company, its significant shareholders or its executives that, had it been sufficiently significant or important, would have resulted in the impossibility of treating the Director as an Independent Director under the definition set forth in section 5 of the Unified Good Governance Code:

YES  NO

Name of Director	Type of relationship	Explanation

This Annual Corporate Governance Report was approved by the Company's Board of Directors at the meeting held on February 27, 2012, following a favorable report from the Audit Committee and from the Corporate Responsibility and Governance Committee, at the meetings held on February 20, 2012.

Indicate whether there are any Directors who voted against or abstained from voting to approve this Report.

YES  NO

Name of Director who did not vote to approve this Report	Reason (against, abstained, absence)	Explain the reasons

Other information of interest:

Compensation for the Board of Directors and Senior Management

In addition to the information contained in sections B.1.11 to B.1.16 of this Report, it should be noted that this year the Company intends to prepare a report on Director compensation at Red Eléctrica Corporación, S.A., taking into account, insofar as the report structure and content are concerned, the new Article 61 ter of the Securities Market Law, the reporting requirements and demands of foreign international investors and their advisers, and cutting-edge corporate governance practices in Spain and abroad in this area.

The abovementioned Report offers detailed information on 2012, 2013 and following years, and on 2011.

◆ Board of Directors

The total compensation earned by members of the Company's Board of Directors in 2011, in thousands of euros, broken down by Director, was as follows:

	Fixed compensation	Variable compensation	Board meeting attendance fees	Dedication to committees	Contributions to life insurance and pension plans	Total
Mr. Luis M <sup>a</sup> Atienza Serna	404	316	56	29	17	822
Mr. Antonio Garamendi Lecanda	—	97	56	29	—	182
Mr. Manuel Alves Torres <sup>(1)</sup>	—	97	56	29	—	182
Mr. Rafael Suñol Trepas	—	97	56	—	—	153
Ms. M <sup>a</sup> Ángeles Amador Millán	—	97	56	29	—	182
Mr. Francisco Javier Salas Collantes	—	97	56	17	—	170
Mr. José Folgado Blanco	—	97	56	12	—	165
Ms. Arantza Mendizábal Gorostiaga	—	97	56	29	—	182
Ms. M <sup>a</sup> Jesús Álvarez González <sup>(1)</sup>	—	97	56	29	—	182
Mr. Miguel Boyer Salvador	—	97	56	—	—	153
Mr. Rui Manuel Janes Cartaxo	—	97	56	—	—	153
<b>Total compensation</b>	404	1,286	616	203	17	2,526

(1) Amounts received by SEPI.

In addition, the Executive Director has allocated €56,000 to the retirement-linked group saving-life insurance policy against compensation outstanding from previous years.

The annual variable compensation of the Executive Director is established by the Corporate Responsibility and Governance Committee at the start of each year using quantifiable and pre-determined objective criteria. The targets are in line with the strategies and steps established in the Company's Strategic Plan and the Corporate Responsibility and Governance Committee is also responsible for assessing the level of achievement of the targets.

In 2009, an Executive Compensation Plan (2009-2013 "Plan Extraordinario 25<sup>a</sup> aniversario") was established, including the Executive Director, linked to the 25th anniversary of the Company, as a management tool and an incentive to drive fulfillment of the five-year Strategic Plan. Compliance with the Plan will be assessed at the end of its term in 2014. Depending on the level of achievement of the targets set, the overall assessment for the five years may be up to 1.8 times the fixed annual compensation. As with the annual targets, the Plan takes into account quantifiable and pre-determined objective criteria which are in keeping with the medium and long-term vision of the Company's Strategic Plan, and the establishment and assessment of the targets falls to the Corporate Responsibility and Governance Committee. At December 31, 2011 the Company has recorded an accrual proportional to the period



elapsed under the assumption that the targets set in the Plan will be met in 2013; this accrual will not be recognized individually as compensation until compliance with the Plan in 2014 is assessed, or failing this, if prior to that date the relationship between the Company and the executives included in the program ends, for the causes envisaged in the program.

There are safeguard or golden parachute clauses in favor of the Executive Director to cover dismissal or changes in control. These clauses were proposed by the Appointments, Compensation and Corporate Governance Committee (now the Corporate Responsibility and Governance Committee) and approved by the Board of Directors. These clauses are in line with standard market practice and cover the termination of the employment relationship, providing for indemnification of one year's salary, unless the applicable legislation provides for a higher amount.

At December 31, 2011 and 2010 there were no loans, advances or guarantees established by the Company in favor of members of the Board of Directors reflected on the balance sheet. There were also no pension liabilities incurred vis-à-vis members of the Board of Directors at those dates.

◆ Senior Management:

In 2011, compensation and contributions to life insurance and pension plans for senior executives amounted to €966,000 and €57,000, respectively (€957,000 and €30,000, respectively, in 2010). In addition, these senior executives have allocated €34,000 to the retirement-linked group saving-life insurance policy against compensation outstanding from previous years.

There were no loans or advances to senior executives at December 31, 2011 or 2010.

There are safeguard or golden parachute clauses for dismissal in favor of two senior executives. These clauses are in line with standard market practice and cover the termination of the employment relationship, providing for indemnification of up to two years' salary, unless the applicable legislation provides for a higher amount. The agreements containing these clauses were approved by the Appointments, Compensation and Corporate Governance Committee and were duly notified to the Board of Directors.

In 2009, an Executive Compensation Plan (2009-2013 "*Plan Extraordinario 25º aniversario*") was established, linked to the 25th anniversary of the Company, as a management tool and an incentive to drive fulfillment of the five-year Strategic Plan. Compliance with the Plan, which includes the senior executives, will be assessed at the end of its term in 2014. Depending on the level of achievement of the targets set, the overall assessment for the five years may be up to 1.8 times the fixed annual compensation. As with the annual targets, this plan takes into account quantifiable and pre-determined objective criteria which are in keeping with the medium and long-term vision of the Company's Strategic Plan, and the establishment and assessment of the targets falls to the Corporate Responsibility and Governance Committee. At December 31, 2011 the Company has recorded an accrual proportional to the period elapsed under the assumption that the targets set in the Plan will be met in 2013; this accrual will not be recognized individually as compensation until compliance with the Plan in 2014 is assessed, or failing this, if prior to that date the relationship between the Company and the Executives included in the program ends, for the causes envisaged in the program.

For further information, please see the Annual Directors' Compensation Report for 2011 which will be available shortly.

### Professional experience of the Executive Director and the External Nominee Directors

In addition to the information provided in section B.1.3, which, together with other information, provides a brief summary of the profile and professional career of each of the External Independent Directors on the Board of Directors, and in order to make available to all the Shareholders similar information on the other members of the Board of Directors of Red Eléctrica Corporación, S.A., set out below is the same information regarding the Executive Director and the External Nominee Directors:

#### Chairman, Executive Director

**Luis M<sup>a</sup> Atienza Serna**, born August 30, 1957.

Degree in Economics and Business Studies, Universidad de Deusto.

