2011

# Annual Report

Terna S.p.A. and the Terna Group

Terna

Terna is a leading grid operator for energy transmission. The Company manages electricity transmission in Italy and guarantees its safety, quality and affordability over time. It ensures equal access conditions for all grid users.
It develops market activities and new business opportunities with the experience and technical expertise acquired in managing complex systems.
It creates value for shareholders with a strong commitment towards professional excellence and with a responsible approach towards the community, fully respecting the environment it operates in.

2011

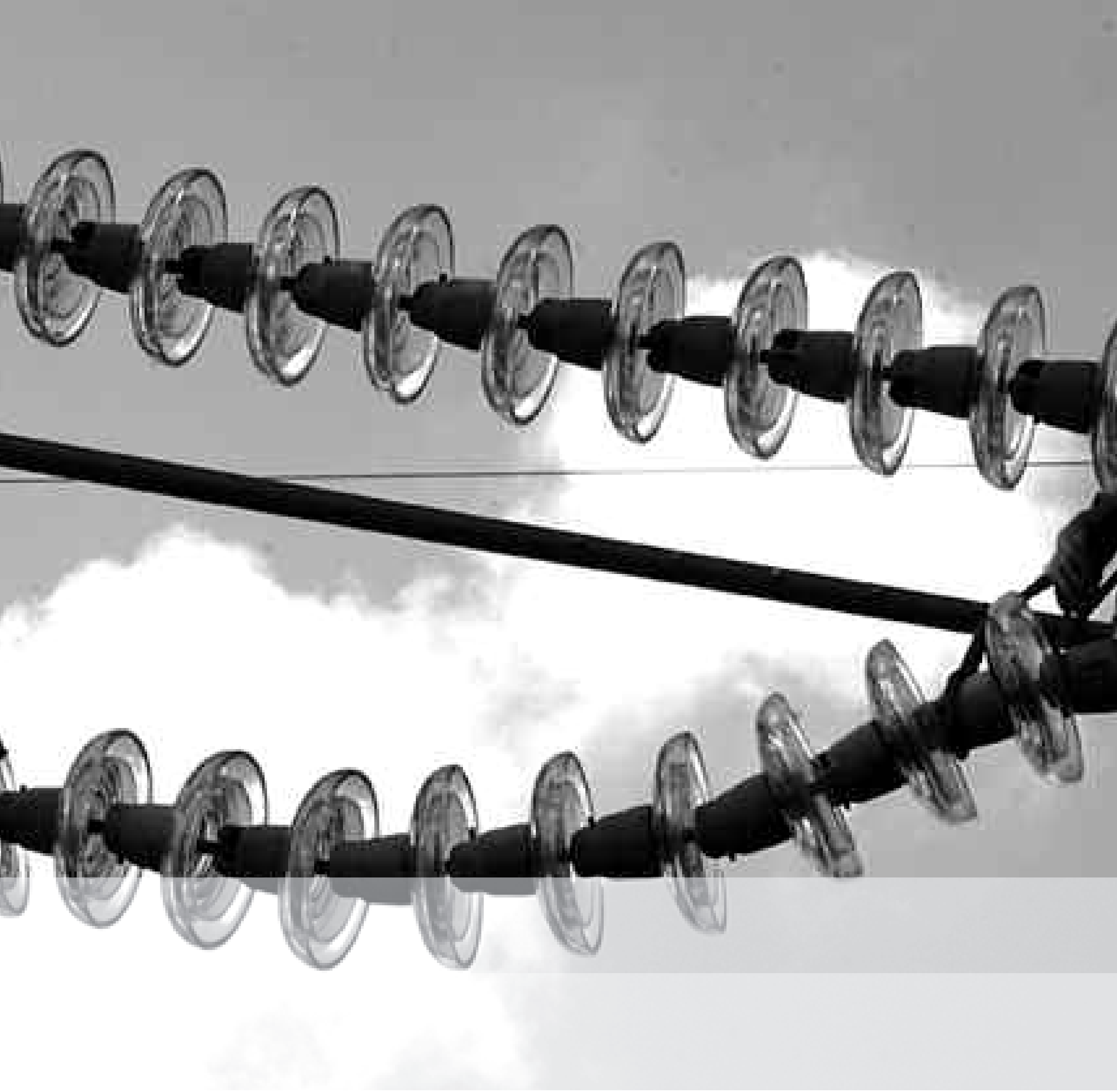
# Annual Report

Terna S.p.A. and the Terna Group

Terna

# transmitting ENERGY

Terna A useful grid for the Country.



# transmitting VALUE

Terna A useful grid for the Country.

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# Chairman's message

**Dear Terna's Shareholders and  Stakeholders,**

the Financial Statement that we are presenting once again underlines our Company's capability in identifying, through the ongoing market changes, opportunities for our growth and that of the country. In 2011, a very difficult year economically, politically and socially, not only for Italy, we nonetheless succeeded in confirming our trend of continuously improving results. First of all, this occurred in terms of investments, representing the most significant indicator of our role as a useful company for the country, that marked a further increase compared to the previous year. Developing transmission infrastructures was carried out – according to a responsible approach adopted years ago and implemented over time – as part of searching for shared solutions with local authorities and with great attention devoted to placing such infrastructures into the landscape and the environment.
The grid has grown significantly and sustainably: the Chignolo-Po-Maleo electricity line, inaugurated in July 2011, represents the most significant example. Its 88 mono-pole pylons, less environmentally impacting without losing their technical functionality, have made this work a primary example of the grid's sustainable development that will allow saving over 25 million euros a year for the electricity system and consequently also for the communities. Work also continued for implementing another strategic project, the Sorgente-Rizziconi electricity line that will connect Sicily and Calabria contributing in a determining way to solving electricity criticalities in the major Italian island.
Searching for solutions that join pylon functionality and aesthetics – one of the most significant aspects of our applied research activities – has led, also following the entrance into operation of the Foster pylons in Tuscany, to a substantial completion of the engineering of pylons designed by the architect Dutton, winner of the international contest that ended last year. Focusing on the environment and on biodiversity was implemented by continuing activities for controlling and reducing the environmental impacts as part of our environmental management system and also with environmental mitigation and restoration measures in three WWF Oases, in collaboration with this organization.
More generally, Terna has increasingly opened up to dialogue with stakeholders. This approach included the agreement with Legambiente for promoting a sustainable energy culture and the presentation of the Development Plan to associations, entrepreneurs, the sector and consumers, that favored the agreement signed in April 2012 with 18 consumer associations for sharing a vision focused on the electricity system's functionality and on consumer protection.
Internally, our knowhow transfer and strengthening objective has been confirmed by the high level of investments for training, in support of the professional excellence that underlies Terna's operational and financial success. The Group's new organizational structure, officially approved in April 2012, supports our strategic objectives, focusing professional contributions towards uniform results and consequently further enhancing the input from human resources.
2011 was therefore another year marked by success, that the Group's strategic objectives will allow attaining also in the next years. Our work, that we have never interrupted, for improving processes and our capability for creating value for shareholders and all stakeholders, is the best basis for confidently looking ahead to future challenges.

The Chairman
LUIGI ROTH

# Letter to Shareholders

**Dear Shareholders,**

2011 was the seventh consecutive year that registered positive results. We did very well, confirming **a 21 eurocent dividend in line with the previous year, despite the impact of the Robin Hood Tax and the difficult national and international situation**. Our Group, that since 2005 to the present has climbed 4 positions in the ranking of the leading global TSOs for km of electricity lines managed, reaching the absolute sixth place ahead of the American AEP, can rely on an unparalleled solidity.

We have demonstrated quickness in adapting and today our strategic pillars, solidity and capability for creating value, are stronger than ever. A value that we have also proudly given the country, **with 4 billion euros saved for the electricity system from 2005 to the present and a focus on sustainability that represents globally recognized excellence.**

Revenues, Ebitda, Profits and Investments increased thanks to a preventive strategy on non-traditional and non-regulated business, on innovation and technology.

As of December 31, 2011, the Terna Group invested 1,229 million euros increasing by 67 million euros compared to 2010. Of particular importance, the projects for the Sorgente-Rizziconi connection (118 million euros) and the Chignolo-Po-Maleo line (69 million euros), the Italy-France connection (55 million euros) and the Montercorvino-Benevento power line (25 million euros).

At the consolidated level and comparing data with the results achieved in 2010, revenues increased by 2.9% standing at 1 billion and 636 million euros, the Gross Operating Margin stood at 1,230 million euros increasing by over 4.7%. The negative impact of the Robin Hood Tax (153.8 million euros, equal to approximately 40% of 2011 taxes) was offset by the proceeds from Non Traditional Activities registering Group Net Profits at 440 million euros, while the adjusted Net Profits for continuing activities of extraordinary items reached 465 million euros, increasing by 1.1%.

These results allow proposing the distribution of a total **dividend** equal to 21 eurocents, thanks to the proceeds from Non Traditional Activities, in line with the previous year.

The company's objectives continue to be focused on technology and innovation for grid safety. 2012 will aim at implementing the projects included in the 2012-2016 Strategic Plan: in the next 5 years 4.1 billion euros will be invested for the safety and modernization of the electricity Grid, developing over 300 building sites across Italy, when full operating.

The amount of the capex will be practically doubled for **Non Traditional Activities** (up to 1.9 billion euros) compared to 1 billion euros included in the previous Plan. By enhancing the company's strong technical and engineering expertise, in addition to 1 billion euros for building battery storage systems, up to 900 millions could be included for Non Traditional Activities both in Italy and abroad in projects for private customers where the expected returns are higher than those for regulated activities.

As already announced to the market, we are confirming our dividend policy in line with the above-mentioned strategy for creating value that will continue to be satisfactory for shareholders: as of 2012, the base dividend from Traditional Activities will be equal to 19 eurocents per share, to which the contribution from Non Traditional Activities will be added (60% pay out on results and/or gains).

We are now aiming at a different mix for our investments and as of April 1, 2012 the Terna Group's new organizational structure became operational, developed for strategically assessing business opportunities deriving from the Industrial Plan and for maximizing efficiency in managing our activities.

**The new corporate structure** intends to reflect our willingness in supporting this strategic development as best as possible through our unique technical expertise in the field.

Terna Rete Italia, that includes most of our people, is responsible for all activities regarding the national electricity grid included in the concession: operation, maintenance and development of the national electricity transmission grid. The company will also have the task of implementing the projects the Parent Company established in the Development Plan.

Terna Plus will be responsible for developing non traditional and non regulated activities: particularly, for implementing battery storage and energy efficiency systems and for developing engineering solutions for third parties. Terna Plus will also be responsible for finding development opportunities abroad.

Lastly, the Parent Company Terna Spa, will have Management and Coordination power and duties for developing the Group's activities, particularly referred to defining strategic guidelines for the financial policy, to governing accounting and tax processes as well as planning and controlling the Group's operational management; moreover, it will oversee risk management activities, as well as management of institutional relations, including relations with the public authorities and activities regarding legal issues and fulfilling the Group's obligations, managing the entire corporate organization.

**Our values and our identity are always the same and represent our greatest strength. The new organization and the Industrial Plan represent not only a challenge, but also the natural development of our consolidated history that now looks ahead to new objectives to be reached together.**

2012 started off well and the commitment undertaken by all the Terna team leads me to believing that growth will once again be achieved.

The CEO

FLAVIO CATTANEO

# Notice of Call
# Call of ordinary and extraordinary Shareholders' Meeting

The ordinary Shareholders' Meeting of Terna S.p.A. has been convened in Rome, at TERNA's Auditorium in Piazza Giuseppe Frua no.2, for its ordinary session on May 15 and 16, 2012, respectively on first call at 11.00 am and on second call at 3.00 pm and, for its extraordinary session, on May 15, 16 and 17, 2012, respectively on first call at 11.00am, on second call at 3.00 pm and on third call at 11.00am to discuss and resolve on the following

## Agenda

### Ordinary Session

1. Financial Statement as of December 31, 2011. Reports by the Board of Directors, the Board of Statutory Auditors and the Independent Auditors. Related resolutions. Presentation of the Consolidated Financial Statement as of December 31, 2011;
2. Allocation of the net income of the fiscal year;
3. Appointment of a member of the Board of Directors;
4. Annual Report on Remuneration: consultation on the Remuneration Policy pursuant to article 123 *ter*, paragraph 6 of Legislative Decree no. 58/98 (Consolidated Law on Finance).

### Extraordinary Session

1. Amendments to Art.14.3, 14.5, 26.1 and 26.2 of the Corporate Bylaws, in compliance with the provisions introduced by Law no. 120 dated July 12, 2011 regarding gender balance in administration and control bodies of listed companies, with articles 147 *ter*, paragraph 1 *ter* and 148, paragraph 1 *bis* of Legislative Decree no. 58/98 (Consolidated Law on Finance) and introducing the new article 31 "Transitional Clause" as an effect of said provisions.

### Reports and documentation

The illustrative reports by the Directors on the items on the agenda, required by governing rules, will be made available to the public at the company headoffice and at Borsa Italiana S.p.A. according to the following timetable:
- by April 5, 2012, the report concerning item 3 of the agenda for the ordinary Shareholders' Meeting;
- by April 15, 2012, the reports concerning items 1 and 2 of the agenda for the ordinary Shareholders' Meeting;
- by April 24, 2012, the reports concerning item 4 of the agenda for the ordinary Shareholders' Meeting and the only item on the agenda for the extraordinary Shareholders' Meeting.

Documents submitted to the Shareholders' Meeting will be made available to the public at the company headoffice and at Borsa Italiana S.p.A. in the terms provided for by rules in force.
The reports and documentation will also be published in the Company's website (www.terna.it - "Investor Relations"). Shareholders have the right to obtain copies.

### Right to supplement the agenda

Shareholders who, also as a group, represent at least one fortieth of the share capital with voting rights, may ask, pursuant to and in the modes pursuant to Article126 *bis* of Legislative Decree no. 58 of February 24, 1998 (TUF), within ten days from the publication of this notice, to add subjects to be discussed, indicating the proposed subjects in the request.
The request must be submitted in writing and must be accompanied by a report on the matters being proposed, and be brought to TERNA S.p.A. at its head office (attention: TERNA S.p.A. Corporate Secretary), or sent by mail or fax to 06-83138218, or by e-mail or certified electronic mail at the following certified e-mail address: Assemblea2012@pec.terna.it.

Please remember that pursuant to law, supplements to the agenda are not allowed for subjects which the Shareholders' Meeting will be resolving upon according to the law and based on Directors' proposals or on the basis of a project or a report prepared by them that is different from the one dealing with the subjects in the agenda. In the event of supplements to the agenda, the modified list of subjects to be dealt with in the Shareholders' Meeting will be published, with the same modes of publication as this notice, at least fifteen days before the one scheduled for the Shareholders' Meeting.

### Share capital

Please note that as of the date of this notice, and pursuant to Article 5.1 of the Bylaws published in the website of the Company (www.terna.it - "Investor Relations") (the "Bylaws"), the share capital is of 442,198,240 euros, completely paid-in and divided into 2,009,992,000 ordinary shares having a value of 0.22 euros each, each of which, pursuant to Article 6.1 of the Bylaws, entitles to one vote. The Company does not hold any own shares.

### The right to participate in the Shareholders' Meeting and exercising the right to vote

The right to participate in the Shareholders' Meeting and exercise the right to vote, according to the provisions in Article 10.1 of the Bylaws, is governed by applicable regulatory standards in force. Pursuant to governing Article 83sexies of the TUF, such right is demonstrated by notification to the Company by an intermediary, in compliance with its own accounting records, on behalf of the individual who is entitled to the right to vote, based on evidence related to the close of the accounting day of the seventh open-market day prior to the date set for the Shareholders' Meeting in first call (i.e., May 4, 2012), the so-called "record date".

The credit and debit registrations made on accounts subsequent to said term are not material for purposes of legitimizing the exercise of the right to vote in the Shareholders' Meeting. Therefore, those who appear as owners of the Company shares subsequent to said date will not be allowed to participate and vote.

Communications by intermediaries for participation must be received by the Company by the end of the third open-market day prior to the date set for the first call of the Shareholders' Meeting (i.e., May 10, 2012). There is no prejudice to the entitlement to participate and vote if the Company has received the communications after said indicated term, provided that they are received by the time the Meeting begins on single call.

There are no procedures for voting by mail or by electronic means.

### Representation at the Shareholders' Meeting

#### Ordinary proxy

Each party entitled to participate and vote at the Shareholders' Meeting may be represented by means of a proxy pursuant to governing law provisions. For this purpose, the proxy form issued upon request of the entitled party by the qualified intermediary can be used, or the proxy form available on the Company's website (www.terna.it - "Investor Relations") or at the headoffice.

The Company can be notified of the proxy by filing it with the headoffice (the Corporate Secretary of TERNA S.p.A.) or by mail, or e-mail or certified electronic mail to the following certified e-mail address: Assemblea2012@pec.terna.it, or using the section of the Company website (www.terna.it - "Investor Relations") and the proxy must be received by the Company by the time the Meeting begins on single call. In replacement of the original, the representative may deliver or transmit to the Company a copy of the proxy, also by electronic means, stating under his/her own responsibility that the proxy is in compliance with the original, as well as to the identity of the person issuing the proxy.

#### Designated Representative Proxy

The proxy may also be granted with voting instructions to Servizio Titoli S.p.A., with headoffice in Via Lorenzo Mascheroni no. 19, Milan, 20145, appointed by the Company for this purpose as "Designated Representative" pursuant to Article 135undecies of the TUF. In this regard, the specific guided web application prepared and managed by Servizio Titoli S.p.A., which can be accessed on the Company's website (www.terna.it - "Investor Relations"), can be used to fill in the proxy form for the designated representative. The Designated Representative proxy form is also available in a printable version from the website, or from the Company's headoffice. The Designated Representative proxy must contain voting instructions to all or some of the subjects on the agenda and the original must be given to said Designated Representative by the end of the second open-market day prior to the date set for the Shareholders' Meeting on first call (i.e., by May 11, 2012) at the following address: Servizio Titoli S.p.A. (ref. "Terna S.p.A. Shareholders' Meeting proxy."), Via Monte Giberto no. 29, 00138 Rome. A copy of the proxy, accompanied by a declaration stating that it is in compliance with the original, can be anticipated to the Designated Representative by the same term by fax at: 06 45417450 or at the certified e-mail address terna@pecserviziotitoli.it.

