

**REPORT BY THE BOARD OF DIRECTORS OF RED ELÉCTRICA DE ESPAÑA, S.A.  
REQUIRED PURSUANT TO ARTICLE 116 BIS OF SECURITIES MARKET LAW  
24/1988**

**I. SUBJECT-MATTER OF THE REPORT**

Pursuant to Article 116 bis of Securities Market Law 24/1988, introduced by Law 6/2007, each year listed companies must submit to the Shareholders' Meeting a report explaining the additional information which is to be included in the management report.

Accordingly, the Board of Directors of Red Eléctrica de España, S.A. resolved, at its meeting held on March 27, 2008 and upon the preparation of the financial statements for 2007, to offer shareholders this report explaining the matters which, pursuant to Article 116 bis of Securities Market Law 24/1988, were included in the management report of the 2007 financial statements.

**II. CONTENTS OF THE REPORT**

**a) Capital structure, including securities not traded on a Community regulated market, indicating, if appropriate, the various classes of shares and, for each class of shares, the rights and obligations conferred and the percentage of capital stock represented:**

Pursuant to Article 5.1 of the Company's Bylaws, the Company's capital stock 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 a par value de two euros (€2), fully subscribed and paid in and represented by book entries.

All shares relate to the same class and series and confer the same rights on their holders.

**b) Any restriction on the transferability of securities**

The transfer of the shares into which the capital stock of Red Eléctrica de España, S.A. is divided is not subject to any restriction whatsoever. Nonetheless, the legislation governing the electricity industry stipulates certain limits on the holding of shares, on the terms set forth in paragraph d) below.

Like any other listed company, the acquisition of certain significant holdings must be reported to the issuer and to the National Securities Market Commission, pursuant to Article 53 of Securities Market Law 24/1988, to Royal Decree 1362/2007, and to National Securities Market Commission Circular 2/2007, which provide for a first reporting threshold of 3% of the capital or of the voting rights.

**c) Significant holdings in the capital, whether direct or indirect**

As of December 31, 2007 and according to the information available to the Company when this report was prepared, the following are owners of significant holdings in Red Eléctrica de España., S.A.:

Owner	Number of shares	% of capital
State Industrial Holding Company ( <i>Sociedad Estatal de Participaciones Industriales</i> or SEPI)	27,054,000	20

**d) Any restriction on the right to vote**

Each share carries one voting right and any shareholder may attend Shareholders' Meetings without being required to own a minimum number of shares, as was the case until the Extraordinary Shareholders' Meeting held on July 17, 2003, which eliminated the bylaw requirement according to which shareholders had to own at least 50 shares before they were entitled to attend Shareholders' Meetings.

The coming into force of Law 17/2007, amending Electricity Industry Law 54/1997, so as to bring it into line with 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 introduced various amendments to Law 54/1997 which affect the restrictions on the right to vote.

In particular, Section Two of Additional Provision Three of Law 17/2007 stipulates new maximum limits on the exercise of voting and other non-economic rights with a view to guaranteeing the Company's independence, since it pursues regulated activities in the electricity industry which, pursuant to Electricity Industry Law 54/1997, constitute an essential service.

Thus, any individual or legal entity can own a holding in the Company provided that the total of its direct or indirect holding in the Company's capital does not exceed five percent (5%) of the capital stock and that it does not exercise voting and other non-economic rights of more than three percent (3%). These shares cannot be syndicated for any purpose.

Parties pursuing activities in the Electricity Industry and individuals or legal entities which directly or indirectly own holdings in the capital thereof equal to more than five percent (5%) cannot exercise voting and other non-economic rights of more than one percent (1%) at the company in charge of system operation

The special regime for the State Industrial Holding Company (*Sociedad Estatal de Participaciones Industriales* or SEPI) is maintained and has not been amended, and such Company must, in all cases, own a holding of not less than ten percent (10%).