Certificate in Advanced European Studies, Université de Nancy (France), Center for Advanced European Studies.

Certificate in Development Economics (D.E.A.), Université de Nancy, Faculty of Law and Economics.

#### Formerly:

Minister for Agriculture, Fisheries and Food.

Secretary General for Energy and Mineral Resources, Ministry of Industry and Energy.

Chairman, Institute for Energy Saving and Diversification (IDAE).

Chairman, Geomining Technological Institute of Spain.

Chairman, Centre for Energy, Environmental and Technological Research (CIEMAT).

Secretary General, Agrarian Structures, Ministry of Agriculture, Fisheries and Food.

Regional Economy Minister, Basque Autonomous Community Government.

Member of the Basque Regional Parliament.

Lecturer, Faculty of Economics and Business Studies, and International Business Administration Institute, and Institute for European Studies, Universidad de Deusto.

Member of the Boards of Directors of Instituto Nacional de Hidrocarburos (INH), Corporación Logística de Hidrocarburos (CLH) and Ente Vasco de la Energía (EVE).

He has given many courses, seminars and lectures, and has published articles on economic, energy and agrarian policy and European research in the economic and general press, including working documents for university institutes and research centers.

#### Currently:

Member of the Board of the European Network of Transmission System Operators for Electricity (ENTSO-e).

President, Very Large Power Grid Operators (VLPGO-GO14).

President, Asociación Tertulias Hispano-Británicas.

Individual representative of the corporate Director Red Eléctrica Corporación, S.A. on the Board of Directors of the Portuguese company REN-REDES ENERGÉTICAS NACIONAIS, SGPS.

**External Nominee Director proposed by SEPI**

**Rafael Suñol Trepas**, born July 4, 1944.

Degree in Economics and Business Studies, E-1969, ADE-ESADE 1980, PADE-IESE 1999.

**Formerly:**

Managing Director of Aurica, SCR, S.A.

Partner of Socios Financieros and President of Activa Ventures.

Director and Deputy Chairman of Fecsa and Director of Endesa.

Managing Director of Banco de Fomento.

Chairman of Banco de Crédito Industrial and Director of ICO.

Assistant General Manager of GDS, Caja de Barcelona, after working for Banco Urquijo, Barcelona.

Chairman of Crédito & Docks and of Dinvergestión, and Director of companies related to Banco Central.

Director of Ericsson España, Frida Alimentaria and Visual Tools, and Chairman of Cobrhi.

**Currently:**

Director of Peugeot España, Inypsa, Serveis Funeraris de Barcelona and Mémora y Dalkia España.

**External Nominee Director proposed by SEPI**

**Manuel Alves Torres**, born March 18, 1954.

Degree in Economics and Business Studies.

**Formerly:**

Head of Budgeting, Standard Eléctrica, S.A.

Graduate Technical Expert, Assistant Manager of Companies and Corporate Sub-Manager, INI.

Planning and Supervision Manager at INI, Teneo and SEPI.

Member of the Board of Directors of: Potasas de Subiza, Potasas de Suria, Grupo Ence, Grupo Inespal, Enatcar, Clínica Castelló, Minas de Almagrera, Agencia Efe, Binter Canarias, Hipódromo de la Zarzuela and Sedettur.

**Currently:**

Planning and Control Manager, SEPI.

Member, Management Committee, SEPI.

SEPI representative, Fundación SEPI (formerly Fundación Empresa Pública) and Fundación Laboral SEPI.

Member, Board of Directors, Tragsa.

### External Nominee Director proposed by SEPI

**María Jesús Álvarez González**, born June 21, 1957.

Degree in Economics and Business Studies.

#### Formerly:

Member, Board of Directors, Enusa Industrias Avanzadas, S.A.

Member, Board of Directors, Equipos Nucleares, S.A.

Member, Board of Directors, Clínica Castelló, S.A.

Member, Board of Directors, Indra Sistemas, S.A.

Member, Board of Directors, Infoinvest, S.A.

Member, Board of Directors, Infoleasing, S.A.

Member, Board of Directors, Empresa Nacional de Residuos Radioactivos, S.A. (ENRESA).

Member, Board of Directors, Aluminio Español, S.A.

Member, Board of Directors, Agencia Efe, S.A.

She has held various executive positions within SEPI and has engaged in various activities in the banking and industrial sectors.

#### Currently:

Economics-Finance Manager, SEPI.

Member of the Management Committee of SEPI.

Member, Board of Trustees of Fundación SEPI and of Fundación Laboral SEPI.

### Director attendance at meetings

There were seven (7) absences from the eleven (11) Board meetings held in 2011, representing an attendance rate of 94%.

### Company Chairman Succession Plan

At a meeting held on October 27, 2011 the Board of Directors approved the Succession Plan for the Company Chairman, following an increasingly common corporate governance practice worldwide, consisting in preparation and approval by listed companies of succession plans for their CEO or most senior executive, to minimize the impact of the handover on the organization, aiming to determine a model profile for the candidates and to ensure continuity in the corporate business, reducing insofar as possible the possible risks or negative effects of the appointment of a new chairman, until he or she is fully integrated into the post. The Company Chairman Succession Plan was approved on the basis of the special conditions present in Red Eléctrica's chief executive, which position is held by the Chairman of the

Board of Directors, as established in Article 25 of the Corporate Bylaws. The Plan establishes a succession process split into several stages, attributing responsibilities to the different bodies concerned. All the above is to create an environment in which the appointment of a new chairman is made in an orderly and efficient manner that does not affect the Company's normal operations.

#### Relations with institutional investors

Relations between the Company and institutional investors are general in nature and no specific or special relationships are held with any of them.

The Company regularly organizes road shows at principal financial centers in Spain and abroad where there is a high concentration of institutional investors, to inform them of its activities and its business performance, in an attempt to forge closer ties with this group of investors.

In light of the high percentage of foreign institutional shareholders (close to 70% in 2011), and as in previous years, the Company has conducted visits to investors and proxy advisors to explain its corporate governance practices and policies to them directly, aiming to establish appropriate mechanisms for the regular exchange of information with Spanish and foreign institutional investors and with the main proxy advisors, with a view to continuing to adapt to the most advanced international corporate governance standards.

Under no circumstances does the Company disclose to institutional shareholders any information that might place them in a privileged or advantageous situation vis-à-vis the other shareholders, in accordance with the provisions of the Board Regulations.

## Annex 2

### ADDITIONAL INFORMATION FOR ARTICLE 61 BIS OF SECURITIES MARKET LAW 24/1988, OF JULY 28, 1988

**I.** Information about securities that are not traded on an official market in the EU, stating, whenever appropriate, the different classes of shares and the rights and obligations pertaining to each class of shares and the percentage of the capital it represents, as well as the percentage of capital represented by the company's treasury stock and any major changes therein (Art. 61 bis 4, a, 3 LMV).