A "Designated Representative" proxy is valid only for resolutions proposed at the Shareholders' Meeting for which the person issuing the proxy gave voting instructions. The proxy and the voting instructions are revocable within the same term as hereinabove (i.e., by May 11, 2012), with the manner and terms indicated above.

### Right to pose questions on items on the agenda

Pursuant to Article 127 *ter* of the TUF, parties entitled to participate in the Shareholders' Meeting may pose questions on subjects on the agenda also before the Shareholders' Meeting. The questions must be made in writing and sent to TERNA S.p.A. to its headoffice (to the attention of the Corporate Secretary of TERNA S.p.A.) by fax at the number 06 83138218, or by e-mail or certified electronic mail at the certified e-mail address: Assemblea2012@pec.terna.it.

### Appointment of a member of the Board of Directors

For appointing a member of the Board of Directors, the modalities established by art. 14.5 of the Bylaws shall apply as well as the regulations in force. For the appointment of a member of the Board of Directors, please remember in particular, that statutory provisions apply regarding i) limitations to exercising the voting right when appointing Directors pursuant to art. 14.3, lett. e) and, (ii) the requirements of respectability, professional skills and independence of Directors, pursuant to art. 15.

## Annual Report on Remuneration

Regarding the fourth item on the agenda for the ordinary session, please remember that the Meeting, pursuant to and in compliance with art. 123 *ter*, paragraph 6, TUF, is called to resolve in favor or against the first section of "Terna's Annual Report on Remuneration"; this report details the Remuneration Policy adopted by TERNA S.p.A. concerning the remuneration of the members of administration bodies, of general directors and of managers holding strategic responsibilities, as well as the procedures used for adopting and implementing such Policy. As established by the abovementioned provisions, the resolution is not binding.

## Other Information

Further information concerning the subjects on the agenda is made available to the shareholders in the Directors' report concerning the respective items on the agenda, as well as in the Bylaws and in governing legislation, which shall be specifically referred to for what is not expressly provided for in this notice.

For the purposes of exercising the company rights mentioned in this notice, please remember that pursuant to Articles 22 and 23, paragraph 1, of the Regulation adopted by the Bank of Italy and by Consob with the provision of February 22, 2008 and subsequently amended by deed of the Bank of Italy/Consob dated December 24, 2010 (hereinafter referred to as the "Bank of Italy/Consob Regulation"), the legitimacy of exercising, also jointly, corporate rights such as: participation in and exercising the right to vote in the Shareholders' Meetings, the right to supplement the agenda, the right to pose questions on subjects on the agenda, is certified by a communication to the issuer made by the intermediary in compliance with his accounting records for holders.
Pursuant to Article 25 of the Bank of Italy/Consob Regulation, legitimization to rights different from those provided for in Articles 22 and 23 is assessed by certification issued by the intermediary in compliance with his own accounting records.

In order to facilitate the verification of their entitlement to participate in the Shareholders' Meeting, the holders of the right to vote may send documentation demonstrating said entitlement to the Company by mail (to the Corporate Secretary of TERNA S.p.A. - Viale Egidio Galbani, 70 - 00156 Rome), also a copy of it or by fax to 06/83138218, at least two days prior to the scheduled date for the Shareholders' Meeting on first call.
Please note that the offices in charge of personal identification and verification of entitlement to participate in the Shareholders' Meeting will be available on the day of the Shareholders' Meeting, two hours before the Meeting begins.
A service dedicated to Meeting assistance is available to give further information at the following numbers: telephone 06 45417413 - fax 06 45417450.
This notice has been published in the company website at www.terna.it and in the April 5, 2012 edition of the newspaper "Il Sole 24 Ore".

Chairman of the Board of Directors
**Luigi Roth**

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Considering the shareholding of the Company and how previous occasions unfolded, it is estimated that the ordinary and extraordinary Shareholders' Meeting will be able to be convened and resolve on May 16, 2012.

Terna S.p.A. - Headoffice in Rome - Viale Egidio Galbani, no. 70
Share Capital 440,967,054 euros (as of 31 December 2010) fully paid-in
Company Register of Rome, Tax ID code and VAT code no. 05779661007
R.E.A. of Rome no. 922416

# Summary of the resolutions of the ordinary and extraordinary Shareholders' Meeting

Terna S.p.A.'s Shareholders' Meeting met on second call on May 16, 2012 for the ordinary and extraordinary session at Terna's Auditorium in Piazza Giuseppe Frua No. 2 in Rome and in the ordinary session it:

- approved Terna S.p.A.'s Financial Statement as of December 31, 2011;
- examined the data of the Terna Group's consolidated financial statements also as of December 31, 2011 that closed with the Group's net profits equal to 440 million euros;
- resolved to allocate Terna S.p.A.'s 2011 net profits, equal to 453,587,553.23 euros as follows:
  - 246,237.20 euros to Legal Reserves (or up to reaching 20% of the share capital as of the financial statement's reference date);
  - 160,799,360.00 euros to cover the interim dividend paid on November 24, 2011;
  - 261,298,960.00 euros as a final dividend to be distributed in the amount of 0.13 euros for each one of the 2,009,992,000 ordinary shares (as of March 20, 2012) to be paid – gross of any withholdings according to the law – on June 21, 2012 with "registration date" of coupon No. 16 on June 18, 2012;
  - 31,242,996.03 euros as Balance Brought Forward.

In its ordinary session, the Meeting also:

- appointed as a Company Director Mr. Francesco Pensato [(1)], previously co-opted by the Board of Directors in its meeting on July 29, 2011, whose term of office will expire, together with that of the other directors, upon the approval of the 2013 financial statement;
- approved, pursuant to and in compliance with Article 123 *ter*, paragraph 6 of Legislative Decree No. 58 dated February 24, 1998 (Consolidated Law on Finance) – the first section of "Terna's Annual Report on Remuneration" that – with reference to the members of administration bodies, to general directors and to other executives with strategic responsibilities – illustrates the Remuneration Policy adopted by Terna S.p.A. as well as the procedures used for adopting and implementing such Policy.

In its extraordinary session, the Meeting approved changes to articles 14.3, 14.5, 26.1 and 26.2 of the Company By-laws and the introduction of new Article 31 ("Transitional Clause") with new numbers 31.1 and 31.2 for the paragraphs forming this Article, aiming at ensuring, for three consecutive terms and without prejudice to any additional extensions as provided for by the law, gender balance in the composition of the Board of Directors and of the Board of Statutory Auditors of companies with listed shares, implementing the provisions introduced by Law No. 120 dated July 12, 2011, by Articles 147 *ter*, paragraph 1 *ter*, and 148, paragraph 1 *bis* of the Consolidated Law on Finance.

The main changes concern:

- the methods used for coordinating observance of gender quotas with the slate vote procedure, with the sole exception for lists containing less than three candidates;
- the mechanisms used to ensure observance of gender quotas should there be substitutions during the course of a mandate and
- methods to ensure that exercising the right of appointment, when provided for, does not contrast with the regulatory provisions of the Consolidated Law on Finance on the matter.

(1) In possession of the independence requirements as provided for by the law and by Terna S.p.A.'s Bylaws, and by the Governance Code which Terna adopted.

# Corporate bodies

## Board of Directors

**Chairman**
Luigi Roth

**CEO**
Flavio Cattaneo

**Directors**
Fabio Buscarini
Paolo Dal Pino
Matteo Del Fante
Salvatore Machì
Romano Minozzi
Francesco Pensato
Michele Polo

**Board Secretary**
Ernesto Calaprice

## Board of Auditors

**Chairman**
Luca Aurelio Guarna

**Statutory auditors**
Alberto Luigi Gusmeroli
Lorenzo Pozza

**Alternate auditors**
Stefania Bettoni
Flavio Pizzini

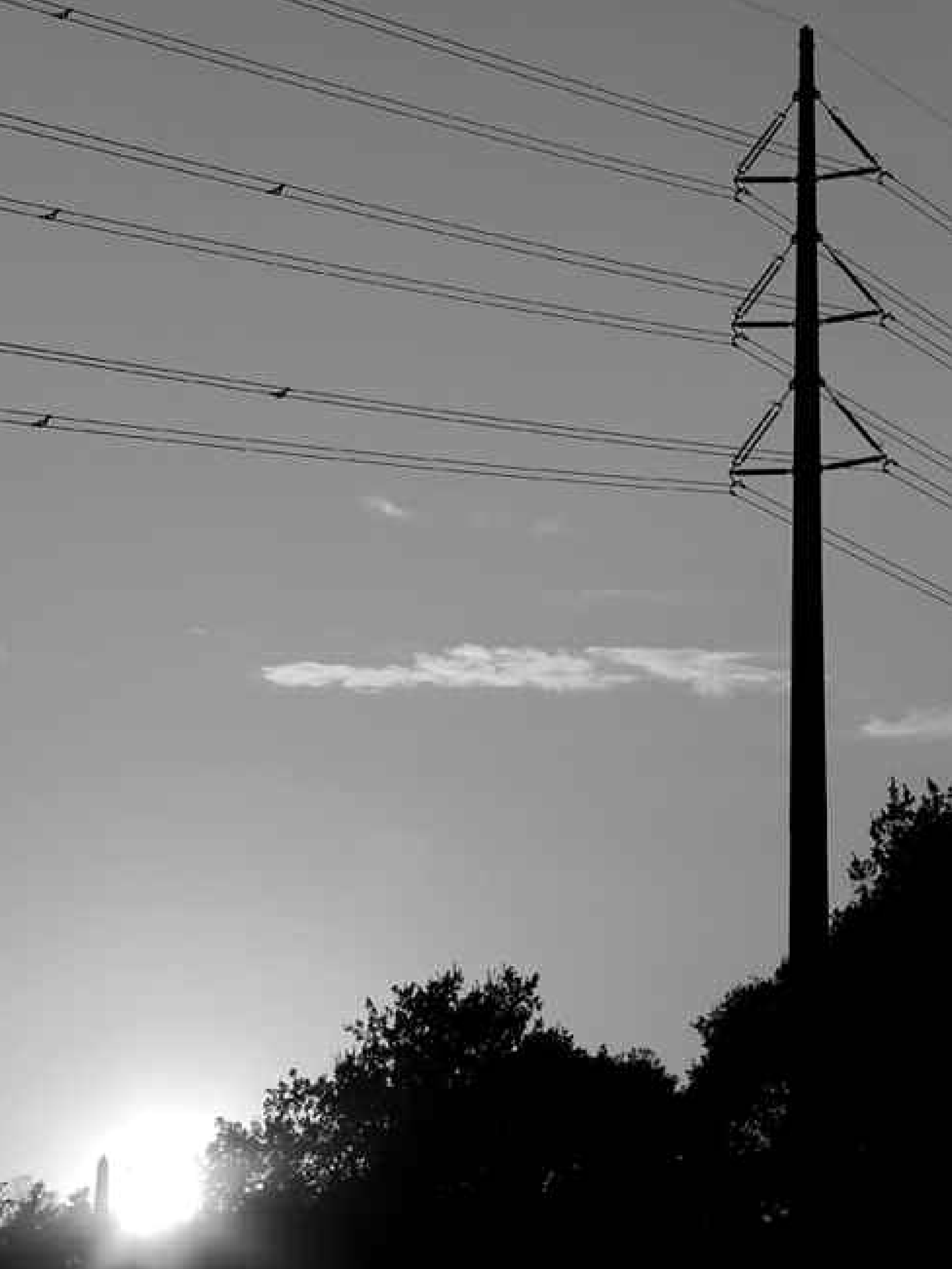
**Auditing Company**
PricewaterhouseCoopers S.p.A.

## Powers

**Board of Directors**
The Board is vested by the articles of association with the broadest powers for the ordinary and extraordinary management of the Company, and specifically has the power to carry out all the actions it deems advisable to implement and attain the corporate purpose, with the sole exception of those actions that are reserved to the shareholders by law and the articles of association.

**Chairman of the Board of Directors**
The Chairman is vested by the articles of association with the powers to represent the Company legally and to sign on its behalf, presides over shareholders' meetings, convenes and presides over the Board of Directors, and ascertains that the Board's resolutions are carried out.

**CEO**
The Chief Executive Officer is also vested by the articles of association with the powers to represent the Company legally and to sign on its behalf, and in addition is vested by a Board resolution with all powers for managing the Company, with the exception of those that are otherwise assigned by law or the articles of association or reserved for the Board of Directors.



# Terna’s management

**Flavio Cattaneo**
Chief Executive Officer

**Giuseppe Saponaro**
Finance, Control and M&A Director

**Luigi de Francisci**
Regulatory Affairs Director

**Giuseppe Lasco**
Company Security Director

**Stefano Conti**
Institutional Affairs Director

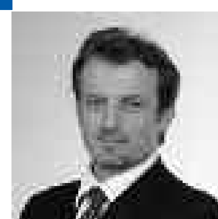
**Giovanni Buttitta**
External Relations and Communication Director

**Elisabetta Colacchia**
Investor Relations Manager

**Cesare Ranieri**
Human Resources and Organisation Director

**Gianni Armani**
Interim Italian Operations and Facility Maintenance Director

**Luigi Roth**
Chairman



**Alessandro Fiocco**
Procurement Director

**Fulvio De Luca**
Internal Audit Manager

**Francesco Del Pizzo**
Non Traditional Activities and International Department Director

**Pier Francesco Zanuzzi**
Dispatching and Energy Operation Director

**Filomena Passeggio**
Corporate Secretary and Legal Department Director

**Carlo Sabelli**
Real Time Manager

**Luciano Di Bacco**
Administration Director and Officer in charge

**Evaristo Di Bartolomeo**
Grid Development and Engineering Director


Terna

2011

# Directors' Report

Terna

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## Directors' Report


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# Introduction

## Terna and the financial markets

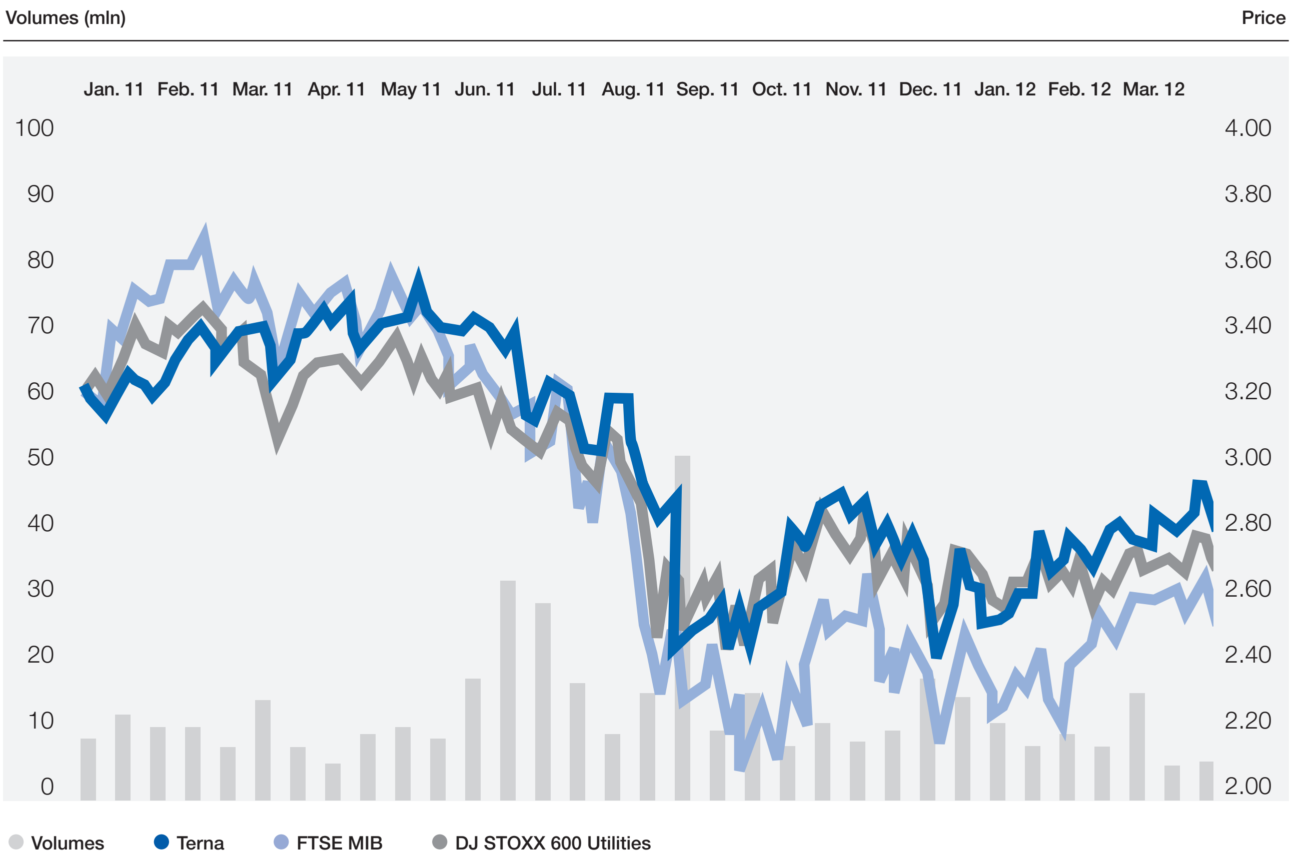
| FINANCIAL INDICATORS | | 30 December 2011 |
|---|---|---|
| **Weight of Terna shares** [(1)] | | |
| > in the FTSE MIB index (%) | | **1.93%** |
| > in the FTSE Italy All Share index | | **1.79%** |
| **Ratings** | | |
| Standard & Poor's | Outlook | **Negative** |
| | M/L term | **A-** |
| | Short-term | **A-2** |
| Moody's | *Outlook* | **Negative** |
| | M/L term | **A2** |
| | Short-term | **Prime-2** |
| Fitch | *Outlook* | **Negative** |
| | M/L term [(2)] | **A** |
| | Short-term | **F1** |

(1) Source: Bloomberg. Figures at 30 December 2011.
(2) Issuer Default Rating.