**e) Side agreements**

As of December 31, 2007, the Company has no record of any agreements or covenants between shareholders which oblige them to adopt a common policy or to exercise voting rights on a concerted basis at Shareholders' Meetings or which restrict or condition the unrestricted transferability of the shares.

**f) Rules applicable to the appointment and replacement of members of the managing body and to the amendment of the Company's Bylaws**

## **1. Appointment and replacement**

Article 19 of the Board Regulations provides that Directors shall be designated by the Shareholders' Meeting or by the Board of Directors by co-optation. Proposed appointments of Directors, including by co-optation, must be the subject of a prior report by Appointments, Compensation and Corporate Governance Committee. The Board of Directors, within the scope of its powers, shall ensure that candidates of good standing, competence and experience are appointed, as stipulated in Article 20 of the Regulations.

Pursuant to Article 21 of the Regulations, Directors shall hold office for the period stipulated in the Corporate Bylaws. Proposals submitted by the Board to the Shareholders' Meeting for the appointment or reelection of Directors, as well as their provisional appointment by co-optation, shall be approved by the Board:

- i) at the proposal of the Appointments, Compensation and Corporate Governance Committee, in the case of Independent Directors;
- ii) following a report by the Appointments, Compensation and Corporate Governance Committee in the case of all other Directors.

Article 20 of the Corporate Bylaws provides that Directors shall hold office for four years and may be reelected indefinitely. Pursuant to Article 7 of the Board Regulations, Independent Directors cannot maintain their status as such for an ongoing period of more than twelve years.

Article 22 of the Board Regulations provides that Directors shall leave office at the end of the period for which they were appointed or when so decided by the Shareholders' Meeting, exercising the powers conferred on it by law or in the Bylaws. The Board of Directors must not propose the removal of Independent Directors before the end of the period stipulated in the bylaws for which they were appointed, other than with just cause and following a report by the Appointments, Compensation and Corporate Governance Committee.

Directors must also surrender their post to the Board of Directors and formalize, if the latter considers appropriate, the appropriate resignation in the following cases:

- a) when they reach 70 years of age;
- b) when they are subject to any of the statutory grounds for incompatibility or prohibition;
- c) when they are convicted of an offense or penalized in disciplinary proceedings for a serious or very serious infringement investigated by the supervisory authorities of the securities, energy and telecommunications markets;
- d) when they are in serious breach of their obligations as Directors;
- e) when they leave the executive posts 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 Section 30.4 of these Regulations, and the Board deems this to be the case with the affirmative vote of two thirds of its members. If a Director is processed or is brought to trial for any of the crimes

mentioned in Article 124 of the Spanish Corporations Law, the Board shall examine his case as soon as possible and, in the light of the specific circumstances, shall decide pursuant to the preceding paragraph whether or not it is appropriate for him to remain in office. All of the foregoing shall be set forth in the Annual Corporate Governance Report;

g) in the case of a Nominee Director, when the shareholder whose shareholding interests he represents on the Board disposes of his shareholding in the Company or reduces it below the level which reasonably justified his appointment as such.

Committee members shall leave office when they cease to be Directors. Where a Director leaves office before the end of his term, whether by resignation or on other grounds, he shall explain his reasons in a letter addressed to all Board members, record of which shall be left in the Annual Corporate Governance Report.

## **2. Amendment of Bylaws**

The amendment of the Company's Bylaws does not differ from the corporate law regime stipulated in Article 144 of the Spanish Corporations Law, which requires approval by the Shareholders' Meeting, with the majorities stipulated in Article 103 of the Corporations Law. The powers of the Shareholders' Meeting set forth in Article 3 d) of the Regulations of the Shareholders Meeting include the amendment of the bylaws, which is not subject to majorities other than those stipulated in the Corporations Law.