None of the Company's shares are traded on an official market in the EU.

The percentage of the capital accounted for by the treasury stock held by the company is 0.493% and major changes in this figure are set out in sections A.8 and A.9 of the Annual Corporate Governance Report.

**II.** Any restriction on the transferability of securities and any restriction on voting rights (Article 61 bis 4, b LMV).

The transfer of the shares representing the capital of Red Eléctrica Corporación, S.A. is free and is not subject to any restriction.

As for all listed entities, the acquisition of certain significant holdings must be notified to the issuer and to the CNMV, as provided in Article 53 of Securities Market Law 24/1988 of July 28, 1988, in Royal Decree 1362/2007 of October 19, 2007, and in CNMV Circular 2/2007 of December 19, 2007, which establish the first notification threshold at 3% of capital or voting rights.

Each share gives the right to one vote and all shareholders are entitled to attend Shareholders' Meetings, without any required minimum number of shares, as was the case until the Special Shareholders' Meeting of July 17, 2003, which removed the bylaw requirement to hold at least 50 shares in order to attend Shareholders' Meetings.

Various amendments to Electricity Industry Law 54/1997 of November 27, 1997, affecting restrictions on voting rights were introduced with the entry into force of Law 17/2007 of July 4, 2007, amending Electricity Industry Law 54/1997 to adapt it to the provisions of Directive 2003/54/EC of the European Parliament and of the Council of June 26, 2003 concerning common rules for the internal market in electricity, a Community provision that has been superseded by Directive 2009/72/EC of July 13, 2009, which proclaims the mandatory independence of transmission companies and operators of European electricity systems.

Specifically, Subprovision two of Additional Provision Three of Law 17/2007 established new maximum limits on the exercise of voting rights, in order to guarantee the independence of a company engaging in regulated activities in the electricity industry which, pursuant to Electricity Industry Law 54/1997 of November 27, 1997, constitute an essential service.

Thus, any individual or legal entity may hold shares in the Company, provided that the sum of their direct and indirect interests in the Company's capital does not exceed five percent of capital and they do not exercise more than three percent of voting rights. These shares may not be pooled for any purpose whatsoever.

Parties that pursue activities in the electricity industry, and those individuals or legal entities that directly or indirectly hold more than five percent of their capital, may not exercise more than one percent of voting rights at the company responsible for operation of the system.

The special regime for Sociedad Estatal de Participaciones Industriales (SEPI) remains unchanged, whereby it must hold at least ten percent (10%) of capital in all cases.

There are no other additional bylaw restrictions differing from purely legal restrictions.

In turn, the National Energy Commission is authorized to take legal action to enforce the aforementioned statutory limits. Breach of the established shareholding limits constitutes a very serious infringement under the Electricity Industry Law and the individuals or legal entities that own the securities or to whom the excess shareholding is attributable will be liable.

The legal regime established by Directive 2009/72/EC, of July 13, 2009, which proclaims the mandatory independence of transmission companies and operators of European electricity systems has endorsed the legal limitations on shareholders established in Law 17/2007.

### III. Information about the rules applying to the altering of the Corporate Bylaws (Article 61 bis 4,a,4 LMV).

The amendment of the Corporate Bylaws introduces no new features other than the corporate legal system provided for in Article 290 of the Corporate Enterprise Law and which requires approval by the Shareholders' Meeting, with the majorities provided for in Article 194 of said Law. The competencies of the Shareholders' Meeting set out in Article 11 c) of the Corporate Bylaws and Article 3 c) of the Shareholders' Meeting Regulations, expressly include the amendment of the Corporate Bylaws, without stipulating any majority other than those set out in the Law.

IV. Information about the major agreements entered into by the Company that come into force, are changed or terminate in the event that the control of the Company changes as a result of a tender offer, and its effects, except when disclosing them would seriously damage the company's interests. This exception shall not apply when the company is legally required to disclose this information to the public (Article 61 bis 4, c, 4 LMV).

The Company has not entered into any agreements that come into force, are changed or terminate in the event of a change in control of the Company as a result of a tender offer for the shares.

**V. Information about agreements between the company and its managers, executives or employees which provide for indemnification in the event of their resignation or unjustified dismissal or in the event that the employment relationship ends as a result of a tender offer (Article 61 bis 4, c, 5 LMV).**

There are safeguard or golden parachute clauses in favor of the Executive Director to cover dismissal or changes in control. These clauses were proposed by the Appointments, Compensation and Corporate Governance Committee (now called the Corporate Responsibility and Governance Committee) and approved by the Board of Directors. These clauses are in line with standard market practices and cover the termination of the employment relationship, providing for indemnification of one year's salary, unless the applicable legislation provides for a higher amount.

There are safeguard or golden parachute clauses in favor of two Company executives. These clauses are in line with standard market practices and cover the termination of the employment relationship, providing for indemnification of up to two years' salary, unless the applicable legislation provides for a higher amount. The contracts containing these clauses were approved by the Appointments, Compensation and Corporate Governance Committee and they were duly notified to the Board of Directors.

**VI. Information about the powers of the members of the Board of Directors and, in particular, those relating to the possibility of issuing or buying back shares (Article 61 bis 4, c, 3 LMV).**

The new Corporate Enterprises Law (LSC) has consolidated the legal regime applicable to the treasury stock of companies established in Law 3/2009, of April 3, 2009, on Structural Modifications to Commercial Companies, without introducing any material amendments to the regime.

In light of the foregoing, and although the authorization approved by the Shareholders' Meeting on May 20, 2010, in relation to the award of treasury shares, as compensation, to employees of the Company and of the RED ELÉCTRICA Group, was still in force, pursuant to the law, for another four years, it was submitted for approval by the Shareholders' Meeting held on April 13, 2011. It was intended that the shareholders renew the authorization granted last year, in accordance with the most recent corporate governance practices. As a separate item on the agenda, it was also intended to establish a Compensation Plan for members of Senior Management and the Executive Directors of Red Eléctrica Corporación, S.A., which may be extended to companies in its Consolidated Group, allowing part of their compensation to be awarded in the form of Company shares, on the same terms as last year. This Plan requires a resolution with certain legally established conditions.

Accordingly, the Shareholders' Meeting of the Company held on April 13, 2011, gave an authorization to the Board of Directors, pursuant to the provisions of Article 146 and related provisions of the Corporate Enterprises Law and other applicable legislation, for the derivative acquisition of treasury stock in Red Eléctrica Corporación, S.A. by the Company itself and by companies of the Red Eléctrica Group directly or indirectly and insofar as the Board of Directors considers that the circumstances so dictate, subject to the following conditions:

- ◆ The maximum number of shares to be acquired shall not exceed the legal limit. The maximum number of shares to be acquired must not exceed the established legal limit, provided that the other applicable legal requirements can also be fulfilled.