### Performance of Terna stock

In 2011, European price lists recorded very negative trends due to the worsening of the outlook, marked by a weak economic recovery and high unemployment rates. The continuation of the sovereign debt crisis has made new economy stimulation plans necessary by governments and has also contributed towards creating further uncertainty amongst investors and increasing volatility in trade.
In this situation and despite the negative impact of the extension of the "Robin Hood Tax" to the electricity transmission sector, the defensive nature of the Terna stock has allowed it to record a better performance than that of Italian Blue Chips (Terna -17.6% vs. FTSE-MIB -25.2%).
The stock traded on a dialy average volume of 10 million, down from the previous year.
In terms of Total Shareholder Return (or TSR, namely the return inclusive of both the share performance and the dividends paid during the period), Terna has overperformed the segment and the Italian Blue Chips index (Terna -11.4%, DJ Stoxx Utilities -11.6%, FTSE-MIB -22%).
During the first few months of 2012, Terna recorded a rise of 8.9%, in line with the market (FTSE-MIB +9.2%) and better than the sector generally (DJ Stoxx Utilities +2.2%).
Since listing (23 June 2004) up to end of 2011, the Terna stock has risen by 53.2% against a negative performance of the FTSE MIB of 45.9%. The TSR over this period was actually 140.6%, in marked contrast with the average loss of 27.4% generated by the Italian Blue Chips.

PERFORMANCE OF TERNA SHARES AND THE FTSE MIB AND DJ STOXX 600 UTILITIES INDEXES




Source: Bloomberg. Data at 9 March 2012.

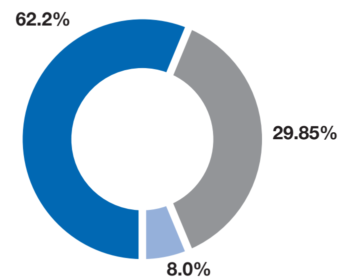
## Ownership

At the date on which these financial statements are prepared, the share capital of Terna S.p.A. amounts to €442,198,240, represented by 2,009,992,000 ordinary shares, with a par value €0.22 each.
Based on the register of shareholders and other information available at the date of preparation of this report, the ownership of Terna S.p.A. is analysed as follows:

- Cassa Depositi e Prestiti S.p.A. (CdP) 29.85%;
- Other Major Shareholders (1) 8% of which:
  - Romano Minozzi 5.6%;
  - BlackRock Inc. 2.4%;
- Other Institutional and Retail Investors 62.2%.

### TERNA'S SHAREHOLDING STRUCTURE BY TYPE

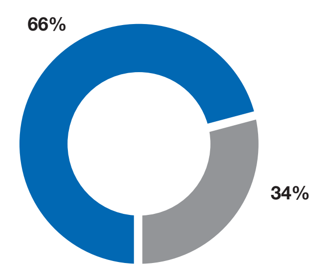
| | |
|---|---|
| Other Institutional Investors + Retail | 62.2% |
| CdP | 29.85% |
| Other Major Shareholders (1) | 8.0% |
| **Total 100%** | |




Based on periodic surveys carried out by the Company, it is believed that 66% of the shares of Terna S.p.A. are held by Italian investors (CdP 29.85%, Retail Investors 27.8% and Institutional Investors 7.9%), with the remaining 34% being held by Foreign Institutional Investors, primarily within Europe and America.

### TERNA'S SHAREHOLDING STRUCTURE BY GEOGRAPHIC AREA

| | |
|---|---|
| **Italian Investors** | |
| of which CdP | 29.85% |
| of which Retail | 27.8% |
| of which Institutional Investors | 7.9% |
| **Foreign Institutional Investors** | |
| of which UK | 6.7% |
| of which USA/CANADA | 4.8% |
| of which Europe (excl. UK) | 11.5% |
| of which Others | 11.4% |
| **Total 100%** | |




(1) The term "Major Shareholders" is used to refer to shareholders holding an interest of more than 2% in the share capital of Terna S.p.A., on the basis of the information available and communications received in accordance with CONSOB Resolution no. 11971/99.

## The Terna Business Model

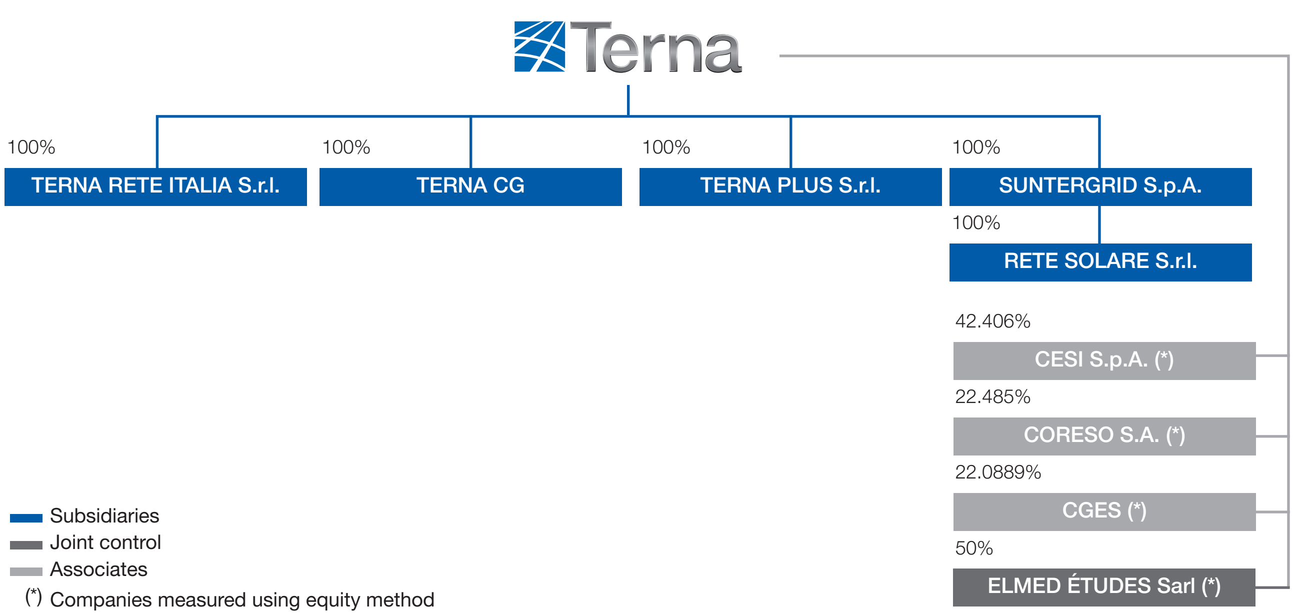
Terna is Europe's most important independent grid operator for the transmission of electricity (Transmission System Operator - TSO) and is sixth worldwide in terms of kilometres of lines managed.
The Terna Group owns the Italian National Transmission Grid (NTG) with more than 57,600 kilometres of high voltage lines (more than 63,600 km three-phase power lines), 454 transformation stations and 22 interconnection lines with foreign countries (at 31 December 2011).
In Italy, Terna acts as TSO under a government concession. It is responsible for transmitting and dispatching electricity along the high-voltage and very-high-voltage grid throughout the whole of national territory. Terna is also responsible for planning, constructing and maintaining the grid.

Terna's mission is:
- to manage electricity transmission in Italy, guaranteeing its security, quality and affordability over time;
- to ensure equal conditions of access to all grid users;
- to develop market activities and new business opportunities with the experience and technical skills gained in the management of complex systems;
- to create value for the shareholders with a strong commitment to professional best practices and with a responsible approach to the community, respecting the environment in which it operates.

The current scope of Terna's activities is the result of a process of the liberalisation of the electricity sector that began in 1999, the year in which the system operator functions were assigned to GRTN - Gestore della Rete di Trasmissione Nazionale, a company under public control. In November 2005, Terna, already the owner of almost all the National Transmission Grid, acquired from the latter the functions of grid operator, with the related human resources and assets, as established by Prime Ministerial Decree of 11 May 2004. The unification of the ownership of the grid (apart from small residual portions) and its management have coincided with Terna's independence from the Enel Group to which it previously belonged. Terna today faces the market with complete independence of strategy and management, on the strength of the technical skills it has acquired in the past: it is therefore both innovation and tradition at the same time, two values that often accompany its development prospects.

### The Terna Group

The Group structure at 31 December 2011:



**Core business:** the Terna Group transmits and dispatches electricity on the National Transmission Grid; the Group companies:
- Terna S.p.A. (Concession holder);
- Terna Rete Italia S.r.l. (2) (formerly TELAT);
- Terna Crna Gora d.o.o..

**Non-core business:** the Terna Group develops new activities and business opportunities with the experience and technical skills acquired; the Group companies:
- Terna Plus S.r.l.;
- SunTergid S.p.A. and Rete Solare S.r.l..

## Associates

CESI leads the market of the testing and certification of electromechanical equipment and advisory services on electrical systems; it covers all stages of the life cycle of the electrical system and offers electrical system companies (generation, transmission and distribution), manufacturers of electrical and electronic equipment, major electricity users and local and national public administrations, a full range of services seeking to solve problems connected with the production processes of the whole electrical energy sector.

CORESO is a Belgian service company with its headquarters in Brussels; Terna joined the ownership structure in November 2010 with an equity interest of 22.485%. The ownership structure of the company includes the operators of France (RTE), Belgium (Elia) and Great Britain (National Grid), each holding an equal share to that of Terna, and the German operator, 50Hertz Transmission, with 10%. CORESO prepares daily forecasts and analyses in real time of energy flows in Central-Western Europe, identifying possible critical issues and duly informing the TSOs concerned in a timely manner.

CrnoGorski Elektroprenosni Sistem AD ("CGES") is the Montenegro TSO of which Terna became a shareholder with 22.09% of the capital following the approval by the shareholders' meeting of CGES of the capital increase reserved to Terna. The agreement represents the end point of a process of industrial and country cooperation and is part of the intergovernmental agreements between Italy and Montenegro which were initiated on 19 December 2007 and sanctioned by the signing of a strategic partnership agreement in November 2010, for the construction of a new submarine electrical interconnection and the implementation of partnerships with national transmission operators.

## Joint ventures

ELMED ÉTUDES is a special purpose entity, held equally by Terna and by the Tunisian electrical company STEG, which is developing Elmed, an integrated electricity production project in Tunisia, from conventional and renewable sources, and transport towards Italy through an underwater interconnection. Production rights will be assigned by means of an international competition.

(2) Renamed by resolution of the ordinary shareholders' meeting of the subsidiary held on 21 December 2011.

## The Business Plan

On **20 March 2012**, Terna approved the Terna Group Business Plan for the period 2012-2016; guidelines are set out below:

- **core business:** over the next 5 years, €4.1 billion will be invested in the safety and modernisation of the electricity grid, of which 82% will be for the National Transmission Grid development with investments focused on maximizing the use of system capacity and reducing congestion, fostering the development of generation capacity from renewable sources;
- **non-core business:** up to approximately €1 billion will be used for the development of battery accumulation systems for 240 MW, at present awaiting authorisation and in any case as long as suitable remuneration is obtained. Additionally, both in Italy and abroad, investments of up to 900 million are planned in projects for private customers, with a forecast return that exceeds that of regulated business. In thus doing, the objective expenditure in non-core business is doubled (up to €1.9 billion), with respect to the previous plan;
- **improved margins (EBITDA margin):** it is expected that the increased revenue and the control of costs will allow to achieve an accumulated EBITDA over period 2012-16, up approximately 19% with respect to the previous five-year plan. Average annual growth in EBITDA goes from 5% to 7.5%, showing a consistent improvement in operative cash flow. At the end of the period, the EBITDA margin will exceed 80% increasing with respect to the previous target of 78%;
- **a sound capital structure:** the commitment to strengthen equity coefficients continues. During the course of the plan, net debt is estimated as growing by approximately €1.6 billion to €6.7 billion, with a significant reduction of €1 billion with respect to the previous plan. The capital structure remains solid: during the plan, the ratio of net debt and RAB remains below 55% in all years of the plan and the ratio of net debt and EBITDA with respect to the 4.2 times of end 2011, remaining below the 4 times;
- **new dividends policy:** as from 2012, a basic dividend is envisaged from core business amounting to 19 euro cents per share, in addition to the contribution of non-core business (payout of 60% on results and/or gains).

## Economic-financial and sustainability performance

### Main 2011 economic-financial results

2011 was a year that stood out not only for the reliability of the national power transmission grid and the continued investments forecast by the grid Development Plan, but also for the action taken to increase the efficiency of dispatching. It was these latter efforts in particular that have allowed us to achieve the high target for incentives, which was measured in these financial statements at fair value, in view of the three-year duration of the incentives mechanism.

The Group has also been involved in developing the photovoltaic project, which culminated in the completion of a sales contract between Terna, SunTergrid and Terra Firma Investments (GP) 3 Limited, whereby the entire share capital of Rete Rinnovabile S.r.l. was transferred. The sale generated total net income of approximately €196 million (of which €147 million recognised in the 2010 "Profit for the year from discontinued operations and assets held for sale", as contract margin as compared with total costs sustained during the year, on the basis of works completion). Additionally, during the financial year, in order to pursue the optimisation of the projects in the field of the construction of renewable source plants, the Terna Group also undertook an investment programme named "New photovoltaic project", which culminated in the sale, on 24 October 2011, to the private equity fund Terra Firma, of 100% of the share capital of the newly-incorporated Nuova Rete Solare S.r.l. ("NRTS S.r.l.") for a total price of €264 million. The investments made under the scope of the "New photovoltaic project" amounted to a total of approximately €200 million.

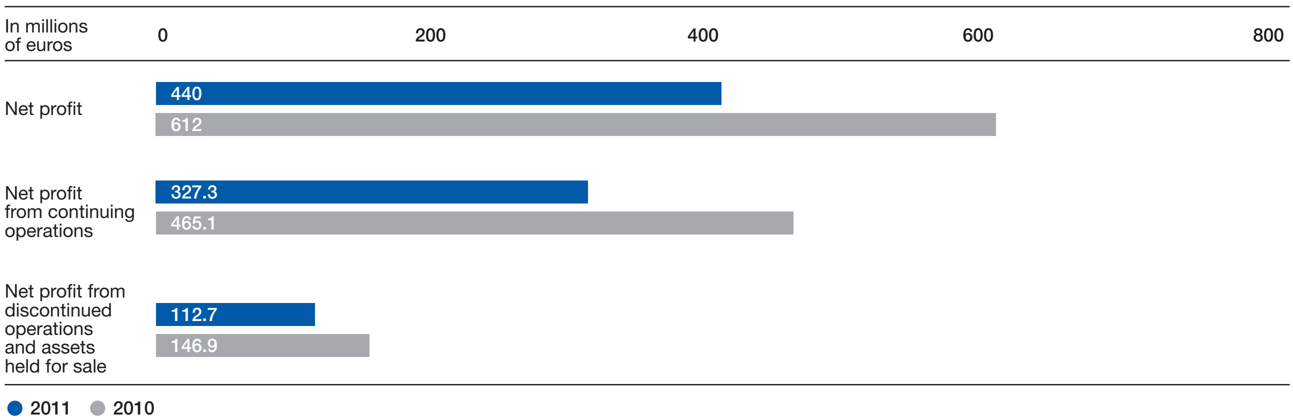
In addition to continuing its business, optimising the management of energy flows and developing the grid, Terna did not lose sight of the opportunities arising under the scope of its core business in Italy and abroad: we note, in Montenegro, the purchase of the investment in CrnoGorski Elektroprenosni Sistem AD ("CGES"), functional to the development of the Italy-Montenegro electrical interconnection and the incorporation of the company Terna Crna Gora d.o.o..

The figures discussed below have been drawn from the reclassified statements included in the section "Group performance and financial position" of this report, taken from the consolidated financial statements as described in the notes to the reclassified statements.

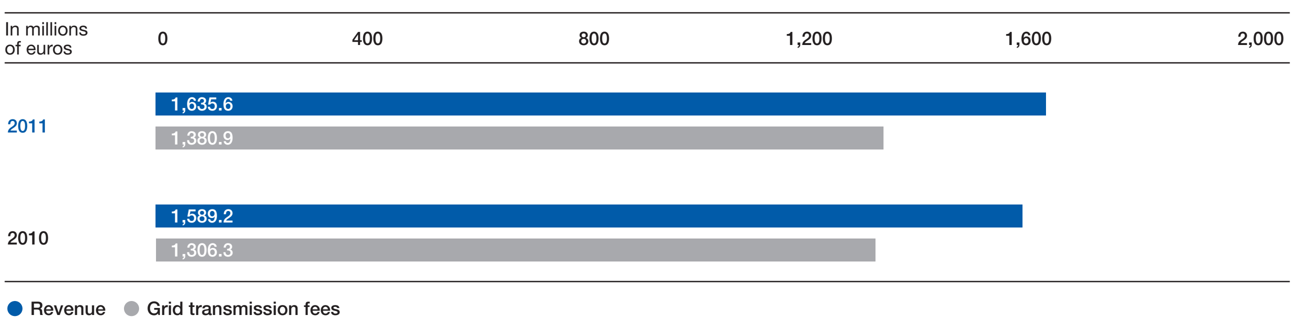
Finally, we should mention the severely negative incidence seen during the financial year on the excellent results achieved by the Group during 2011. This was determined by the application to Terna and the subsidiary Terna Rete Italia, of an increased IRES (corporate income tax) rate of 10.5%, introduced by the "corrective manoeuvre-*bis*" approved by Italian Law Decree no. 138 of 13 August 2011, converted into Law by the Parliament on 14 September 2011. It therefore followed that for both companies, the total IRES tax rate in determining current taxes came to 38% and, in that sense, all net deferred tax funds recorded on the Parent Company's financial statements and those of the subsidiary Terna Rete Italia were adjusted to this balance of the results as of 31 December 2011.