### **g) Powers of the members of the Board of Directors and, in particular, those relating to the possibility of issuing or repurchasing shares:**

The Shareholders' Meeting of the Company held on May 31, 2007 authorized the Board of Directors so that, pursuant to Article 75 and concordant articles of the Corporations Law, it may carry out directly or indirectly and insofar as deemed necessary given the circumstances, the derivative acquisition of shares in Red Eléctrica de España, S.A., on the following terms. The term of the authorization is 18 months as from the aforesaid date. The maximum number of shares acquired may not exceed the statutory limit, all of the foregoing provided that all other applicable statutory requirements can be met. Acquisitions cannot be made at a price higher than the stock market price at the time of acquisition or for a price lower than 50% of the stock market value at such time. The acquisition may be made as a sale/purchase or swap, or in any other form of transaction for consideration, as deemed necessary given the circumstances. Pursuant to paragraph three of Article 75.1 of the Corporations Law, the Company's Board of Directors may use all or some of the treasury stock acquired, as well as that which is already owned by the Company.

The Ordinary Shareholders' Meeting held on May 26, 2006 also delegated to the Board of Directors, within the maximum statutory period of five years, the power to issue debt documented in non-convertible debentures, bonds of any type, promissory notes, warrants, directly or through subsidiaries, or any other fixed-income securities, in euros or in another currency, capable of being subscribed in cash or in kind, represented by certificates or book entries, simple or with any type of guarantee, including a mortgage guarantee, with or without including warrants, whether or not subordinated, with a fixed or indefinite term, pursuant to the applicable legislation.

Article 25 of the Company's Bylaws provides that the Chairman of the Board is the Chairman of the Company, and is in charge of the senior management as well as of the full representation of the Company in all matters, acting with the delegated powers of the Board. In this connection, the Company's Board of Directors, at its meeting held on July 29, 2004, according to the proposal of the Appointments and Compensation Committee, unanimously resolved: "to delegate to the Chairman of the Board of Directors, under and in accordance with Article 141 of the current Spanish Corporations Law, Article 22 of the Corporate Bylaws and Article 5 of the Regulations of the Board of Directors, all powers of the Board of Directors which by law and pursuant to the Bylaws may be delegated".

In addition to the powers expressly delegated to him, the Chairman is empowered pursuant to the Bylaws to adopt, for reasons or urgency, such measures as he deems appropriate in the Company's interest, reporting them immediately to the Board of Directors and informing the Board regularly, at ordinary meetings, of the corporate management carried out in the various areas of the Company, asking, if necessary, for the relevant approvals of the resolutions submitted. The creation of the Audit Committee and the Appointments, Compensation and Corporate Governance Committee, composed entirely of members of the Board of Directors specialized in the matters under their authority, gave rise to the exercise of specific control over the Company's basic and strategic responsibilities which are in no case discharged exclusively by the Chairman.

Notwithstanding the powers delegated to the Chairman, in practice, it is the Board of Directors, in plenum, that makes decisions which are strategic and significant decisions for the Company.

- h) Significant agreements executed by the Company and which will come into force, be amended or be terminated in the event of a change of control at the Company arising from a public tender, and their effects, except where their disclosure could be seriously detrimental to the Company. This exception shall not apply where the Company is obliged by law to make such information public**

No agreements have been executed by the Company which will come into force, be amended or be terminated in the event of a change of control at the Company arising from a tender offer.

- i) Agreements between the Company and those occupying its administration and management posts or with employees who are to receive severance pay when they resign or are dismissed without justification or whose employment relationship will come to an end in the event of a tender offer**

There are clauses on guarantees or severance pay for cases of dismissal or changes of control in favor of the Executive Director. This contract was approved by the Appointments and Compensation Committee and was reported to the Company's Board of Directors. The clauses are in line with habitual market practice and include grounds for the termination of the employment relationship, contemplating severance pay equal to one year's compensation unless the applicable legislation stipulates a higher amount.

There are also clauses on guarantees or severance pay for cases of dismissal or changes of control in favor of two senior managers. These clauses are in line with

habitual market practice and include grounds for the termination of the employment relationship, contemplating severance pay equal to two years' compensation unless the applicable legislation stipulates a higher amount. The contracts including these clauses were approved by the Appointments and Compensation Committee and were reported to the Company's Board of Directors.