- ◆ Acquisitions cannot be made for a consideration higher than the market value of the shares at the time of acquisition, or for a consideration lower than 50% of the market price at that time.
- ◆ The methods of acquisition may consist of sale and purchase, swap or any other type of transaction for consideration or for no consideration, as the circumstances so dictate. In the case of acquisition for no consideration, pursuant to the provisions of Article 146.4 of the Corporate Enterprises Law, the shares acquired may be partially paid-in.
- ◆ Pursuant to the provisions of Article 146.1 b) of the Corporate Enterprises Law, the acquisition, including any shares previously acquired by the Company and held as treasury stock, may not have the effect of leaving net worth below the amount of capital stock plus legal reserves or restricted reserves pursuant to the bylaws.

For these purposes, 'net worth' will be considered the amount classed as such pursuant to the criteria used to prepare the financial statements, reduced by the amount of income attributed directly to same and increased by the amount of uncalled subscribed capital stock, as well as by the nominal amount and the subscribed additional paid-in capital recorded for accounting purposes as shareholders' equity.

In accordance with paragraph three of Article 146.1 a) of the Corporate Enterprises Law, the Board of Directors of the Company may use some or all of the treasury stock acquired under this authorization and the treasury stock already owned by the Company on the date of approval of the resolution to implement compensation programs consisting of the direct award of shares to employees and Executive Directors of the Company and of the companies belonging to the RED ELÉCTRICA Group.

For all of the foregoing, an authorization as broad as may be necessary is granted to the Board of Directors to request all such authorizations and adopt all such resolutions as may be necessary or appropriate for compliance with the legislation in force, and the implementation and successful outcome of this resolution.

The term of this authorization will be five (5) years as from the date of this Shareholders' Meeting.

The Shareholders' Meeting expressly revoked and, therefore, rendered ineffective the authorization for the derivative acquisition of treasury stock given to the Board of Directors by the Shareholders' Meeting held on May 20, 2010.

The Shareholders' Meeting held on May 20, 2010, delegated to the Board of Directors, for a period of five (5) years, the power to increase capital, at any time, on one or more occasions, up to a maximum amount of one hundred and thirty-five million, two hundred and seventy thousand euros (€135,270,000), equal to half of the current capital, in the amount and at the issue price decided on in each case by the Board of Directors, with the power to exclude, in whole or in part, the preemptive subscription right and with express authorization to redraft, as the case may be, Article 5 of the Corporate Bylaws and to request, as the case may be, the admission, continued listing and/or delisting of the shares on organized secondary markets.

The Shareholders' Meeting held on May 20, 2010, also delegated to the Board of Directors, for a period of five (5) years, and with a combined limit of five thousand million euros (€5,000,000,000), powers to issue, on one or more occasions, directly or through companies of the Red Eléctrica Group, debentures, bonds and other fixed-income instruments or debt instruments of an analogous nature, both nonconvertible and convertible or exchangeable for shares of the Company, of other companies of the Red Eléctrica Group or of other companies not related to same, including, without limitation, promissory notes,

securitization bonds, preferred participations and warrants giving entitlement to the delivery of shares of the Company or of other companies of the Red Eléctrica Group, whether newly-issued or in circulation, with the express power to exclude, in whole or in part, the pre-emptive subscription right; authorization to enable the Company to secure new issues of fixed-income securities (including convertible or exchangeable securities) made by companies of the Red Eléctrica Group; authorization to redraft, as the case may be, Article 5 of the Corporate Bylaws and to request, as the case may be, the admission, continued listing and/or delisting of the shares on organized secondary markets.

Both the Annual Shareholders' Meeting held on April 13, 2011 and the Shareholders' Meeting held on May 20, 2010, adopted a resolution to delegate powers to the members of the Board of Directors to implement all of the Resolutions adopted by the Annual Shareholders' Meeting. The Resolution states: *"Without prejudice to the authorizations expressly conferred by the Shareholders' Meeting on the Board of Directors, the broadest powers are delegated to the Chairman and to each member of the Company's Board of Directors, as well as the Secretary and Deputy Secretary of the Board, so that they may exercise them, individually, with a view to the implementation, execution and registration of each and every one of the resolutions adopted by this Shareholders' Meeting, including the signature of the corresponding contracts and documents, with the clauses and conditions they deem appropriate, and interpret, remedy and complete the aforementioned resolutions and have them notarized, according to their effectiveness and the comments of any body or authority, in particular the oral or written comments of the Mercantile Registrar, performing all such steps as may be necessary or appropriate to ensure their successful outcome and, in particular, to ensure the registration at the Mercantile Registry of the registrable resolutions"*. Furthermore, Article 25 of the Corporate Bylaws stipulates that the Chairman of the Board of Directors is the Chairman of the Company and of all its governing and administrative bodies, and he has the job of ensuring that the resolutions of the Board of Directors, which he represents on a permanent basis, are implemented. The power to represent the Company, in and out of court, is held by the Chairman of the Company, in addition to the Board of Directors. The Chairman of the Company is the senior manager of all the Company's services and signs for, administers and represents the Company in all matters, in and out of court, and is authorized to adopt, for reasons of urgency, the measures he deems appropriate in the interests of the Company, but must immediately report on such measures to the Board of Directors.

In this connection, the Board meeting held on June 25, 2009 unanimously resolved, as proposed by the Corporate Responsibility and Governance Committee: *"To delegate to the Chairman of the Board of Directors of RED ELÉCTRICA CORPORACIÓN, S.A., Mr. Luis María Atienza Serna, pursuant to the provisions of Article 141 of the current Corporations Law (currently regulated in Article 249 of the Corporate Enterprises Law), Article 149 of the Mercantile Registry Regulations, Article 22 of the Corporate Bylaws and Article 5 of the Board Regulations, all powers of the Board of Directors that may be delegated by law and pursuant to the Bylaws"*.

In addition to the powers that have been expressly delegated to him, the Chairman is authorized by the Corporate Bylaws to adopt, for reasons of urgency, the measures he deems appropriate in the interests of the Company, immediately informing the Board of such measures and reporting regularly to the Board, at its ordinary meetings, on the corporate management of the different areas of the Company, requesting, as the case may be, approval of the resolutions submitted. The creation, in 1999, of the Audit Committee and the Appointments, Compensation and Corporate Governance Committee (now called the Corporate Responsibility and Governance Committee), entirely composed of members of the Board of Directors specializing in matters within their sphere of responsibility, specific control exercised over the basic and strategic responsibilities of the Company, which in no event will be performed exclusively by the Chairman.

Notwithstanding the powers delegated to the Chairman, in practice, it is the Board of Directors meeting in plenary session that adopts the strategic and significant decisions for the Company.

## VII. Description of the major features of the internal control and risk management systems in connection with the process of financial reporting (Article 61 bis 4, h LMV).