## Comprehensive Group results

The consolidated financial statements as at and for the year ended 31 December 2011 show a **net profit** for the year of €440.0 million, **entirely attributable to the Group**. It includes €327.3 million relating to the profit from continuing operations and €112.7 million to the profit from **assets held for sale**.

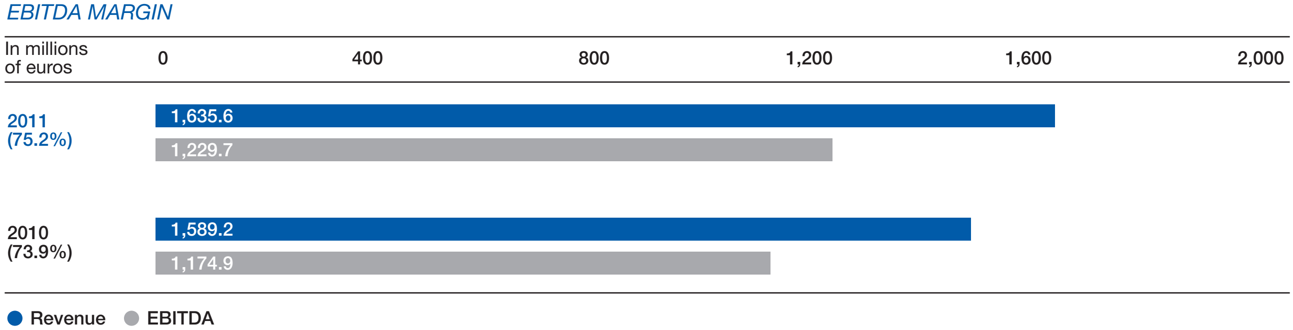



**Revenue** amounts to approximately €1,635.6 million, of which €1,380.9 million refers to the transmission fee with an increase of €46.4 million (+2.9%) over 2010. More specifically, the transmission fee refers to the Parent Company for approximately €1,237.6 million and to the subsidiary Terna Rete Italia for approximately €143.3 million.




**Operating expenses** amounted to some €405.9 million, of which €211.0 million relates to personnel expense and €149.0 million to services. **EBITDA** (gross operating profit) for the year stands at €1,229.7 million, rising by €54.8 million (+4.7%) over €1,174.9 million of 2010. The subsidiary Terna Rete Italia accounted for €139.3 million.
The **EBITDA margin** went from 73.9% in 2010 to 75.2% in financial year 2011.

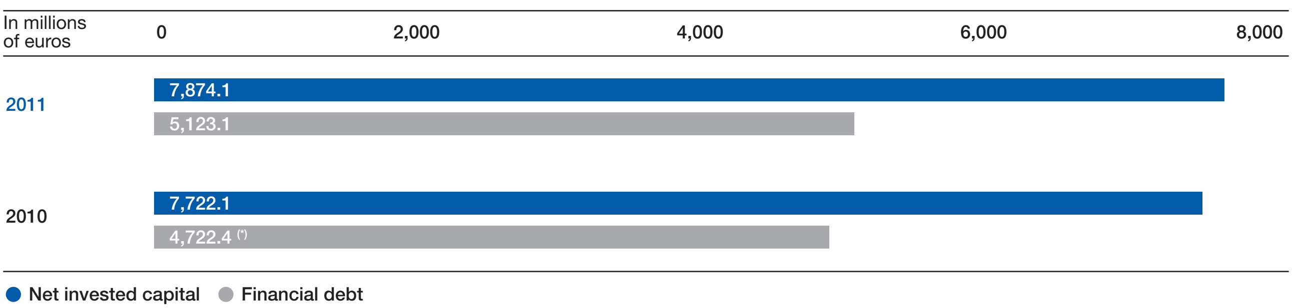
*EBITDA MARGIN*



**EBIT** (operating profit) stands at approximately €835.6 million, after **depreciation and amortisation** charges of €394.1 million, of which €348.8 million recorded by the Parent Company and €45.2 million by the subsidiary Terna Rete Italia.
The **financial position** for the financial year, with a negative balance amounting to €121.0 million, fully attributable to the Parent Company, posts an increase amounting to €18.5 million (+18.0%) on the 2010 figure, mainly due to the increase in gross debt and the rise in market interest rates.
**Income tax** for the financial year amounts to €387.3 million, up on the previous financial year by €140.5 million (+56.9%), mainly as a result of the increased IRES (corporate income tax) introduced by the "corrective manoeuvre-*bis*" (the "Robin Hood Tax").

**Net profit for the financial year from continuing operations** stands at €327.3 million, whilst the **Group's net profit**, including the result of discontinued operations and assets held for sale (equal to €112.7 million), stands at €440.0 million.
**Net profit from continuing operations adjusted** by the total effects of the Robin Hood Tax, and the extraordinary one-off items, including adjustment of IRAP amounts to €465.3 million, up €5.2 million on the same figure of the previous financial year (+1.1%).

**Invested capital net of continuing operations and comprehensive invested capital**, amounting to €7,874.1 million, is financed through shareholders' equity for €2,751.0 million and through **total net financial debt** for €5,123.1 million.



(*) This includes the net cash position of Terna S.p.A. with regard to RTR, amounting to €254.6 million.

The **debt/equity ratio** stands at 1.86.

**Total investments made in core business** by the Group during the year amount to €1,219.8 million (of which €1,168.7 million refer to property, plant and machinery), up 5.0% on the €1,161.7 million figure recorded for 2010.

### Result of discontinued operations and assets held for sale

**Net profit deriving from discontinued operations and assets held for sale** amounts to €112.7 million and relates to the extraordinary sales of the companies of the photovoltaic sector (€50.6 million for the share relating to Rete Rinnovabile S.r.l. and €28.3 million for NRTS S.r.l.) in addition to the reversal of the hold-harmless guarantee issued in relation to the sale of the Brazilian subsidiaries (€33.8 million). The previous financial year figure, amounting to €146.9 million, basically included the net margin for 2010 obtained on photovoltaic plants sold with the subsidiary Rete Rinnovabile.

### Sustainability performance

#### Sustainability indexes and recognitions

The continued improvement in ESG (Environmental, Social, Governance) performance has earned Terna constant growth over time in sustainability ratings, the inclusion on the main international stock exchange indexes for sustainability and the appreciation of socially responsible investors.

In 2011, Terna was confirmed on all the major international sustainability stock exchange indexes, including the Dow Jones Sustainability Index (World and Europe), and was included on the new STOXX Global ESG Leaders indexes, with a presence – the only Italian utility – in all the related sub-indexes specialised in the environmental, social and governance field (STOXX Global Environmental Leaders, STOXX Global Social Leaders and STOXX Global Governance Leaders).

2011 recognitions include:

- entrance into the Gold Class of the “SAM Sustainability Yearbook 2012”, based on the detailed analyses performed by SAM-Sustainable Asset Management, the sustainability ratings agency that carries out assessments for the Dow Jones indexes. On the basis of this assessment, Terna is amongst the top three electricity companies in the world with regard to sustainability performance, out of a total of 104 segment companies. The fact of belonging to the Gold Class requires a ratings score that must be less than 1% from that of the sector leader;
- the confirmation, for the second year running, in the “Carbon Disclosure Leadership Index” prepared by the Carbon Disclosure Project, the international initiative run in 2011 by 551 investors managing 71,000 billion dollars and aimed at guaranteeing transparency on $CO_2$ emissions generated by businesses and on the limitation programmes implemented. In 2011, Terna came in second amongst utilities and an absolute third in terms of transparency in communication on its carbon footprint, a result that is even more important if we consider that Terna is not subject to any obligation to reduce emissions nor to any type of emission trading scheme.

# Comments on the results and significant events

## Significant events

### Corporate

#### Appointment of new Board of Directors and Board of Statutory Auditors

On **13 May 2011**, the Shareholders' Meeting of Terna S.p.A. in addition to approving the separate financial statements at 31 December 2010 and resolving a dividend for the whole of 2010 of €0.21 per share, also appointed the new Board of Directors, whose term of office will expire upon the approval of the financial statements for the year ending 2013. The new Board consists of:

- Luigi Roth (Chairman);
- Flavio Cattaneo (Chief Executive Officer);
- Andrea Camporese (3);
- Paolo Dal Pino;
- Matteo Del Fante;
- Michele Polo;
- Romano Minozzi;
- Fabio Buscarini;
- Salvatore Machì.

Standing auditors were also appointed for the three-year period:

- Luca Aurelio Guarna (Chairman);
- Alberto Luigi Gusmeroli;
- Lorenzo Pozza.

The alternate auditors appointed are Stefania Bettoni and Flavio Pizzini.

The Shareholders' Meeting appointed PricewaterhouseCoopers S.p.A. to carry out the statutory audit of the accounts for the nine-year period from 1 January 2011 to 31 December 2019.

### Core business

#### The new "SA.PE.I" power line linking Sardinia to mainland Italy is opened

On **17 March 2011**, Terna opened the new SA.PE.I. electric main – acronym for SArdinia-PEninsula-Italian – the first direct electrical connection between Sardinia and the continent.

#### Terna Rete Italia-Terna transfer of plants for the development and upgrading of the NTG

On **28 April 2011** Terna Rete Italia S.r.l. sold certain transmission plants to the Parent Company Terna, in order to complete a series of strategic development and renewal investments in the NTG in the operational territories of Milan, Rome, Padua, Florence, Naples and Turin. The total price paid for the transaction amounted to €19.3 million.

#### Terna purchases additional shares in the associate CESI S.p.A.

During the financial year, Terna finalised the purchase of further equity interests in CESI S.p.A., corresponding to 1.5% (on **23 May 2011**) and 1% of the share capital (on **15 November 2011**), respectively from Tirreno Power S.p.A. and SO.G.I.N. - Società Gestione Impianti Nucleari S.p.A..

Following these tansactions, the total equity interest of Terna in the associate stood at 42.406% of the share capital.

CESI S.p.A. develops and manages plants and laboratories for tests, studies and experimental research.

#### Additional IRES

The "corrective manoeuvre-*bis*" approved by Italian Law Decree no. 138 of 13 August 2011, converted into Law by Parliament on 14 September, amongst other matters, amended regulations of the "Robin Hood Tax", establishing an increase for three financial years, from the current additional IRES rate of 6.5% to 10.5% as well as the extension of this additional rate to include companies from the electricity and gas distribution and transmission sector and companies in the renewable energies sector.

It therefore follows that for Terna and the subsidiary Terna Rete Italia, the total IRES tax rate comes to 38%.

This tax increase for the Terna Group has also entailed an overall recalculation of the net provision for deferred tax liabilities of the start of the financial year for approximately €78 million.

#### New 2012-2015 tariff system

By Resolutions nos. 199/11, 204/11 and 197/11 for the regulatory period 2012-2015, the Authority for Electricity and Gas (AEEG) has established remuneration for the supply of electricity transmission, distribution and measurement services,

(3) Resigned on 20 June 2011. In its meeting of 29 July 2011, the Terna Board of Directors resolved the appointment by co-option of Francesco Pensato.

prices for dispatching and the regulation of the quality of the transmission service for the fourth regulatory period (2012-2015) in addition to the ways in which they are updated in subsequent years. In this regard, please refer to the attachment named "Italy's regulatory framework" on AEEG Resolutions.

## International

### Acquisition of the shareholding in CGES and agreement for the construction of the electrical interconnection linking Italy to Montenegro

Terna has fully paid-in the capital increase reserved, thereby becoming the shareholder of CGES with 22.09% of the share capital and, as new shareholder, signed the shareholders' agreement for the new governance system and the industrial contract for investments.
The agreement, which was finalised on **25 January 2011**, represents the end point of a process of industrial and country cooperation and is part of the intergovernmental agreements between Italy and Montenegro which were initiated on 19 December 2007 with the agreement for the start-up of activities of the Italy-Montenegro work group and confirmed on 6 February 2010 by means of the contract which ratified the commitment at an institutional level for the construction of a new submarine electrical interconnection and the implementation of partnerships with national transmission operators.
It is expected that the overall investment of Terna for the first "electrical bridge" to the Balkans will amount to some €760 million. The investment by CGES for the connection to the existing network and the reinforcement of the local grid will total some €100 million.

### Incorporation of new company in Montenegro

On **22 June 2011** Terna incorporated Terna Crna Gora d.o.o. in Montenegro, a limited liability company organised under the laws of Montenegro with an initial share capital of €2 million.
The new company will construct and subsequently run the local transmission infrastructures comprising the Italy-Montenegro electrical interconnection.

## Non-core business

### Photovoltaic project

#### Sale of Rete Rinnovabile S.r.l. completed

In implementation of the agreement signed on 18 October 2010 by Terna S.p.A., SunTergrid S.p.A. and Terra Firma Investments (GP) 3 Limited – wholly owned by Terra Firma Capital Partners III, L.P. – on **31 March 2011** the transfer was completed to RTR Acquisitions S.r.l. (an indirect subsidiary of Terra Firma Investment (GP) 3 Limited) of 100% of the share capital of Rete Rinnovabile S.r.l..
Rete Rinnovabile S.r.l. (including the subsidiary Valmontone Energia S.r.l.), at the date of the sale, held 62 photovoltaic plants – located in 11 different regions of Italy – for a total capacity of 143.7 MWp, of which 101.6 MWp benefit from the Feed-In Tariffs 2010 whilst the remaining 42.1 MWp take advantage of the Feed-In Tariffs of the first quarter 2011.
The sale of the equity interest in Rete Rinnovabile S.r.l. generated total net income of approximately €196 million (of which €147 million recognised in the 2010 consolidated net profit, as contract margin) and the reduction in actual net financial debt of continuing operations of the Terna Group for more than €200 million.
In addition to renting the land, Terna will also provide Rete Rinnovabile S.r.l. with plant maintenance, surveillance and monitoring services, according to multiyear contracts made as part of sale. When the individual rental contracts expire, Terna will regain possession of the leased areas.

#### Sale of Nuova Rete Solare S.r.l. completed

In implementation of the agreement signed on **29 July 2011**, on **24 October 2011**, SunTergrid S.p.A. and RTR Holding III S.r.l. (the "Buyer"), a subsidiary of Terra Firma, completed the transfer to the Buyer of 100% of the share capital of Nuova Rete Solare S.r.l.
The company **Nuova Rete Solare S.r.l.**, incorporated on 8 March 2011 by the subsidiary SunTergrid S.p.A. had been vested, under the scope of the Terna Group, to develop the new investment programme in renewable energies ("New photovoltaic project"), which, *inter alia*, took tangible form through the acquisition of the entire shares in three companies, operating under the scope of the non-conventional energy sector: on 18 May 2011, **Reno Solar 2 S.r.l.**; on 1 June 2011, **Lira PV S.r.l.**; on 7 June 2011, **Solar Margherita S.r.l.**. In September, the three companies were merged into the subsidiary NRTS. As at the sale date, NRTS owns a photovoltaic portfolio (10 sites) with a total capacity of approximately 78.5 MWp, developed and connected but not currently producing. These plants are able to benefit from the incentive tariffs envisaged by the various Energy Accounts, insofar as they had started up by 31 August 2011.
The price agreed in terms of Enterprise Value amounts to €264 million.
Terna provides NRTS with maintenance, surveillance and monitoring services on the plants according to multiyear contracts defined in the context of the sale transaction.

### Incorporation of Terna Plus S.r.l.

On **15 December 2011**, Terna incorporated the company named "Terna Plus S.r.l." of limited liability and with share capital amounting to €50,000. The company object is the design, construction, management, development, operation and maintenance of plants, equipment and infrastructures also on the grid and systems, including the diffused accumulation of energy and pumping and/or storage.

## Finance

### 10-year bond issue for €1.25 billion

On **8 March 2011** Terna launched a bond issue on the market in euros, at a fixed rate, with expiry in 10 years, for a total of €1.25 billion under the scope of its Euro Medium Term Notes (EMTN) programme. This has been assigned an A+ rating for Standard and Poor's, A2 for Moody's and A+ for Fitch.
The bond matures on 15 March 2021 with annual coupon of 4.750% and issue price amounting to 99.245. The share has therefore been priced with a spread of 130 basis points with respect to the mid swap.
The bonds are listed on the Luxembourg Stock Exchange.
The transaction, destined for Institutional Investors, has been placed by a syndicate of banks comprising Banca Akros S.p.A., MPS Capital Services S.p.A., Natixis, UniCredit Bank AG and WestLB AG as joint-lead managers and joint-bookrunners.
The transaction is intended to finance the grid development investments envisaged in the Parent Company's business plan.

### Repayment of syndicate loan

On **8 April 2011** the syndicated bank loan originally taken out on 13 December 2004 and subsequently renegotiated on 10 April 2006 with Banco Bilbao Vizcaya Argentaria S.A, Mediobanca, Intesa Sanpaolo, BNL, Unicredit and Monte dei Paschi di Siena S.p.A. for a total amount of €750 million was repaid.

### Use of credit line

Also, on date of **8 April 2011** the credit line of €500 million signed with Cassa Depositi e Prestiti (CDP) on 2 February 2009 and amended on 22 June 2009 was used.

### Renewal of EMTN Programme worth €4 billion

On **20 May 2011**, Terna renewed its bond issue programme named the "Euro Medium Term Note Programme" (EMTN) worth €4 billion.
Deutsche Bank and Citigroup were the Joint Arrangers for the programme, which obtained ratings of A+ from Standard & Poors, A2 from Moody's and A+ from Fitch.

### Loan from the European Investment Bank (EIB) to finance a four-year investment plan 2011-2014

On **25 July 2011**, Terna S.p.A. signed an agreement with the European Investment Bank (EIB) for a loan of €325 million aimed at strengthening and enhancing the Italian electricity transport system in order to guarantee the safety and efficiency standards required of the transmission service. The loan was disbursed on 1 August 2011.
The loan matures in 2030 and will be repaid in semi-annual instalments as from the sixth year; the annual cost amounts to the 6-month Euribor with a spread of 50 basis points.