The Red Eléctrica Group (for the purposes of this section REE) has, as part of its internal control systems, a System for Internal Control of Financial Reporting (hereinafter referred to as ICFR), for the purposes of meeting the requirements imposed with regard to the reliability and transparency of the process of generating financial information.

The ICFR in place at REE involves the entire Organization by implementing and monitoring on a regular basis the functioning of different controls in the area of the generation of financial information.

The ICFR currently in force at REE arose as a result of a voluntary project for improvement embarked on by the Company. The ICFR resulting from the project, with updated mechanisms, has been reviewed by an independent third party since 2008.

REE's ICFR is in line with the standard legal references in the area of internal control (including those relating to the COSO framework).

In addition to the above, REE has followed the recommendations included in the "Report on the System for Internal Control of Financial Reporting" drawn up by the Internal Control Working Group on financial reporting at the financial institutions set up by the National Securities Market Commission (CNMV), which uses the COSO framework as a benchmark, and which defines a set of principles and good practices which are grouped into 5 components and detailed in 16 indicators.

The basic structure of REE's ICFR is formally documented in the "REE ICFR Manual". The main elements characterizing the ICFR are as set out below:

- ◆ General controls: transversal controls throughout the entire organization which, as applicable, have a particular use at the level of the REE ICFR. Connected with these general controls, there are the "indicator assessment items" (IEIs) which provide a broader picture of the area of overall control in the ICFR.
- ◆ Controls designed in the processes, deployed in:
  - Areas affected by the ICFR:
    - ◆ Acquisitions.
    - ◆ Fixed Assets.
    - ◆ Inventories.
    - ◆ Revenues.
    - ◆ Payroll and Staff.
    - ◆ Financial Management.
    - ◆ Support Services.
    - ◆ Financial Reporting.

- 26 formally documented cycles.
- 45 formally documented sub-cycles.

Every one of these areas, cycles and sub-cycles have been formally documented in the Corporate Modeler computer tool.

Set out below is a more in-depth description of the major attributes characterizing the REE ICFR.

## Mechanisms that make up the control and risk management systems in connection with the financial reporting process (ICFR) of the entity.

### 1. THE ENTITY'S CONTROL ENVIRONMENT

#### 1.1 Bodies and/or functions responsible for: (i) the existence and upkeep of an adequate, effective ICFR; (ii) its implementation and (iii) its supervision.

REE's control environment has been designed on the basis of various different elements that make for an internal control atmosphere that favors the generation of full, reliable and appropriate financial information, anticipating, as necessary, the possible existence of irregularities and/or errors in order that they may be remedied. There are therefore specific Departments, Corporate Bodies and organizational units that develop, maintain and supervise everything connected with the model in the area of the entire process of preparing financial information.

Specifically, the defined functions of the Board of Directors (according to Article 5.6 vii) of the REE Board Regulations) include: the «*approval of the policy for control and management of the principal risks of the Company and of the Group, and knowledge and periodic monitoring of internal control, prevention and reporting systems. The control and risk management policy shall identify at least the following: the different kinds of risk (operating, technological, financial, legal, reputational, etc.) the Company and the Group are exposed to, including contingent liabilities and other off-balance-sheet risks among the financial or economic risks. The determination of the risk level the Company deems to be acceptable. The measures envisaged to mitigate the impact of the identified risks, should they materialize. The internal reporting and control systems to be used to control and manage the above risks, including contingent liabilities and off-balance-sheet risks*».

In line with what has been described in section 1.2., there are different organizational levels at REE that are in charge of maintaining, implementing and supervising the ICFR.

In this regard, of note are the steps taken in the area of the Directorate-General of Administration and Finance as the part of senior management responsible for designing, implementing and operating the ICFR and ensuring that it is efficient and up-to-date, and, on the other hand, by the Internal Audit Function of the Audit Committee which, by way of the annual action plan, helps to assess the efficiency of the ICFR and periodically reports any weaknesses detected.

Finally, the different organizational units of the Group are jointly responsible for the controls defined for their areas of responsibility.

## 1.2 List of existing items relating to the financial reporting process.

Departments and/or mechanisms in charge of: (i) designing and reviewing the organizational structure; (ii) clearly defining the lines of responsibility and authority, with a suitable distribution of tasks and duties and (iii) that there are sufficient procedures for it to be properly disclosed throughout the company, in particular, in connection with the financial reporting process.

REE's Human Resources Department has the job of defining the basic structure of the organization, defining the different levels of authority and the consequent levels of responsibility. All of this aims to maintain a design structure, which is implemented, reviewed and updated constantly.

In addition, the Directorate-General of Administration and Finance, the Human Resources Department, the Corporate Governance Department, and the Office of the Secretary to the Board of Directors take an active part in helping to draw up other benchmark internal documents, such as the «Revised Text of the Corporate Bylaws», the «Internal Code of Conduct on the Securities Markets», the «Corporate Responsibility Manual» and the "Code of Ethics and Corporate Values" which, among other aspects, further define the general framework of the organizational structure, at the level of duties and of responsibilities; as a complement to these benchmarks for internal rules, the ICFR Action Guide attributes the special characteristics that may be required in the area of the System for Internal Control of Financial Reporting, including the functions of maintaining, updating and supervising the ICFR at each of the different levels of responsibility that have been described, emphasizing that the Directorate-General of Administration and Finance has delegated part of its tasks to the Economic Department and to the Accounting Information and Administration Department.

Moreover, additional rules and regulations have been defined that are binding at the level of the main corporate bodies, and at the level of senior management, together with compulsory procedures at the different stages that are performed throughout the tasks relating to preparing, reviewing and approving the closing of the Financial Statements of the companies that belong to REE.

This entire structure is aimed at ensuring, inter alia, that the organizational structure set up provides a sound model in the ICFR environment.

Code of conduct, approving body, degree of disclosure and instruction, principles and values included (stating whether there are any specific mentions of the recording of operations and preparation of financial information), the body tasked with analyzing any breaches and proposing corrective measures and penalties.

An appropriate framework of conduct, which sets specific values and guidelines for action, reinforces the bases in order to achieve the objective of reliable and transparent financial information.

In this regard, at REE, there are elements that refer to the «Internal Rules of Conduct in the Securities Markets», «Code of Ethics and Corporate Values» and «Corporate Responsibility Policies of Red Eléctrica de España S.A.U.», which set the ethical values and principles of the Company as regards compliance with law, integrity, responsibility and transparency, use of data and of the information systems, among others. With the aim of achieving the highest level of rigor among REE employees, the Company has implemented a system for detecting and handling breaches and reports of breach of the code of ethics that is completely anonymous, with a view to informing senior management of any improper practices, among other aspects, connected with the processes for preparing financial information. REE ensures that any reports made remain entirely anonymous.

The «Code of Ethics and Corporate Values» is approved by REE's Board of Directors and is incumbent upon everyone at REE in the exercise of their functions and responsibilities in all professional areas in which they represent the Company, this being understood to include the employees, executives and directors. These individuals receive a copy of the «Code of Ethics and Corporate Values», together with appropriate training, either by attending courses and/or distance training, which is also permanently available in the internal rules and on the corporate website.

The «Code of Ethics and Corporate Values» is reviewed on a regular basis in order to bring its requirements into line with the needs of the Company and its relationship with the environment and with its stakeholders.

The «Code of Ethics and Corporate Values» sets out the following aspects relating to economic and financial information:

#### Chapter I Description of the values, including the following:

- ◆ *«Visible commitment to society, indicating that: the companies in the Group shall engage in actions and projects that reduce the problems and needs of society in a transparent way, so that the development and economic growth of the business is in harmony with that of society.*
- ◆ *Pride of belonging: involvement in the business project, assuming the vision, strategies and policies of each company in the Group, loyalty, trust in the management carried on and a responsible attitude involved in protecting the company's interests, strengthens its value and conveys an image of a united, firm, consolidated business.*
- ◆ *Focus on constant improvement: the commitment to excellence in management is supported by efficient systems and processes, systematically seeking out improvements, identifying and applying best practices, internally analyzing the results obtained and studying the position and development of the company with regard to the industry and the markets. The integrated, prioritized management of these activities is the main channel for ensuring the permanence and growth of the companies in the Group in the industries in which they are operate. The competencies and capacities of the companies in the Group are key factors that need to be developed, both by the directors and executives of the Group and by its workers (training, detection of best practices and technological advances).*
- ◆ *Quality and service to stakeholders: stakeholders are groups or entities that are or may be affected by the services or activities of the business and others whose opinions or decisions affect the economic results or the reputation of the companies in the Group. Product development and presentation of the services of the company should be aimed at achieving satisfaction among stakeholders. This factor is the main platform for achieving excellent results and for the positive development of the Group in the short, medium and long term».*

Channel for reporting financial and accounting irregularities to the Audit Committee, in addition to any breach of the code of conduct and any irregular activities at the organization, stating, as applicable, if it concerns a confidential matter.

In this regard, Chapter IV of the "Code of Ethics and Corporate Values" establishes: System for detecting and handling breaches and reports of breach of the code of ethics, setting out in detail the procedure to be followed in order to make any kind of notification under the following premises:

*«The system for receiving and handling any breaches and reports of breach of the Code of Ethics shall be administered by the Ethics Manager, in collaboration with the Chairman and the chairmen of the Audit Committee and Appointment and Compensation Committee. This individual shall be appointed by the Chairman of the Company and shall act independently and report to the Management Committee at the end of each financial year in the manner and as often as is stipulated in the management process.*

*Any employee of the Group or any stakeholder may report any alleged breaches of the Code of ethics that he or she detects at any of the companies in the Group or by any employee.*

*Reports shall preferably be sent by e-mail. In the Corporate Responsibility section of the website of each company there will be a channel that may be used to send reports to the Ethics Manager electronically, without the company knowing.*

*The Ethics Manager will analyze the information submitted, request the relevant evidence and, whenever appropriate, submit dossiers with all the information he possesses to the Chairman. If the report concerns any member of the Management Committee or of the Board of Directors, it shall be submitted to the chairman of the Audit Committee or, as the case may be, to the chairman of the Appointments and Compensation Committee.*

*In order for a report to be received and accepted as valid, the following elements are required:*

- Full name of the reporting party with identity number or corresponding identification code.*
- Arguments or true and precise evidence to support the report.*
- Person or group reported (including the business as a whole).*

*The system shall ensure that there are no reprisals and that confidentiality is assured in all stages. The Ethics Manager shall sign a confidentiality agreement which, should it be breached, may lead to claims for damages as deemed appropriate, and shall be answerable to the relevant judicial bodies.*

*However, reports that do not include the identity of the reporting party may also be assessed and handled if the evidence submitted and the subsequent investigation proves that there has been an actual breach».*

Training and regular refresher programs for the staff involved in preparing and reviewing the financial information, and in the assessment of the ICFR, which cover at least, accounting policies, auditing, internal control and risk management.

In this regard, the Human Resources Department manages and plans all matters concerning programs and other support items for all REE staff and, in particular, concerning items that are connected with specific training in accounting subjects, internal control and risk management, which are organized for staff in the Accounting and Administration, Internal Control and Internal Audit units, as required.

In the first instance, the different training programs are coordinated with the units that request them, and are then proposed and subsequently approved to be carried out in the current year.

Ongoing checks are carried out, at both department and employee level, assessing the number of training hours accumulated throughout the year.

Among the subjects taught to staff, the following training programs are particularly noteworthy: «New National Chart of Accounts», «International Accounting Standards», «Analysis of Financial Statements», «Systems for internal control over financial reporting», etc.

## 2. Assessment of risks of the financial information

### Major features of the process for identifying risks, including error or fraud.

The risk identification process is established as one of the fundamental cores underlying the analysis of the risks associated with the process for preparing financial information. Resting on this core are the «Integrated Risk Management Group Policies» which serve as a reference point in this connection, since they set out the guiding principles by which the Company may effectively deal with uncertainty, its associated risks and opportunities, thereby improving the ability to generate value and facilitating the achievement of the Organization's goals, such as the reliability of the financial information.

In this connection, «*The purpose of the REE Risk Policy, approved by the Board of Directors on July 24, 2008, is to establish principles and guidelines to ensure the systematic identification, analysis, assessment, management and control of material risks that may affect REE's objectives and activities, applying uniform criteria, within the established risk limits*».

Material risks of REE are those that may significantly affect the overall objectives of REE, related to:

- ◆ Sustained creation of value over time. Sustained profit growth, which must allow appropriate returns for investors and enable the company to implement its strategy.
- ◆ The continuity and quality of the energy supply in the electricity systems. The achievement of this objective involves the management by the System Operator and is dependent on the reliability and availability of the transmission network.
- ◆ The construction of the electricity transmission infrastructure network necessary to meet future needs. Red Eléctrica, as the sole transmission company, must design, fulfill the formalities for and construct the facilities specified by energy planning. This overall objective must be achieved on a cost-effective basis. The compatibility of the above objectives with social and environmental concerns.

The most significant risks to which the Group is exposed, and which form part of the risk control system, are:

- ◆ **Regulatory**, since the principal business activities of the Group are subject to regulation.
- ◆ **Operational**, basically arising from its assigned activities within the electricity system and the requirement to care for and protect the natural environment.
- ◆ **Market**, since most revenues, as well as certain expenses, may be influenced by variables such as inflation and interest rates.
- ◆ **Business and Credit (or counterparty)**, albeit to a lesser extent due to the lesser weight of the subsidiaries in the overall Group and the existing regulation regarding invoicing and collection for transmission and operation activities.