### Terna rating

On **23 May 2011**, in compliance with the criteria of the Agency for "government-related entities", S&P reviewed Terna outlook from stable to negative, to reflect the action taken on the Italian Government. On **21 September 2011**, the Agency further reduced the long-term rating of Terna S.p.A. from A+ to A with negative outlook, reflecting the downgrading of the Italian Republic, in compliance with S&P criteria for government-related entities. On **13 December 2011**, the agency set the long and short-term rating of Terna to A/A-1 under observation with negative implications, as a consequence of the similar decision made with regard to the rating of the Italian Republic and the risk that political and social pressure deriving from a worsening of tax and economic restrictions could entail a worsening of the regulatory framework for the company's transmission business.
On **5 October 2011**, Moody's ratings agency reduced the long-term rating of Terna and of its non-subordinate debt from A2 to A3. The outlook assigned to the rating is negative. At the same time, Moody's lowered the short-term rating from Prime-1 to Prime-2. This concludes the review begun by Moody's on 20 June 2011 and follows the agency's downgrading of Italy's credit rating from Aa2 to A2 with negative outlook.
On **18 November 2011**, Fitch revised the outlook of the rating of Terna S.p.A. from "stable" to "negative" due to uncertainties linked to the Company's long-term financial profile, in consideration of the evolution of the scenario for Italy's sovereign rating and the final result of the regulatory review for 2012-2015. On **19 December 2011**, the agency put the A+ rating of Terna's unsecured senior debt under observation for possible downgrading, as a consequence of the same decision recently made by the Agency with regard to the rating of the Italian Republic.
At the same time, Fitch has confirmed both the short-term rating of Terna as F1 and the long-term rating of the issuer as A.

# Terna Group performance and financial position

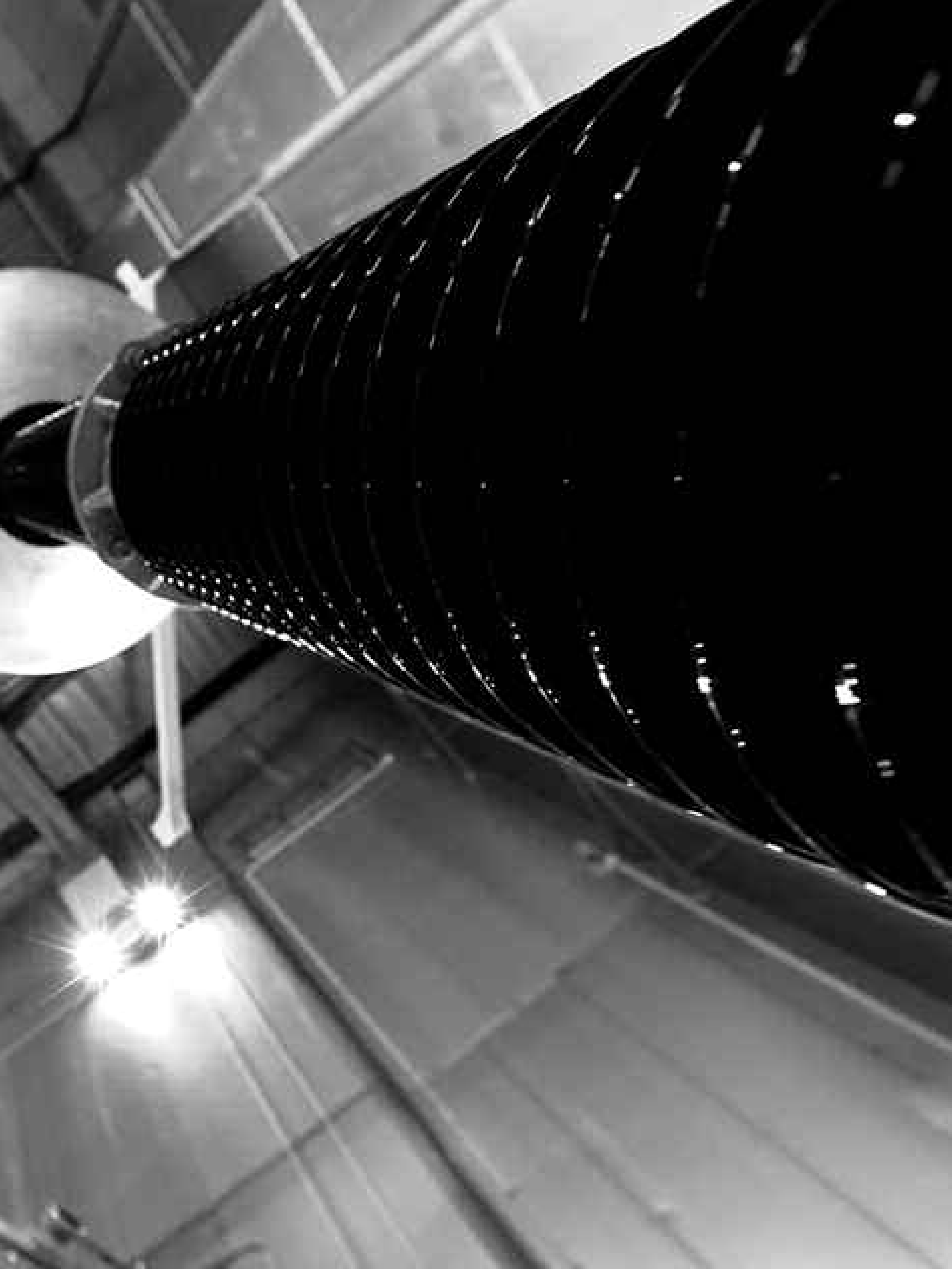
## Introduction

The 2011 annual report of the Terna Group has been prepared in accordance with the provisions of Art. 154-*ter* of Italian Legislative Decree no. 58/98 introduced by Italian Legislative Decree no. 195 of 6 November 2007 (the "Transparency Decree"), as amended by Italian Legislative Decree no. 27 of 27 January 2010.
In implementation of the provision of Italian Legislative Decree no. 38 of 28 February 2005 and EEC Regulation no. 1606/2002, the Terna Group prepares the consolidated financial statements as at and for the year ended 31 December 2011 in compliance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board and endorsed by the European Commission (hereinafter "IFRS-EU").
The 2011 annual report has been prepared on a historic cost basis, modified where necessary for certain financial instruments, as well as on a going concern basis.

## Scope of consolidation

At the 2011 year end, the Group consolidation area includes the following companies:

| Company | Registered office | Business | Currency | Share/quota capital | % held | Consolidation method |
|---|---|---|---|---|---|---|
| COMPANIES CONTROLLED DIRECTLY BY TERNA S.P.A. | | | | | | |
| **Terna Rete Italia S.r.l.** | Rome | Design, construction, management, development, operation and maintenance of high-voltage power lines. | € | 243,577,554 | 100% | Line-by-line |
| **Terna Crna Gora d.o.o.** | Podgorica | Authorisation, construction and management of transmission infrastructures comprising the Italy-Montenegro electrical interconnection in Montenegro. | € | 2,000,000 | 100% | Line-by-line |
| **SunTergrid S.p.A.** | Rome | Construction and maintenance of electricity transmission grids and plants for the generation of electricity, including renewables generation, for own use and sale in Italy and abroad. | € | 120,000 | 100% | Line-by-line |
| **Terna Plus S.r.l.** | Rome | Design, construction, management, development, operation and maintenance of plants, equipment and infrastructures including grids and systems, including diffused energy storage, pumping and/or storage. | € | 50,000 | 100% | Line-by-line |
| CONTROLLED THROUGH SUNTERGRID S.P.A. | | | | | | |
| **Rete Solare S.r.l.** | Rome | Construction and maintenance of electricity transmission grids and plants for the generation of electricity, including renewables generation, for own use and sale in Italy and abroad. | € | 10,000 | 100% | Line-by-line |



Changes in the scope of consolidation since 31 December 2010 relate to:

### Continuing operations:

- the incorporation on 22 June 2011 by Terna of the company **Terna Crna Gora d.o.o.**, a limited liability company incorporated under the laws of Montenegro, which will construct and subsequently run the local transmission infrastructures comprising the Italy-Montenegro electrical interconnection;
- Terna's establishing, on 15 December 2011, the company named **Terna Plus S.r.l.** (hereinafter "**Terna Plus**"), with share capital of €50,000; the company object of Terna Plus is the design, construction, development, operation and maintenance of plants, equipment and infrastructures also on the grid and systems, including the diffused accumulation of energy and pumping and/or storage systems.

It is also specified that on 21 December 2011, the shareholders' meeting of Terna Linee Alta Tensione S.r.l. ("TELAT S.r.l."), resolved to change the company name to "**Terna Rete Italia S.r.l.**".
With reference to associates, according to the development of said interconnection linking Italy to Montenegro, on 25 January 2011 Terna purchased a 22.09% equity interest in the transmission operator of Montenegro **CrnoGorski Elektroprenosni Sistem AD ("CGES")**.
Additionally, following the purchase of further shares in the company **CESI S.p.A.**, on 23 May 2011 and 11 November 2011, Terna now holds 42.406% (from the previous 39.906%).

### Discontinued operations and assets held for sale:

- to the sale of the company **Rete Rinnovabile S.r.l.** (hereinafter "**RTR S.r.l.**"), completed on 31 March 2011 and already extensively described in the paragraph entitled "Significant events", to which we would refer you.

Additionally, during the financial year, on 8 March 2011, the subsidiary SunTergrid S.p.A. incorporated the company **Nuova Rete Solare S.r.l.** (hereinafter "NRTS S.r.l."), which, with a view to developing the investment programme in renewable energies ("New photovoltaic project"), had also acquired the entire shares in three companies, operating in the non-conventional energy sector: on 18 May 2011, **Reno Solar 2 S.r.l.**; on 1 June 2011, **Lira PV S.r.l.**; on 7 June 2011, **Solar Margherita S.r.l.**. In September, the three companies were merged into NRTS. On 24 October 2011, the company was sold to the company RTR Holding III S.r.l. - an indirect subsidiary of Terra Firma Capital Partners III, L.P. ("Terra Firma") through RTR Capital S.r.l..

### Basis of presentation

The measurement and recognition criteria applied in this financial report are consistent with those adopted in the consolidated financial statements at 31 December 2010.
It should be noted that, following the completion of the extraordinary transactions consisting in the sale of the companies Rete Rinnovabile S.r.l. and NRTS S.r.l., as described in detail in the section "Significant events" (see above), the balances related to the sale of the companies have been reclassified in accordance with **IFRS 5 - Non-current assets held for sale and discontinued operations**.
It is also specified that some comparative financial and economic balances of year 2010 have been adjusted to consider the change to the model for booking the effects relating to the release (4) of goodwill made by the Parent Company in 2009. More specifically, the previous model for booking substitute tax (advances on current taxes) has been reviewed in line with the different accounting recognition (prepaid and current taxes) of the substitute tax paid in relation to the release (5) of goodwill resulting from the consolidation of the subsidiary Terna Rete Italia.
More specifically, this restatement has entailed the recording at 31 December 2010 of greater deferred tax assets for an amount of €25.2 million and less tax assets for €12.6 million, with an impact of €14.2 million recognised amongst retained earnings and €1.6 million as a lower result (greater current taxes) on the shareholders' equity as at 31 December 2010.

(4) Italian Law Decree no. 185 of 29 November 2008, converted into Italian Law no. 2 of 28 January 2009.
(5) Italian Law Decree no. 98 of 6 July 2011, converted with amendments by Italian Law no. 111 of 15 July 2011.

## Reclassified consolidated income statement

The reclassified consolidated income statement of the Terna Group for 2011 and 2010 is shown below.

| In millions of euros | 2011 | 2010 | Change | % |
|---|---|---|---|---|
| **Revenue** | | | | |
| Grid transmission fees [(1)] | 1,380.9 | 1,306.3 | 74.6 | 5.7% |
| Other energy items [(1)] | 163.4 | 169.8 | (6.4) | (3.8%) |
| Other revenue from sales and services [(1)] | 47.0 | 57.0 | (10.0) | (17.5%) |
| Other revenue and income | 44.3 | 56.1 | (11.8) | (21.0%) |
| **Total revenue** | **1,635.6** | **1,589.2** | **46.4** | **2.9%** |
| **Operating expenses** | | | | |
| Personnel expenses | 211.0 | 212.2 | (1.2) | (0.6%) |
| Services and leases and rentals | 149.0 | 152.2 | (3.2) | (2.1%) |
| Materials | 20.7 | 28.2 | (7.5) | (26.6%) |
| Other costs [(2)] | 25.2 | 21.7 | 3.5 | 16.1% |
| **Total operating expenses** | **405.9** | **414.3** | **(8.4)** | **(2.0%)** |
| **EBITDA (gross operating profit)** | **1,229.7** | **1,174.9** | **54.8** | **4.7%** |
| **Amortisation and depreciation** [(3)] | **394.1** | **360.5** | **33.6** | **9.3%** |
| **EBIT (operating profit)** | **835.6** | **814.4** | **21.2** | **2.6%** |
| Net financial income (expense) [(4)] | (121.0) | (102.5) | (18.5) | 18.0% |
| **Profit before taxes** | **714.6** | **711.9** | **2.7** | **0.4%** |
| Income taxes | 387.3 | 246.8 | 140.5 | 56.9% |
| **Profit for the year from continuing operations** | **327.3** | **465.1** | **(137.8)** | **(29.6%)** |
| Profit for the year from discontinued operations and assets held for sale | 112.7 | 146.9 | (34.2) | (23.3%) |
| **Profit for the year** | **440.0** | **612.0** | **(172.0)** | **(28.1%)** |
| *Attributable to owners of the Parent* | *440.0* | *612.0* | *(172.0)* | *(28.1%)* |

In the consolidated income statement:
(1) this amount is included in the “Revenue from sales and services” caption;
(2) corresponds to “Other operating expenses” and “Amortisation, depreciation and impairment” for the impairment of non-current assets (€2.1 million) and trade receivables (€0.1 million);
(3) corresponds to “Amortisation, depreciation and impairment” net of the impairment of non-current assets (€2.1 million) and trade receivables (€0.1 million);
(4) total of the captions presented in points 1, 2 and 3 of letter C. “Financial income/expense”.

In 2011, the Terna Group recorded **revenue** for €1,635.6 million, relating to the Parent Company for approximately €1,484.5 million and to the subsidiary Terna Rete Italia for approximately €150.1 million, up €46.4 million on the previous financial year (+2.9%), **attributable to the trend of the grid transmission fees**, up €74.6 million and relating to:

- the Parent Company for €64.6 million, as a result of the combination of:
  - review of the tariffs (€51.2 million, including the incentive on the remuneration of strategic works, pursuant to Resolution ARG/elt 87/10) and the related contingency items of competence (€2.1 million);
  - grid transmission fees related to the Defence Plan (€11.3 million);
- the subsidiary Terna Rete Italia, for its share of the NTG, €10.0 million (compared with the €133.3 million reported in 2010).

The increase in the transmission fee is partially compensated for by lesser revenue (overall for a negative €28.2 million) for:
- dispatching activities, totalling a negative €6.4 million, mainly attributable to lower investments made on dispatching infrastructures [6] with respect to the previous financial year (a negative €4.2 million);
- other sales and services (a negative €10 million), mainly for less engineering and renewable plant connection activities; and
- lower other revenue and income (a negative €11.8 million), mainly due to the recognition during the previous financial year of:
  - gain from bargain purchase, of €6.0 million, deriving from the acquisition of the investment in Rete di Trasmissione Brescia; and
  - greater reimbursements for damages to major plants (3.5 million) recognised by the Parent Company.

In 2011, **operating expenses** amounted to €405.9 million and mainly referred to the Parent Company (€394.4 million) and the subsidiary Terna Rete Italia (€10.8 million), recording a decrease of approximately €8.4 million on last year (a negative 2%), mainly by virtue of the combined effect of the following phenomena:
- personnel expenses: a €1.2 million reduction, mainly due to greater capitalisation;
- costs for services and materials: overall reduction of €10.7 million, referring to lesser investments in dispatching infrastructures [6] (a negative €4.3 million), mainly for the optimisation on the Services Market in 2010; and for the reduction of non-regulated activities and engineering towards third parties;
- other costs: the item in question increases by €3.5 million, referring for the most part to greater impairment of fixed assets (€1.9 million) and to higher net costs linked to energy transmission and dispatching (€1.4 million).

**EBITDA** (gross operating profit) for the year stands at around €1,229.7 million, up €54.8 million on the €1,174.9 million recorded for 2010 (+4.7%). Terna Rete Italia contributes for €139.3 million (amounting to approximately 11.3%).
The increase in revenue, together with the drop in costs is reflected in the **EBITDA margin** which went from 73.9% in 2010 to 75.2% in financial year 2011.

**Amortisation and depreciation** for the year are up by €33.6 million on 2010, for €30.0 million related to the Parent Company, basically for the start-up of new plants, and for €3.5 million to the amortisation of the subsidiary Terna Rete Italia.

As a result, **EBIT** (operating profit) stands at about €835.6 million, up by €21.2 million (+2.6%) compared with 2010.

**Net financial expense**, amounting to €121.0 million, refers entirely to the Parent Company and increases to €18.5 million from €102.5 million of 2010, mainly as a result of the increase in financial expense relating to the medium and long-term debt and related hedges (a negative €60 million), mainly due to the increase in gross debt and the rise in market interest rates; partially compensated for by:
- greater liquidity invested at higher interest rates (€21.2 million); and
- higher capitalised financial expense (€8.5 million) due to greater capital expenditure during the financial year;
- positive impact deriving from the currency adjustment to the provision for probable expenses relating to the sale of the equity interest held in the Brazilian subsidiaries (€6.8 million);
- recognition and adjustment of the equity interests in the companies CGES (€1.8 million) and CESI (€2.3 million) to the share held in the shareholders' equity of the associates.

After the impact of net financial expense, the **profit before taxes** stands at €714.6 million, €2.7 million higher than the previous financial year (+0.4%).