From an analysis of these risks, different elements of control are defined under the ICFR with a view to properly covering the objectives of transparency and reliability, free of fraudulent information, which must govern the process of preparing the financial information. These elements of control aim to provide sufficient coverage, as far as design and operations are concerned, for the following specific risks associated with the ICFR:

- ◆ **Risk of completeness**: to ensure that no transactions go unrecorded.
- ◆ **Risk of validity**: the transactions carried out are valid.
- ◆ **Risk of recording**: incorrect recording of transactions.
- ◆ **Risk of cut-off**: not all transactions are recorded in the period in which they accrue for accounting purposes.



- ◆ **Risk of valuation:** the transactions are incorrectly valued.
- ◆ **Risk of presentation:** transactions are presented in a way that might lead to confusion, or include insufficient items of information for compliance with applicable reporting requirements.

The Board of Directors is, via the Audit Committee, the body that ultimately has the duty of «*periodically supervising the internal control and risk management systems, so that the principal risks are adequately identified, managed and disclosed*» as stipulated in the Board Regulations.

### 3. Control activities

REE has a wide range of specific **Control activities** that are designed to reduce any risks of error or irregularity that underlie the process of preparing the financial information at every level.

Procedures for reviewing and authorizing financial information and description of the ICFR, to be published on the securities markets, stating the persons responsible, and documents that describe the flows of activities and controls (including those relating to the risk of fraud) for the different types of transactions that may have a material effect on the financial statements, including the procedure for the accounting close and the specific review of significant opinions, estimates, assessments and forecasts.

The Board of Directors delegates to the Audit Committee the functions «*To approve the Company's internal control procedures in the areas of expenditure and investment, making the appropriate amendments, as the case may be*». To supervise the internal audit function, which will ensure the sound functioning of the internal reporting and control systems and must address requests for information from the Audit Committee in the performance of its functions.

**Control activities** are a key element in the setting up of an efficient ICFR, which must undoubtedly be accompanied by a suitable design and operating procedures.

In this regard, the model ICFR sets up a series of critical control targets, the achievement of which, without exception, must allow it to achieve reliability and transparency in the process of drawing up the financial information. Achieving this is intrinsically connected with ensuring that the Control activities so defined are efficient in all their terms, throughout the performance of these activities in every one of the processes.

In this context, the control structure defined specifically in the area of the Control activities of the ICFR determines three scales of controls:

- ◆ Controls or element for assessing the indicators set by the CNMV.
- ◆ General controls.
- ◆ Process controls.

The **Controls or element for assessing the indicators set by the CNMV and the General Controls** represent the basis which underlies the model ICFR. They are transversal controls that directly affect the organizational and processes structure of REE. At 2011 year-end, there were 36 controls or elements for assessing the indicators set by the CNMV operating in the area of the ICFR and 19 general controls in the area of the ICFR. Responsibility for these controls lies with Management, detailed as follows:

- ◆ Directorate-General of Administration and Finance, through the Economic Department.
- ◆ Office of the Secretary of the Board of Directors.
- ◆ Regulation Department (Internal Audit).
- ◆ Human Resources Department.

The significance acquired by the reporting systems in the area of control of the ICFR is reflected by the level of management involved.

The **process controls** have been integrated in each of the main cycles and sub-cycles that make up the processes of the REE ICFR, ensuring that REE's financial information is reliable and transparent, as well as being mitigating factors associated with the risks in the processes for preparing the financial information referred to above. These control activities have been deployed in the ICFR throughout the different areas of the model (cycles and sub-cycles).

On the basis of their characteristic features, these process controls may be classified:

- ◆ According to their nature:
  - **Preventive:** to prevent the materialization of financial risks.
  - **Detective:** to identify errors after they have occurred.
  - **Corrective:** to rectify errors after they have occurred.
  - **Executive (Policy):** controls supported by policies or procedures/instructions of the company; they are usually associated with signature and formal approval requirements.
- ◆ Depending on the level of automation:
  - **Manual:** controls carried out directly by individuals.
  - **Semi-automatic:** controls carried out by individuals and validated by «IT means», or vice versa.
  - **Automatic:** «IT-based» controls.

Major transactions that attempt to ensure reliability and transparency in the process for drawing up the financial information include, in particular:

- ◆ Reviewing the processes for estimates and provisions (at the level of income and expense).
- ◆ Reviewing impairments associated with the assets recorded (essentially referring to assets).
- ◆ Reviewing the bringing of assets into operation and the associated processes for setting values (capitalized items, monitoring administrative approvals, technical conditions for bringing into service, etc.).
- ◆ Reviewing by using specific, compulsory procedures and/or instructions for:
  - Manual recording and/or accounting entries.
  - One-off operations (assessment at the level of senior management of any economic and financial, corporate and legal implications that might arise from such operations).
  - Closing the Financial Statements, drawing up the individual and consolidated Financial Statements.

The internal rules that govern these points are set out in: (i) the «Accounting Policies Manual» (which sets out the accounting policies to be followed at REE when recording accounting entries in the information system, and for drawing up the Financial Statements, for the purpose of ensuring a true and fair view of net worth, financial situation, results of the operations, changes in net equity and cash flows) and (ii) the «Procedures for drawing up and closing the Financial Statements and the individual and consolidated Financial Statements» which states that *«the process for closing the financial statements takes place twice a year (at year-end and half-way through the year when interim half-yearly information is prepared) and which has the purpose of obtaining financial statements that reflect the company's economic situation. In this process all the companies in the group that have to draw up their own financial statements in accordance with the local rules in force in their own countries are affected».*

- Drawing up and publishing the financial information (including aspects relating to the preparation and approval of the Annual Corporate Governance Report, Financial Statements, Annual Report, notifications to the National Securities Exchange Commission, official notifications, etc.). The main internal rules that govern these aspects are set out in: (i) the «Procedure for regular public reporting to regulatory bodies of the securities market», (ii) the «Procedure for drawing up and closing the Financial Statements and individual and consolidated Financial Statements». At this specific level of closure of information and, as applicable, subsequent publication, the Investor Relations Department, the Economic and Financial Department, the General Secretariat, the Board of Directors and Chairman, play an essential role.

Internal control policies and procedures for information systems (inter alia, for secure access, exchange control, system operation, continuity of operations and separation of functions) that support the major processes of the company in connection with the drawing up and publishing of the financial information.

REE's corporate information systems play a major role in the business cycles, sustaining the systems and applications used for preparing financial information.

In this regard, elements such as the General Computer Controls (GCCs) provide a framework for control aimed at providing a reasonable level of security for the information systems that support financial reporting, and guaranteeing, as far as possible, the confidentiality, availability and integrity of the information.

The objectives established in the framework of the General Computer Controls support compliance with the control targets relating to data processing through IT means, by defining, developing, implementing and reviewing control activities regarding strategy and management of information technology (IT), managing change, be it at application or of infrastructure level, controlling security and access parameters for software and hardware, managing users and permissions, dealing with and scaling incidents, continuity of operations, storing and recovering data, monitoring operations, etc.