**Income taxes** for the financial year amount to €387.3 million, up on the previous financial year by €140.5 million (+56.9%), mainly as a result of the "corrective manoeuvre-*bis*" (the "Robin Hood Tax"), against a pre-tax result that was basically in line with 2010.
More specifically, greater taxes are recognised for the year for €153.8 million, resulting from the adjustment to net deferred tax liabilities for approximately €65.4 million and greater current taxes for €88.4 million.
Income taxes also reflect the overall impact of the IRAP adjustment (€8.7 million) with reference to the effects of the economic manoeuvre for the concession holders, lower income from prior years adjustments (€4.0 million) and the one-off positive effects relating to the release of Terna Rete Italia goodwill which is seen in the consolidated financial statements (a negative €23.5 million).
The year's tax rate amounts to 54.2%; without considering one-off elements, it stands at 46%, up approximately 11 points on the 2010 figure, mainly as a consequence of the IRES tax (the "Robin Hood Tax", +10.7%) and also for the additional IRAP (regional tax on productive activities) tax on pre-tax profit (+0.5%).

**Profit from continuing operations** consequently stands at €327.3 million, down €137.8 million on 2010.
Profit from continuing operations adjusted by the total effects of the "Robin Hood Tax", and the extraordinary one-off items described above, including IRAP adjustment, amounts to €465.3 million, up €5.2 million on the same figure of the previous financial year (+1.1%).

(6) Pursuant to IFRIC 12.

**The Group's profit** amounts to €440 million and includes €112.7 million **net profit deriving from discontinued operations and assets held for sale**, relating to extraordinary transactions in the photovoltaic sector (€50.6 million for the share of RTR S.r.l. and €28.3 million for NRTS S.r.l.) and the release of the guarantee connected with the sale of the Brazilian subsidiaries (€33.8 million). In the previous financial year, the item "Profit for the financial year from discontinued operations and assets held for sale", amounting to €146.9 million mainly included the net margin for 2010 realised on photovoltaic plants sold with the subsidiary RTR.

## Reclassified statement of financial position of the Group

Reclassified consolidated statements of financial position of the Terna Group at 31 December 2011, and 31 December 2010, obtained by reclassifying the figures shown in the consolidated statement of financial position, are presented below.

| In millions of euros | At 31.12.2011 | At 31.12.2010 | Change |
|---|---|---|---|
| **Net non-current assets** | | | |
| Intangible assets and goodwill | 470.9 | 470.6 | 0.3 |
| Property, plant and equipment | 8,618.2 | 7,802.6 | 815.6 |
| Financial assets (1) | 74.0 | 30.4 | 43.6 |
| **Total** | **9,163.1** | **8,303.6** | **859.5** |
| **Net working capital** | | | |
| Trade receivables (2) | 612.4 | 511.5 | 100.9 |
| Inventories | 16.3 | 11.4 | 4.9 |
| Other assets (3) | 14.9 | 16.2 | (1.3) |
| Trade payables (4) | 705.0 | 480.6 | 224.4 |
| Payables for pass-through energy items, net (5) | 247.0 | 77.3 | 169.7 |
| Net tax liabilities (6) | 121.5 | 68.3 | 53.2 |
| Other liabilities (7) | 294.3 | 294.2 | 0.1 |
| **Total** | **(724.2)** | **(381.3)** | **(342.9)** |
| **Gross invested capital** | **8,438.9** | **7,922.3** | **516.6** |
| Sundry provisions (8) | 564.8 | 599.0 | (34.2) |
| Net invested capital in continuing operations | 7,874.1 | 7,323.3 | 550.8 |
| Net invested capital in discontinued operations and assets held for sale | 0.0 | 398.8 | (398.8) |
| **Total net invested capital** | **7,874.1** | **7,722.1** | **152.0** |
| Equity attributable to owners of the Parent | 2,751.0 | 2,773.2 | (22.2) |
| Equity attributable to non-controlling interests | 0.0 | 0.2 | (0.2) |
| **Actual net financial debt from continuing operations** (9) (*) | **5,123.1** | **4,722.4** | **400.7** |
| Net financial debt from continuing operations | 5,123.1 | 4,977.0 | 146.1 |
| Net financial debt from discontinued operations and assets held for sale | 0.0 | (28.3) | 28.3 |
| **Total net financial debt** | **5,123.1** | **4,948.7** | **174.4** |
| **Total** | **7.874.1** | **7,722.1** | **152.0** |

(*) At 31.12.2010, includes the net cash position with regard to RTR (€254.6 million)

Reported in the consolidated statement of financial position as:
(1) "Equity-accounted investees", "Other non-current assets" and "Non-current financial assets" for the carrying amount of the other investments (€0.6 million);
(2) "Trade receivables" net of the receivables for energy-related pass-through revenue (€1,077.8 million);
(3) "Other current assets" net of other tax assets (€11.1 million) and "Current financial assets" in relation to the amount of deferred financial assets (€5.5 million);
(4) "Trade payables" net of the payable for energy-related pass-through costs (€1,324.8 million);
(5) "Trade receivables" for the value of receivables for pass-through energy revenue (€1,077.8 million) and "Trade payables" for the value of payables for pass-through energy costs (€1,324.8 million);
(6) "Income tax assets", "Other current assets" for the value of other tax receivables (€11.1 million), "Other current liabilities" for the value of other tax payables (€20.5 million) and "Income tax liabilities";
(7) "Other non-current liabilities", "Current financial liabilities" and "Other current liabilities" net of other tax liabilities (€20.5 million);
(8) "Employee benefits", "Provisions for risks and charges" and "Deferred tax liabilities";
(9) "Long-term loans", "Current portion of long-term loans", "Non-current financial liabilities", "Cash and cash equivalents", "Non-current financial assets" for the value of FVH derivatives (€521.8 million) and "Current financial assets" for the value of the deposit certificates (€150.0 million).

The increase in net fixed assets amounting to €859.5 million with respect to the figures at 31 December 2010 is mainly due to the item **property, plant and equipment** (amounting to €815.6 million), mainly as a result of the joint effect of:
- investments for €1,178.1 of which €1,168.7 in core business;
- amortisation and depreciation for the year of €343.3 million.

**Intangible assets and goodwill** show a balance that is basically in line with the previous financial year (+€0.3 million) as a result of the combination of:
- investments in the year for €51.1 million (of which €34.4 million in dispatching infrastructures);
- amortisation in the year (€50.8 million including, in particular, €25.1 million for the amortisation of dispatching infrastructures and €5.6 million for the amortisation of the concession).

Please remember that this caption includes the net carrying amount of the infrastructures used by the dispatching service totalling €140.9 million at 31 December 2011 (compared with €131.5 million at 31 December 2010).

**The Group's total investments in core business** in 2011 amount to €1,219.8 million, up 5% on the same figure for 2010.

**Financial assets** post an increase of 43.6 million, mainly deriving from the acquisition of the equity interest in the associate CGES (€36 million) and the adjustment to shareholders' equity at the year-end for the associate CESI (€7.1 million) of which the Group acquired a further shareholding during the financial year (for a total of +2.5%).

**Net working capital** stands at a negative €724.2 million and has generated liquidity for €342.9 million, essentially due to the combined effect of:
- increases in trade payables (€224.4 million) for the increase in investing activities during the last period of the financial year and also as a result of the payments made during the first few days of the next financial year;
- an increase in net trade payables and receivables for electricity dispatching services of the Parent Company, which generated cash totalling €169.7 million, in particular due to:
  - increase in payables relating to the capacity payment (€110.8 million);
  - increase in payables linked to the essential production units for the safety of the electrical system (€84.7 million).
- increase in net tax payables (€53.2 million) due to the tax authority for:
  - greater current taxes (€46.9 million);
  - net VAT payable (€11.2 million);
  - net of the greater credits and withholdings on interest accrued on financial assets for €4.5 million;
- increase in trade receivables amounting to €100.9 million, mainly referring to the price for transmission activities, for €51.9 million, mainly as a result of the recognition of the receivable due from CCSE related to the "mitigation" mechanism in consumption established by Resolution ARG/elt 188/08, for the adjustment of the receivable for the incentive connected with the reduction in volumes provisioned on the Market for Dispatching Services (€66 million) and with the quality of the transmission service (€7.7 million); these changes have been partly offset by the income received during the financial year in relation to receivables ascertained in 2009 for said incentive (Market for Dispatching Services).

**Gross invested capital** therefore amounted to €8,438.9 million, up by €516.6 million on the previous financial year.
Other provisions fell by €34.2 million, mainly due to:
- the partial release of the provision set aside in 2009 (€33.8 million at 31 December 2010) for contractual obligations maturing during the financial year, deriving from the sale of the controlling stake in Terna Participações;
- recording of the deferred tax asset on the change of the fair value associated with the derivative cash flow hedging instruments for €24.4 million;
- accrual for deferred tax assets for tax recognition of the goodwill recorded on the consolidated financial statements, arising from the acquisition of the subsidiary Terna Rete Italia S.r.l. (formerly TELAT) established by Italian Law Decree no. 98 of 6 July 2011 (amounting to €39.8 million);
- utilisation of prior period allocations convering the accelerated depreciation recorded by the parent Terna and the subsidiary Terna Rete Italia (€39.1 million and €3.3 million respectively);

partially offset by the adjustment (equal to approximately €72.6 million) of the balances for net deferred tax liabilities for the start of the year, by virtue of the additional IRES (the "Robin Hood Tax") and also by the accruals for probable expenses connected with the sale of Nuova Rete Solare S.r.l. and Rete Rinnovabile S.r.l. (€30.7 million and €11.9 million respectively).

**Net invested capital in continuing operations and comprehensive net invested capital** stand at €7,874.1 million, up respectively by €550.8 million with respect to the net invested capital in continuing operations at 31 December 2010 and €152 million with respect to comprehensive net invested capital at 31 December 2010.
**Comprehensive net invested capital** is financed through the Group's shareholders' equity for €2,751 million, as against the €2,773.4 million at 31 December 2010, and the net financial debt for €5,123.1 million (€400.7 million on the actual net financial debt from continuing operations, which at 31 December 2010 included the net cash position with regard to RTR, amounting to €254.6 million).

The **debt/equity ratio** (total net financial debt/shareholder's equity) stands at 1.86.

### Reconciliation of consolidated profit for the year and equity attributable to the owners of the Parent with the corresponding figures for the Parent Company

A reconciliation of consolidated equity and profit with the amounts reported by the Parent Company is provided below:

| In millions of euros | Net profit 2011 | Equity at 31.12.2011 | Net profit 2010 | Equity at 31.12.2010 |
|---|---|---|---|---|
| **Financial statements of the Parent Company** | **453.6** | **2,555.3** | **432.1** | **2,546.9** |
| Results and equity contributed by TRI (*) | 0.6 | 59.9 | 33.2 | 59.3 |
| Reversal of Dividends from SunTergrid | (100.0) | - | | |
| Results and Equity brought by the SunTergrid Group | 78.6 | 120.9 | 143.4 | 158.3 |
| Results and Equity of the other Group subsidiaries | (0.1) | (0.1) | | |
| Equity-accounted investees | 7.3 | 15.0 | 3.3 | 8.7 |
| *Continuing operations result* | *327.3* | | *466.7* | |
| *Result of discontinued operations and assets held for sale* | *112.7* | | *145.3* | |
| **Terna Group Consolidated financial statements** | **440.0** | **2,751.0** | **612.0** | **2,773.2** |
| Non-controlling interests | - | - | - | 0.2 |
| **Consolidated figures** | **440.0** | **2,751.0** | **612.0** | **2,773.4** |

(*) Includes the one-off effects on provisions for deferred tax liabilities at the start of the year in relation to additional IRES (the "Robin Hood Tax") and IRAP adjustment relating to the consolidation of the subsidiary TRI (€22.4 million).

### Cash flows

#### Net financial debt

The Group's net financial debt at 31 December 2011 (€5,123.1 million) is broken down in the table below.

| In millions of euros | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| **Net financial debt from continuing operations** | | | |
| **A. Medium- and long-term debt:** | | | |
| Bond (1) | 4,303.9 | 2,728.2 | 1,575.7 |
| Floating-rate loans (1) | 2,434.8 | 2,419.3 | 15.5 |
| Derivative financial instruments (2) | (410.4) | (153.2) | (257.2) |
| **Total A** | **6,328.3** | **4,994.3** | **1,334.0** |
| **B. Short-term debt (liquidity):** | | | |
| Floating-rate loans (current portion) (3) | 59.7 | 59.7 | 0.0 |
| Short-term loans | 0.0 | 73.1 | (73.1) |
| Short-term investments (4) | (150.0) | 0.0 | (150.0) |
| Cash and cash equivalents | (1,114.9) | (150.1) | (964.8) |
| **Total B** | **(1,205.2)** | **(17.3)** | **(1,187.9)** |
| **Net financial debt from continuing operations** | **5,123.1** | **4,977.0** | **146.1** |
| **Actual net financial debt from continuing operations** (*) | **5,123.1** | **4,722.4** (*) | **400.7** |
| **Total financial debt from discontinued operations and assets held for sale** | **0.0** | **(28.3)** | **28.3** |
| **Total** | **5,123.1** | **4,948.7** | **174.4** |

(*) At 31.12.2010, includes the net cash position with regard to RTR (€254.6 million).

Reported in the consolidated statement of financial position as:
(1) this balance corresponds to the "Long term loans" caption;
(2) this figure corresponds to "Non-current financial liabilities" and "Non-current financial assets" for the value of the fair value hedge derivatives (€521.8 million);
(3) this balance corresponds to the "Current portion of long-term loans" caption;
(4) this balance is included in the "Current financial assets" caption.

The increase of €400.7 million with respect to actual net financial debt from continuing operations at 2010 year-end - which considers the de-consolidation of the net cash position with regard to RTR at 31 December 2010 (amounting to 254.6 million) - is mainly the result of the combined effect of:

- increase in bonds (€1,575.7 million), for the issue of a bond in March 2011, for a total value of €1,250.0 million (amounting to €1,234.8 million net of expenses and issue fees), as a result of the fair value adjustment of financial instruments (€323.8 million, including the amortised cost) and the capitalisation of period inflation (€17.1 million);
- increase in floating-rate loans (€15.5 million), essentially by virtue of the combined effect of the following changes:
  - obtaining on 1 August 2011 by the European Investment Bank (EIB) of a loan of €325 million expiring in 2030;
  - use on 8 April 2011 of the credit line of €500 million granted by Cassa Depositi e Prestiti (CDP);
  - repayment of the syndicated bank loan (revolving credit facility) originally taken out on 13 December 2004 and subsequently renegotiated on 10 April 2006 with Banco Bilbao Vizcaya Argentaria S.A., Mediobanca, Intesa Sanpaolo, BNL, Unicredit and Monte dei Paschi di Siena S.p.A. for a total amount of €750 million;
  - repayment of the EIB loan instalments due for €59.7 million;
- increase of the positive net balance of derivative financial instruments (€257.2 million), mainly due to the lowering of the reference interest rates compared to the previous financial year. In particular, we note the change in fair value hedges of bonded loans for €321.5 million and the change in cash flow hedges of the floating rate debt for a negative €64.3 million;
- repayment of the short-term loan taken out in late 2010 (€50 million);
- subscription in 2011 of deposit certificates maturing on 14 June 2013 and with the faculty to request early redemption every three months, for a total of €150 million;
- increase in liquid funds for €964.8 million, due to the operations described above in relation to the bonds and other loans and to cash inflows from to the extraordinary operations occurring during the financial year, in addition to the operation connected with the core business.

Financial debt from discontinued operations and assets held for sale at 31 December 2010, amounting to a negative €28.3 [7] million, was represented by the CHF derivative asset of the companies transferred, RTR and Valmontone Energia S.r.l. (€22.1 million) – to hedge a loan stipulated in January 2011 – and liquid funds on bank current accounts (€6.2 million).



(7) Effective financial debt of discontinued operations and assets held for sale at 31 December 2010 amounted to €226.3 million if we consider the net financial liability of RTR to Terna S.p.A..

## Statement of cash flows

| In millions of euros | Cash flow at 31.12.2011 | Reconciliation financial statements | Cash flow at 31.12.2010 | Reconciliation financial statements |
|---|---|---|---|---|
| **Opening cash and cash equivalents** | **156.3** | | **0.1** | |
| *of which Cash and cash equivalents of discontinued operations* | | *6.2* | | *0.0* |
| Profit for the year | 440.0 | | 612.0 | |
| *of which Profit for the year from continuing operations* | | *327.3* | | *465.1* |
| Amortisation and depreciation | 394.1 | | 360.5 | |
| Net change in provisions | (34.2) | | (10.9) | |
| *Employee benefits* | | *(3.1)* | | *(2.8)* |
| *Provisions for risks and charges* | | *22.2* | | *22.2* |
| *Deferred tax liabilities* | | *(53.3)* | | *(30.3)* |
| Net losses (gains) on asset disposals (1) | (3.6) | | (3.1) | |
| **Self-financing** | **796.3** | | **958.5** | |
| Change in net working capital | 342.9 | | (203.5) | |
| Inventories | | (4.9) | | 0.3 |
| Trade receivables | | (194.4) | | (326.7) |
| Current financial assets | | (5.0) | | 0.5 |
| Income tax receivables | | (0.2) | | 0.0 |
| Other current assets | | (0.2) | | 7.3 |
| Trade payables | | 487.6 | | 60.2 |
| Tax liabilities | | 46.9 | | 25.6 |
| Current financial liabilities | | 15.9 | | (1.3) |
| Other liabilities | | (2.8) | | 30.6 |
| **Cash flows from operating activities** | **1,139.2** | | **755.0** | |
| **Investments** | | | | |
| Property, plant and equipment (2) | (1,178.1) | | (1,104.4) | |
| *of which continuing operations - core business investments* | | *(1,168.7)* | | *(1,103.4)* |
| Intangible assets (3) | (51.1) | | (58.3) | |
| Other changes in non-current assets | (20.8) | | (29.7) | |
| Other intangible assets | | 0.0 | | 0.2 |
| Property, plant and machinery (2) | | 22.8 | | (20.6) |
| *of which contribution of newly purchased companies* | | *0.0* | | *(43.4)* |
| Non-current financial assets | | (0.1) | | (0.5) |
| Other non-current assets | | (0.3) | | (0.8) |
| Equity-accounted investees | | (43.2) | | (8.1) |
| Discontinued operations | | 0.0 | | 0.1 |
| **Total cash flows generated by/(used in) investing activities** | **(1,250.0)** | | **(1,192.4)** | |
| **NIC in discontinued operations and assets held for sale** | **398.8** | | **(398.8)** | |
| Change in loans | 1,133.0 | | 1,346.7 | |
| Non-current financial assets | | (321.5) | | (77.1) |
| Current financial assets | | (150.0) | | 500.0 |
| Non-current financial liabilities | | 64.3 | | (35.5) |
| Long-term loans | | 1,591.2 | | 948.3 |
| Short-term loans | | (73.1) | | 33.1 |
| Discontinued operations and assets held for sale | | 22.1 | | (22.1) |
| Other changes in equity attributable to owners of the Parent (4) | (40.1) | | 46.3 | |
| *Equity attributable to the owners of the Parent - Share capital, other reserves and retained earnings/losses carried forward* | | *(24.1)* | | *30.3* |
| *Equity attributable to the owners of the Parent - Reserves for assets held for sale* | | *(16.0)* | | *16.0* |
| Dividends paid to the owners of the Parent (4) | (422.1) | | (400.8) | |
| Equity attributable to non-controlling interests in discontinued operations and assets held for sale (4) | (0.2) | | 0.2 | |
| **Total cash flows generated by/(used in) financing activities** | **670.6** | | **992.4** | |
| **Total cash flows for the year** | **958.6** | | **156.2** | |
| of which continuing operations | | 964.8 | | 150.0 |
| **Closing cash and cash equivalents** | **1,114.9** | | **156.3** | |
| *of which Cash and cash equivalents included in discontinued operations and assets held for sale* | | *0.0* | | *6.2* |

(1) Included in the balances of "Other revenue and income" and "Other operating expenses" of the consolidated income statement.
(2) See note 13 to the financial statements.
(3) See note 15 to the financial statements.
(4) See the statement of changes in consolidated equity.

## Change in net financial position

In order to more clearly present the actual cash flows for the year, the table below shows the contribution of continuing operations to the generation or use of cash in operating activities, investing activities, and in return on capital.

| In millions of euros | 31.12.2011 | 31.12.2010 |
|---|---|---|
| **Opening net financial debt** | **(4,948.7)** | **(3,758.2)** |
| **Self-financing** | **796.3** | **958.5** |
| *of which continuing operations* | *686.5* | *811.6* |
| **Change in net working capital** | **342.9** | **(203.5)** |
| **Cash flows generated from operating activities** | **1,139.2** | **755.0** |
| Investments in property, plant and equipment | (1,178.1) | (1,104.4) |
| *of which continuing operations - core business investments* | *(1,168.7)* | *(1,103.4)* |
| Investments in intangible assets | (51.1) | (58.3) |
| Other changes in non-current assets | 22.5 | (21.1) |
| Change in equity investments | (43.3) | (8.6) |
| **Cash flows used in investing activities** | **(1,250.0)** | **(1,192.4)** |
| **NIC Assets held for sale** | **398.8** | **(398.8)** |
| Dividends | (422.1) | (400.8) |
| Other changes in equity attributable to the owners of the Parent | (40.1) | 46.3 |
| *of which continuing operations* | *(24.1)* | *30.3* |
| Equity attributable to non-controlling interests | (0.2) | 0.2 |
| **Self-financing flows** | **(462.4)** | **(354.3)** |
| Change in financial debt | (174.4) | (1,190.5) |
| *of which continuing operations* (*) | *(400.7)* | *(964.2)* |
| **Closing net financial debt** | **(5,123.1)** | **(4,948.7)** |

(*) At 31.12.2010, includes the net cash position with regard to RTR (€254.6 million).

The cash flow generated from operating activities during the financial year stands at about €1,139.2 million and is related to self-financing (€796.3 million) and other financial resources generated by net working capital (€342.9 million).

Under the scope of **self-financing**, we have a profit for the financial year of €440 million (of which €327.3 million referred to continuing operations), amortisation/depreciation for the year of €394.1 million and a net decrease in provisions amounting to €34.2 million, which reflects the changes in the provision for deferred tax liabilities and the provision for risks and charges.

The change in **net working capital,** equal to €342.9 million, is for the most part due to the net increase of trade payables.

**Investing activities** have used financial resources for approximately €1,250 million, for the most part relating to investments made during the financial year in property, plant and equipment (€1,178.1 million, of which €1,168.7 million relating to investments in core business) and in intangible assets (€51.1 million) - attributable to the Parent Company for a total of €1,172.4 million - net of set-up grants (€12.1 million) and changes for net divestments and impairment (€7.1 million). Financial investments include an equity interest of 22.09% in the share capital of the Montenegro associate CGES (€36 million) and the increase in the value of the equity interest in CESI S.p.A. (€7.1 million).

**Cash flows** used in self-financing are essentially the result of the distribution of the 2010 dividends to the owners of the Parent Company (€261.3 million) and the interim dividend for 2011 (€160.8 million).
The other **changes in equity** attributable to the owners of the Parent refer to the fair value measurement of the cash flow hedges on the floating-rate debt, net of the related tax effect, of the Parent (a negative €34.7 million) and of the transfer

of the derivative asset following sale of the company RTR (a negative €16 million) and the effects of the stock options exercised during the year (€11.6 million) as well as the effects of the acquisition of additional equity interests in the associate CESI S.p.A. (a negative €1 million).

With reference to **discontinued operations and assets held for sale**, the sale of the equity interest in Rete Rinnovabile generated total liquid funds of more than €200 million, whilst the contribution of the sale of NRTS to the self-financing of the Group amounted to €28.3 million.
Therefore, in view of the extraordinary transactions carried out during the financial year, the financial resources generated by operating activities and those used by investing activities and by changes in shareholders' equity, the Group has increased its net debt by €400.7 million with respect to actual net financial debt from continuing operations at 31 December 2010.

## Terna S.p.A. performance and financial position

### Introduction
The 2011 annual report of Terna S.p.A. has been prepared in accordance with the provisions of Art. 154-ter of Italian Legislative Decree no. 58/98 introduced by Italian Legislative Decree no. 195 of 6 November 2007 (the "Transparency Decree"), as amended by Italian Legislative Decree no. 27 of 27 January 2010.
In implementation of the provision of Italian Legislative Decree no. 38 of 28 February 2005 and EEC Regulation no. 1606/2002, Terna S.p.A. prepares the separate financial statements as at and for the year ended 31 December 2011 in compliance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board and endorsed by the European Commission (hereinafter "IFRS-EU").
The 2011 annual report has been prepared on a historic cost basis, modified where necessary for certain financial instruments, as well as on a going concern basis.
In compliance with the provisions of Art. 2364 of the Italian Civil Code and Art. 9.2 of the company's Articles of Association, the Board of Directors has resolved to call the shareholders to meet within one hundred and eighty days of the financial year end, insofar as Terna S.p.A. is a company required to prepare the consolidated financial statements.

### Basis of presentation
The measurement and recognition criteria applied in this annual financial report are consistent with those adopted in the separate financial statements at 31 December 2010.

It is appropriate to point out that, following maturity during the financial year of the contractual obligations deriving from the 2009 sale of the stake in Terna Participações, the economic effect for the release of the related earlier accrual was reclassified in accordance with the provisions of accounting standard "**IFRS 5 - Non-current assets held for sale and discontinued operations**".

It is also specified that some comparative financial and economic balances of year 2010 have been adjusted to consider the change to the model for booking the effects relating to the release (8) of goodwill made by Terna in 2009. More specifically, the previous model for booking substitute tax (advances on current taxes) has been reviewed in line with the different accounting recognition (prepaid and current taxes) of the substitute tax paid for the release (9) of goodwill originating from the consolidation of the subsidiary Terna Rete Italia.
More specifically, this restatement has entailed the recording at 31 December 2010 of greater deferred tax assets for an amount of €25.2 million and lower tax assets for €12.6 million, with an impact of €14.2 million recognised amongst retained earnings and €1.6 million as a lower result (greater current taxes) under shareholders' equity as at 31 December 2010.

(8) Law Decree no. 185 of 29 November 2008, as converted into Law no. 2 of 28 January 2009.
(9) Law Decree no. 98 of 6 July 2011, converted with amendments into Law no. 111 of 15 July 2011.

## Reclassified income statement of Terna S.p.A.

The reclassified income statement of Terna S.p.A. for 2011 and 2010 is shown below.

| In millions of euros | 2011 | 2010 | Change | % |
|---|---|---|---|---|
| **Revenue** | | | | |
| Grid transmission fees (1) | 1,237.6 | 1,173.0 | 64.6 | 5.5% |
| Other energy items (1) | 163.4 | 169.8 | (6.4) | (3.8%) |
| Other revenue from sales and services (1) | 115.0 | 116.3 | (1.3) | (1.1%) |
| Other revenue and income | 37.9 | 46.0 | (8.1) | (17.6%) |
| **Total revenue** | **1,553.9** | **1,505.1** | **48.8** | **3.2%** |
| **Operating expenses** | | | | |
| Personnel expenses | 214.2 | 214.8 | (0.6) | (0.3%) |
| Services and leases and rentals | 165.8 | 166.5 | (0.7) | (0.4%) |
| Materials | 34.1 | 36.7 | (2.6) | (7.1%) |
| Other costs (2) | 18.2 | 17.8 | 0.4 | 2.2% |
| **Total operating expenses** | **432.3** | **435.8** | **(3.5)** | **(0.8%)** |
| **EBITDA (gross operating profit)** | **1,121.6** | **1,069.3** | **52.3** | **4.9%** |
| **Amortisation and depreciation (3)** | **348.8** | **318.8** | **30.0** | **9.4%** |
| **EBIT (operating profit)** | **772.8** | **750.5** | **22.3** | **3.0%** |
| Net financial income (expense) (4) | (8.8) | (87.7) | 78.9 | (90.0%) |
| **Profit before taxes** | **764.0** | **662.8** | **101.2** | **15.3%** |
| Income taxes | 344.2 | 232.1 | 112.1 | 48.3% |
| **Profit for the year from continuing operations** | **419.8** | **430.7** | **(10.9)** | **(2.5%)** |
| Profit for the year from discontinued operations and assets held for sale | 33.8 | 1.4 | 32.4 | |
| **Profit for the year** | **453.6** | **432.1** | **21.5** | **5.0%** |

In the income statement:
(1) this figure is included in “Revenue from sales and services”;
(2) corresponds to “Other operating expenses” and “Amortisation, depreciation and impairment” for the impairment of trade receivables (€0.1 million);
(3) corresponds to “Amortisation, depreciation and impairment” net of the impairment of trade receivables (€0.1 million);
(4) corresponds to the balance of the items described under points 1 and 2 of “C. Financial income/expense”.

2011 **revenue**, amounting to €1,553.9 million, records an increase of €48.8 million (+3.2% on the €1,505.1 million of 2010), which mainly derives from the higher grid transmission fees, amounting to €64.6 million (+5.5%), as a result of the following:

- review of the tariffs (€51.2 million, including the incentive on the remuneration of strategic works, pursuant to Resolution ARG/elt 87/10) and the related contingency items for the period (€2.1 million);
- grid transmission fees related to the Defence Plan (€11.3 million).

This increase is largely offset by:

- other energy items (a negative €6.4 million or -3.8%) mainly due to:
  - incentive mechanism associated with the reduction in volumes procured from the Market for Dispatching Services made available under AEEG Resolution 213/09 (€66 million, being a negative €11 million compared with €77 million incentives reported at 31 December 2010);
  - lesser investments made on the dispatching infrastructures, recognised in pursuance of IFRIC 12 (a negative €4.2 million);
  - increase of other tariff components connected with dispatching activities and quality of service for €8.8 million;
- other revenue and income (a negative €8.1 million), mainly for the higher repayments for damages to primary plants (a negative 3.5 million) and greater contingency assets (a negative 6.0 million) recognised during the previous financial year, net of greater penalties charged to suppliers recognised during the year (€1.5 million).

**Operating expenses** amount to €432.3 million and show a reduction of €3.5 million (-0.8%) on the 2010 figure. This is mainly due to the costs for services and materials (a negative €3.3 million), largely relating to the greater investments in dispatching infrastructures [10] in 2010.

**EBITDA** (gross operating profit) stands at €1,121.6 million, representing to 72.2% of revenue (up 1.2 percentage points from 2010); it rose by €52.3 million over €1,069.3 million of 2010 (+4.9%).

**Amortisation and depreciation** for the year amount to €348.8 million and are up by €30.0 million on 2010 (+9.4%), mainly due to the entry into operation of new plants.

**EBIT** (operating profit) came to €772.8 million, for an increase of €22.3 million (+3%) from financial year 2010.

**Net financial expense** for the year is €8.8 million and was considerably lower than €87.7 million reported for 2010. The €78.9 million decrease) is mainly due to the combined effect of:
- dividends for €100.0 million distributed by the subsidiary SunTergrid;
- greater financial expense deriving from medium and long-term debt and the related hedges (a negative €60.1 million) due to the increased gross debt and the rise in market interest rates in 2011;
- greater liquidity invested at higher interest rates (€21.2 million);
- capitalised financial expense (€8.5 million) due to greater capital expenditure during the year and;
- gain arising from the currency conversion of the provision for risks relating to the sale of the stake in the Brazilian subsidiaries (€6.8 million);

**Income taxes** for the year amount to €344.2 million, up on the previous financial year by €112.1 million (+48.3%), mainly as a result of the tax manoeuvre described above (the "Robin Hood Tax"), against profit before taxes up €101.2 million on 2010.

More specifically, income taxes increased by €129.2 million, as a result of higher net deferred tax liabilities for approximately €47.9 million and greater current taxes for €81.3 million.
Income taxes also reflect the overall impact of the adjustment of IRAP (€6 million) with reference to the effects of the economic manoeuvre for the concession holders, lower income from previous years adjustments (€3.9 million) and the one-off positive effects relating to the release of Terna Rete Italia goodwill which is disclosed in the consolidated financial statements (a negative €23.5 million).

The year's tax rate (45.1%), without considering the initial adjustments of provisions for net deferred tax liabilities, adjustments relating to previous financial years and net of the effects of the release of goodwill as described above, stands at 40.4%, up approximately 5 percentage points on the 2010 figure. This is the result of the greater IRES rate (the "Robin Hood Tax", +9.3%) and the incidence of the additional IRAP tax on the profit before taxes (+0.4%), net of the tax effects on dividends distributed by the subsidiary SunTergrid (-4.7%)

**Profit from continuing operations** stands at €419.8 million, down €10.9 million (-2.5%) on the €430.7 million recorded for 2010.
**Profit for the financial year**, including the result of assets held for sale (€33.8 million for the release of the provision relating to contractual obligations connected with the sale of Terna Participações) is equal to €453.6 million, as compared with €432.1 million of the previous financial year.

(10) Pursuant to IFRIC 12.

## Reclassified statement of financial position of Terna S.p.A.

The reclassified statement of financial position of Terna S.p.A. at 31 December 2011 and 2010 is summarised below. The table is obtained by reclassifying the data stated in the Statement of financial position.

| In millions of euros | At 31.12.2011 | At 31.12.2010 | Change |
|---|---|---|---|
| **Net non-current assets** | | | |
| Intangible assets and goodwill | 362.6 | 362.6 | 0.0 |
| Property, plant and equipment | 7,514.0 | 6,687.7 | 826.3 |
| Financial assets (1) | 629.4 | 590.0 | 39.4 |
| **Total** | **8,506.0** | **7,640.3** | **865.7** |
| **Net working capital** | | | |
| Trade receivables (2) | 606.2 | 511.3 | 94.9 |
| Inventories | 12.4 | 11.4 | 1.0 |
| Other assets (3) | 17.4 | 17.6 | (0.2) |
| Trade payables (4) | 722.9 | 491.2 | 231.7 |
| Payables for pass-through energy items, net (5) | 247.0 | 77.3 | 169.7 |
| Net tax liabilities (6) | 96.5 | 67.0 | 29.5 |
| Other liabilities (7) | 284.7 | 287.9 | (3.2) |
| **Total** | **(715.1)** | **(383.1)** | **(332.0)** |
| **Gross invested capital** | **7,790.9** | **7,257.2** | **533.7** |
| Sundry provisions (8) | 430.6 | 511.1 | (80.5) |
| Net invested capital in continuing operations | 7,360.3 | 6,746.1 | 614.2 |
| Net invested capital in discontinued operations | 0.0 | 4.6 | (4.6) |
| **Total net invested capital** | **7,360.3** | **6,750.7** | **609.6** |
| Equity | 2,555.3 | 2,546.9 | 8.4 |
| Net financial debt from continuing operations | 4,805.0 | 4,458.4 | 346.6 |
| Net financial debt from discontinued operations | 0.0 | (254.6) | 254.6 |
| **Total net financial debt (9)** | **4,805.0** | **4,203.8** | **601.2** |
| **Total** | **7,360.3** | **6,750.7** | **609.6** |

Reported in the statement of financial position as:
(1) "Other non-current assets" and "Non-current financial assets" for the value of equity investments (€622.8 million);
(2) "Trade receivables" net of receivables for energy-related pass-through revenue (€1,077.8 million);
(3) "Other current assets" net of other tax assets (€7.9 million) and "Current financial assets" in relation to the amount of deferred financial assets (€8.2 million);
(4) "Trade payables" net of the payable for energy-related pass-through costs (€1,324.8 million);
(5) "Trade receivables" for the value of receivables for pass-through energy revenue (€1,077.8 million) and "Trade payables" for the value of payables for pass-through energy costs (€1,324.8 million);
(6) "Income tax assets", "Other current assets" for the value of other tax receivables (€7.9 million), "Other current liabilities" for the value of other tax payables (€20.4 million) and "Income tax liabilities";
(7) "Other non-current liabilities", "Current financial liabilities" and "Other current liabilities" net of other tax liabilities (€20.4 million);
(8) "Employee benefits", "Provisions for risks and charges" and "Deferred tax liabilities";
(9) "Long-term loans", "Current portion of long-term loans", "Non-current financial liabilities", "Cash and cash equivalents", "Non-current financial assets" for the value of the loan to Terna Rete Italia and FVH derivatives (€500 million and €521.8 million, respectively) and "Current financial assets" for the value of deposit certificates (€150.0 million).