The rules governing all action taken in connection with the corporate information systems have been set out in the «Information Security Group Policies» and the «Information System Policies», where the principles that are to be used to efficiently manage the security of the data processed by REE's computer systems are stated, together with the assets used in the processes. These policies reflect senior management's commitment to ensuring the security of the data systems, which is also set out in various technical documents that govern the day-to-day operations of the Information Systems Department.

Consequently, the «Information Security Group Policies» and the «Information System Policies» favor the creation of a security framework which aims to establish the responsibilities and the structure of the relationship between the Requesting Units and the Information Systems Department for developing the Corporate Information Systems Management function of REE.

Furthermore, as part of the information systems control objectives, a proper separation of functions has been established, which is an essential requirement for an ICFR of the type used by REE to work efficiently, since it is vitally important to be able to ensure segregation between the person who is performing the acts associated with the processing of the financial information and the person who has to review and/or approve them. For this reason, a correct assignment of roles and profiles, for both technical staff and in positions and functions corresponding to the business areas, are key factors for the success of the process.

Internal control policies and procedures used for supervising the management of activities outsourced to third parties, as well as those aspects of assessments, calculations or valuations that are entrusted to independent experts, which may have a material effect on the financial statements.

REE is particularly concerned about operations carried out by third parties (in order to ensure that, in any key processes that might be outsourced, there is a maximum guarantee of control, regarding the standards required by REE at the level of its processes).

As a fundamental premise, it is general policy not to outsource any activity that is deemed to be significant and which might have a material effect on the financial statements to companies that do not belong to the Red Eléctrica Group.

In all cases, the outsourcing of such activities is set out in a service agreement, which clearly states the service in question and the means to be used by the service provider to provide the service.

#### 4. Information and communication

Reporting and communication tasks carried out throughout the process for drawing up the financial information are of particular significance in Red Eléctrica's ICFR, as they must enable the staff involved in the process of drawing up the financial information to know what action criteria apply, as well as the information systems being used in these processes.

A specific function tasked with defining and updating accounting policies and resolving any queries or disputes arising as a result of their interpretation, maintaining a fluent dialog with the people responsible for operations in the organization, as well as an up-to-date accounting policies manual that is communicated to the units through which the entity operates.

The Economic Department is responsible for defining and resolving any aspect connected with the interpretation of the accounting policies, providing coverage to any area of the Company (any action is taken bearing in mind the references of the «Accounting Policies Manual»). This Department is located within the Directorate-General of Administration and Finance, which in turn reports to the Chairman of the Board of Directors himself.

The accounting policies are established on the basis of the legal framework applicable to the Company, as set out in the Commercial Code and other commercial legislation, and in the International Financial Reporting Standards adopted by the European Union.

REE has an «Accounting Policies Manual». This document, duly disseminated to the employees to whom it applies, is a benchmark for setting the guidelines and activities in the area of accounting records.

The unit responsible for maintaining this manual is the Information and Administration Department, reporting to the Economic Department.

Systems for gathering and preparing the financial information using standard formats, to be applied and used by all the units in the company or the group, which supports the main financial statements and the notes, as well as the information set out on the ICFR.

REE has the following systems:

◆ **Internal:**

- REE has formal processes for closing and preparing the information specifically associated with the financial statements (FS). In both cases, the procedures for closing and drawing up the FS mentioned above contain the guidelines for action and supervision that are developed in obtaining, analyzing and subsequently preparing the information for final approval.
- In addition there is a specific system for the entire process of preparing the Financial Statements, where the Audit Committee, which functionally reports to the Board of Directors, takes on particular significance. It is tasked with ensuring maximum guarantees for the entire process of drawing up the information (both with respect to the supervisory tasks of the Internal Audit function and by the external auditor), as a step prior to the preparation by the Board of Directors.

◆ **External:**

- At this level, REE aims to provide the external agents with true and reliable financial information about its net worth, financial situation and the result of its operations. To do this, the «Internal Code of Conduct on the Securities Market» governs these aspects, both with respect to notifications to supervisory and/or regulatory bodies, and to press releases.

## 5. Supervision and functioning of the system

The supervision and functioning of the system aims to take on a preventive role, in the form of different reviews and analyses and, whenever necessary, solutions to faults in the design and/or way the model works. The rules governing the hierarchical scaling of supervision and/or notifications entrusted to it are adequately set out in the «REE ICFR Manual».

Supervisory activities of the ICFR carried out by the Audit Committee, and if the company has an Internal Audit function that includes among its competencies supporting the Committee in its internal control supervisory work, including the ICFR.

Guaranteeing an up-to-date model that is in line with the reality of the business and with best practices is a critical aspect in order to achieve an efficient ICFR model that ensures that the process for drawing up the financial information is reliable and transparent.

This constant analysis and monitoring of the ICFR, detecting any faults and making the appropriate changes and improvements, is performed via the following actions:

- ◆ The Internal Audit function is a key part of the ICFR. In this connection, it carries out regular checks of the cycles contained in the ICFR in accordance with the planning set out in the Annual Audit Plan.
- ◆ Effective supervision by the Audit Committee, in relation to ultimate control over the ICFR model, delegated by the Board of Directors, and instrumented via the Internal Audit function.
- ◆ Lastly, where proposed actions are finalized and subsequently included, a design and final validation process will be set in motion, so that they may be finally included in the ICFR model.

In all this supervision process, the Internal Audit function plays a key role. Its main objectives are:

- ◆ To ensure and improve compliance with the internal controls established at the Company.
- ◆ To carry out regular checks, on a selective basis, to ensure that documents are kept up-to-date, in accordance with the provisions of the Annual Audit Plan.
- ◆ To check that actions to correct the ICFR have been properly implemented based on the provisions of the Annual Audit Plan.

To ensure that these objectives are achieved, an Annual Internal Audit Plan is established, which is supervised and approved by the Audit Committee.

Discussion procedure whereby the auditor, the internal audit function and other experts may report to senior management and to the Audit Committee or the Board of Directors on major internal control weaknesses that have been identified in the processes for reviewing the financial statements and in any other processes that may have been entrusted to them.

The objectives defined by REE's Audit Committee with respect to the supervision of the functioning of the System include ensuring that the auditor, the Internal Audit function and other experts can report to senior management and to the Board of Directors on the major internal control weaknesses that have been identified in the processes for reviewing the financial statements and in any other processes entrusted to them. In this regard, reports shall be made for each review job carried out when it is completed.

## 6. Other relevant information

REE has submitted its ICFR to a voluntary review since 2008. These reviews have been carried out by Deloitte, S.L.

## 7. External auditor's report

REE has asked DELOITTE, S.L. to review its ICFR. The report on the ICFR appears in REE's Corporate Responsibility Report.