The €865.7 million increase in net non-current assets since 31 December 2010, is attributable to:
- **property, plant and equipment**, which increased by €826.3 million.

The following is a breakdown of the changes in property, plant and equipment for the year:

In millions of euros

| **Investments** | |
|---|---|
| Transmission lines | 431.8 |
| Transforming stations | 569.4 |
| Other | 121.5 |
| **Total investments** | **1,122.7** |
| Depreciation | (299.1) |
| Disposals, impairment losses and other changes | (15.3) |
| Intra-group transactions | 18.0 |
| **Total** | **826.3** |

The increase (€826.3 million) is the net effect of new capital expenditures (€1,122.7 million), depreciation (a negative €299.1 million) and disposals, impairment and other net reductions (a negative €15.3 million) during the year. It also reflects the acquisition of the transmission plants from the subsidiary Terna Rete Italia (€19.6 million) in order to carry out a series of urgent interventions for the development and renewal of the NTG and sale to the subsidiary SunTergrid (€1.6 million) of the MV/HV electrical utilities substation for the connection of the photovoltaic plant of Lanuvio;
- **financial assets**, which show an increase of €39.4 million, mainly due to the acquisition of 22.09% in the share capital of the Montenegro company CGES (€34.2 million) and an additional interest (+2.5%) in the associate CESI (€2.7 million). The caption also reflects the establishment by the Parent Company of the companies Terna Crna Gora and Terna Plus, as extensively described in the paragraph entitled "Significant events" (€2 million).

**Net working capital** stands at a negative €715.1 million and generated €332 million in liquidity during the year essentially deriving from the following:
- **trade payables:** increases in amounts due to suppliers (€231.7 million) for the increase in investing activities during the last period of the financial year and also as a result of the payments made during the first few days of the next financial year;
- **net payables for pass-through energy items:** the increase (€169.7 million) is largely related to:
  - increase in net debt relating to the capacity payment (€110.8 million);
  - increase in payables linked to the essential production units for the safety of the electrical system (€84.7 million);
- **net tax liabilities:** the increase of €29.5 million mainly originates from the greater amounts owing to the tax authorities for current taxes (€19.1 million), net payable for VAT (€15.2 million) after the recognition of greater receivables and withholdings on interest accrued on financial assets (€4.5 million);
- **trade receivables:** increase of €94.9 million mainly refers to the price for transmission activities, for €51.9 million, chiefly as a result of the recognition of the receivable due from CCSE related to the "mitigation" mechanism in consumption established by Resolution ARG/elt 188/08, of the adjustment of the receivable for the incentive connected with the reduction in volumes provisioned on the Market for Dispatching Services (€66 million) and with the quality of the transmission service (€7.7 million); these changes have been partly compensated for by the receipts during the financial year in relation to receivables ascertained in 2009 for said incentive (Market for Dispatching Services).

The **gross invested capital** therefore amounts to €7,790.9 million, recording an increase of €533.7 million as compared with 31 December 2010.

**Sundry provisions**, amounting to €430.6 million, post a decrease of a negative €80.5 million, mainly due to:
- the release of the provision set aside in 2009 (€33.8 million inclusive of the exchange gains or losses) for contractual obligations maturing during the financial year, deriving from the sale of the controlling stake in Terna Participações;
- the recognition for €24.4 million of the deferred tax asset on the change of the fair value associated with the cash flow hedges;
- the accrual for deferred tax assets for tax recognition of the goodwill recorded in the consolidated financial statements deriving from the acquisition of the subsidiary Terna Rete Italia S.r.l. (formerly TELAT) established by Italian Law Decree no. 98 of 6 July 2011 (amounting to €39.8 million);
- the use of the provision for deferred tax liabilities recorded on previous allocations for additional amortisation/depreciation with respect to the tax relevant shares (€39.1 million);

- the adjustment of net deferred tax liabilities at the start of the year, as a result of the IRES (the “Robin Hood Tax”, €52.8 million) and IRAP (€2.7 million) taxes, as described previously.

**Net invested capital** stands at €7,360.3 million and is financed through **equity** for €2,555.3 million (as compared with €2,546.9 million as of 31 December 2010) and by **net financial debt** for €4,805.0 million (+€346.6 million as compared with 31 December 2010).

The **debt/equity** ratio (net financial debt/equity) stands at 1.88.

The following is a breakdown of net financial debt:

| In millions of euro | At 31.12.2011 | At 31.12.2010 | Change |
|---|---|---|---|
| Long-term debt (inclusive of the short-term portion) and related hedges | 6,388.0 | 5054.0 | 1334.0 |
| Short-term loans | 0.0 | 73.1 | (73.1) |
| Short-term investments | (150.0) | 0.0 | (150.0) |
| Cash and cash equivalents | (1,114.3) | (150.1) | (964.2) |
| **Financial transactions with subsidiaries** | | | |
| Loan to Terna Rete Italia | (500.0) | (500.0) | 0.0 |
| Net current a/c position of intercompany treasury | 181.3 | (18.6) | 199.9 |
| **Net financial debt from continuing operations** | **4,805.0** | **4,458.4** | **346.6** |
| **Financial debt from discontinued operations and assets held for sale** | **0.0** | **(254.6)** | **254.6** |
| **Total net financial debt** | **4,805.0** | **4,203.8** | **601.2** |

For a breakdown of the individual components of this net debt at 31 December 2011, see “Cash flows” below.

## Cash flows

### Net financial debt

Net financial debt of the Company (€4,805.0 million) at 31 December 2011 can be broken down as follows:

| In millions of euros | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| **A. Medium- and long-term debt** | | | |
| Bond (1) | 4,303.9 | 2,728.2 | 1,575.7 |
| Floating-rate loans (1) | 2,434.8 | 2,419.3 | 15.5 |
| Derivative financial instruments (2) | (410.4) | (153.2) | (257.2) |
| Loan to Terna Rete Italia (3) | (500.0) | (500.0) | 0.0 |
| **Total** | **5,828.3** | **4,494.3** | **1,334.0** |
| **B. Short-term debt (liquidity)** | | | |
| Floating-rate loans (current portion) (4) | 59.7 | 59.7 | 0.0 |
| Short-term loans | 0.0 | 73.1 | (73.1) |
| Short-term investments (5) | (150.0) | 0.0 | (150.0) |
| Net current a/c position of intercompany treasury (6) | 181.3 | (18.6) | 199.9 |
| Cash and cash equivalents (6) | (1,114.3) | (150.1) | (964.2) |
| **Total** | **(1,023.3)** | **(35.9)** | **(987.4)** |
| **Total financial debt from continuing operations** | **4,805.0** | **4,458.4** | **346.6** |
| **Total financial debt from discontinued operations** | **0.0** | **(254.6)** | **254.6** |
| **Total** | **4,805.0** | **4,203.8** | **601.2** |

In the statement of financial position:
(1) this figure corresponds to the “Long-term loans” caption;
(2) this figure corresponds to “Non-current financial liabilities” and “Non-current financial assets” for the value of the fair value hedge derivatives (€521,8 million);
(3) this figure is included under “Non-current financial assets”;
(4) this figure corresponds to the “Current portion of long-term loans” caption;
(5) this figure is included under “Current financial assets”;
(6) this figure is included under “Cash and cash equivalents”.

Net financial debt of continuing operations records an increase of €346.6 million, mainly as a result of the combination of:

- increase in bonds (€1,575.7 million), for the issue of a bond in March 2011, for a total value of €1,250.0 million (amounting to €1,234.8 million net of expenses and issue fees), as a result of the fair value adjustment of financial instruments (€323.8 million, including the amortised cost) and the capitalisation of period inflation (€17.1 million);
- increase in floating-rate loans (€15.5 million), essentially by virtue of the combined effect of the following changes:
  - obtaining on 1 August 2011 by the European Investment Bank (EIB) of a loan of €325 million expiring in 2030;
  - use on 8 April 2011 of the credit line of €500 million granted by Cassa Depositi e Prestiti (CDP);
  - repayment of the syndicated bank loan (revolving credit facility) originally taken out on 13 December 2004 and subsequently renegotiated on 10 April 2006 with Banco Bilbao Vizcaya Argentaria S.A., Mediobanca, Intesa Sanpaolo, BNL, Unicredit and Monte dei Paschi di Siena S.p.A. for a total amount of €750 million;
  - repayment of the EIB loan instalments due for €59.7 million;
- increase of the positive net balance of derivative financial instruments (€257.2 million), mainly due to the lowering of the reference interest rate compared to the previous financial year. In particular, we note the change in fair value hedges of bonds for €321.5 million and the change in cash flow hedges of the floating rate debt for a negative €64.3 million;
- repayment of the short-term loan taken out in late 2010 (€50 million);
- subscription in 2011 of deposit certificates maturing on 14 June 2013 and with the faculty to request early redemption every three months, for a total of €150 million;
- increase in cash and cash equivalents of €764.3 million – including the change in the net position on the intercompany current accounts held with the subsidiaries in the context of the centralised treasury management – due to the transactions connected with the core business and to the operations described above.

The financial debt from discontinued operations, amounting to a negative €254.6 at 31 December 2010, is represented by the loan granted by Terna to RTR (€500 million), net of the liability of the treasury current a/c (€245.4 million).

## Statement of cash flows

| In millions of euros | Cash flow at 31.12.2011 | Reconcil. financial statements | Cash flow at 31.12.2010 | Reconcil. financial statements |
|---|---|---|---|---|
| **Opening cash and cash equivalents & intercompany current accounts** | **168.7** | | **0.1** | |
| Profit for the year | 453.6 | | 432.1 | |
| *of which continuing operations* | | *419.8* | | *430.7* |
| Amortisation and depreciation | 348.8 | | 318.8 | |
| Net change in provisions | (80.4) | | (9.8) | |
| *Employee benefits* | | *(3.0)* | | *(2.8)* |
| *Provision for future risks and charges* | | *(22.8)* | | *17.2* |
| *Deferred tax liabilities* | | *(54.6)* | | *(24.2)* |
| Net losses (gains) on asset disposals (1) | (3.9) | | (3.1) | |
| **Self-financing** | **718.1** | | **738.0** | |
| Change in net working capital | 336.5 | | (179.6) | |
| *Inventories* | | *(1.0)* | | *0.3* |
| *Trade receivables* | | *(188.4)* | | *(318.5)* |
| *Current financial assets* | | *(5.3)* | | *0.4* |
| *Other current assets* | | *1.5* | | *7.9* |
| *Trade payables* | | *494.9* | | *65.2* |
| *Tax liabilities* | | *19.1* | | *48.3* |
| *Current financial liabilities* | | *15.9* | | *(1.3)* |
| *Other liabilities* | | *(4.8)* | | *22.7* |
| *Discontinued operations and assets held for sale* | | *4.6* | | *(4.6)* |
| **Cash flows from operating activities** | **1,054.6** | | **558.4** | |
| **Investments** | | | | |
| Property, plant and equipment (2) | (1,122.7) | | (1,063.4) | |
| Intangible assets (3) | (49.7) | | (57.0) | |
| Other changes in non-current assets | (38.2) | | (13.2) | |
| *Property, plant and equipment* | | *1.2* | | *(4.7)* |
| *Other intangible assets* | | *0.0* | | *0.2* |
| *Non-current financial assets* | | *(39.0)* | | *(8.1)* |
| *Other non-current assets* | | *(0.4)* | | *(0.7)* |
| *Discontinued operations and assets held for sale* | | *0.0* | | *0.1* |
| **Total cash flows generated by/(used in) investing activities** | **(1,210.6)** | | **(1,133.6)** | |
| Change in loans | 1,365.5 | | 1,111.5 | |
| *Current financial assets* | | *(150.0)* | | *500.0* |
| *Non-current financial assets* | | *(321.5)* | | *(77.1)* |
| *Non-current financial liabilities* | | *64.3* | | *(35.5)* |
| *Long-term loans* | | *1,591.2* | | *948.3* |
| *Short-term loans* | | *(73.1)* | | *30.4* |
| *Discontinued operations and assets held for sale* | | *500.0* | | *(500.0)* |
| *Liabilities from discontinued operations and assets held for sale* | | *(245.4)* | | *245.4* |
| Other changes in equity (4) | (23.1) | | 33.1 | |
| *Equity - Share capital and other reserves* | | *(23.1)* | | *33.1* |
| Dividends (4) | (422.1) | | (400.8) | |
| **Total cash flows generated by/(used in) financing activities** | **920.3** | | **743.8** | |
| **Total cash flows for the year** | **764.3** | | **168.6** | |
| **Closing cash and cash equivalents & intercompany current accounts** | **933.0** | | **168.7** | |

(1) Included in the "Other revenue and income" and "Other operating costs" captions of the income statement.
(2) See note 11 to the financial statements.
(3) See note 13 to the financial statements.
(4) See the statement of changes in consolidated equity.

## Change in net financial position

| In millions of euros | 2011 | 2010 |
|---|---|---|
| **Opening net financial debt** | **(4,203.8)** | **(3,260.9)** |
| **Self-financing** | **718.1** | **738.0** |
| ***of which continuing operations*** | ***684.3*** | ***736.6*** |
| **Change in net working capital** | **336.5** | **(179.6)** |
| **Cash flows generated from operating activities** | **1,054.6** | **558.4** |
| Investments in property, plant and equipment | (1,122.7) | (1,063.4) |
| Infra-group disposals (acquisitions) of fixed assets | (18.0) | (21.2) |
| Investments in intangible assets | (49.7) | (57) |
| Disposals (acquisitions) of equity investments | (39.0) | (8.1) |
| Other changes in non-current assets | 18.8 | 16.1 |
| **Cash flows used in investing activities** | **(1,210.6)** | **(1,133.6)** |
| Dividends distributed | (422.1) | (400.8) |
| Other changes in equity | (23.1) | 33.1 |
| **Equity movements** | **(445.2)** | **(367.7)** |
| Change in financial debt | (601.2) | (942.9) |
| **Closing net financial debt** | **(4,805.0)** | **(4,203.8)** |

The liquidity generated by operating activities during the year, amounting to €1,054.6, can be ascribed to self-financing (€718.1 million, of which €684.3 million continuing operations) and to changes in net working capital (€336.5 million). More specifically, as part of the self-financing, it includes the profit for the financial year of €453.6 million, comprising the result deriving from discontinued operations and assets held for sale (amounting to €33.8 million for the release of the provision referring to the contractual obligations connected with the sale of Terna Participações), amortisation and depreciation for €348.8 million and the net decrease in provisions for €80.4 million that reflects the change in the provision for net deferred tax liabilities and the provision for risks as commented on previously.
**The management in net working capital**, equal to €336.5 million, is largely due to the net increase in trade payables.

**Investing activities** led to a net use of cash of about €1,210.6 million. These cash flows mainly concerned investments in property, plant and equipment (€1,122.7 million) and intangible assets (€49.7 million) for the year, net of set-up grants (€11.8 million). Cash flow also reflects the acquisition from the subsidiary Terna Rete Italia (formerly TELAT) of some transmission plants involved by development and renewal works (€19.6 million) and the transfer to the subsidiary SunTergrid (€1.6 million) of a MV/HV utility electrical substation. Financial investments recognise the equity interest amounting to 22.09% of the share capital of the Montenegro transmission operator CGES (€34.2 million), the increase in the equity interest in the associate CESI (€2.7 million) and the incorporation of the companies Terna Crna Gora and Terna Plus (€2.0 million).
Cash used in relation to **equity movements** is essentially the result of the distribution of the 2010 dividends (€261.3 million) and the interim dividend for 2011 (€160.8 million). Other changes in equity refer to the fair value adjustment of derivative instruments hedging floating-rate payables (cash flow hedges), net of the related tax effect (a negative €34.7 million) and the effects of the stock options exercised during the year (€11.6 million).
Therefore, cash flows used in investing activities and equity movements for the year resulted in total uses of liquidity in the amount of €1,655.8 million, which was funded in part by cash flows generated from operating activities (€1,054.6 million) and the remaining €601.2 million through new debt.

# The Terna Group and outlook

## Subsequent Events

### Resolutions published by the AEEG for the new tariffs in regulatory period 2012-2015

On **2 January 2012**, the Authority for Electricity and Gas (AEEG) published Resolutions nos. 199/11, 204/11 and 197/11 thereby establishing, for the new regulatory period 2012-2015, the remuneration for the supply of electricity transmission, distribution, measurement and dispatching services and the regulation of the quality of the transmission service. The new features introduced by AEEG resolution 199/11 include taking the weighted average cost of capital (WACC) from the previous 6.9% to 7.4% and establishing a review by November 2013, to apply from the second two-year period of the regulatory period (2014-2015). There will also be a new incentive category (category I4) for an extra remuneration of accumulation systems amounting to 2% for a period of 12 years subsequent to the coming into force of the investments. As from 2012, the AEEG has recognised a further 1% on the WACC, aimed at compensating for the effect of the "regulatory lag", i.e. the delay with which the tariff remunerates investments made. Resolution 204/11 updates for 2012 the price for the electricity dispatching service, amounting to €0.0526 c/kWh. Resolution 197/11 on the regulation of the quality of service confirms the framework of the previous regulatory period, based on a premium/penalty mechanism. Quality of service will only be monitored by the Energy not supplied index. With this mechanism, the potential maximum impact is estimated for the Terna Group as ranging between a negative €12/€30 million per year.

### Terna alone in the Gold Class of the Sam Sustainability Yearbook 2012

On **30 January 2012** Terna, the only Italian electrical company and amongst the world's best, joined the Gold Class of the Sam - Sustainability Yearbook 2012, the yearbook of the international ratings agency that screens companies, assessing the possibility of their accessing, remaining in or being excluded from the prestigious Dow Jones indexes. If we compare this result with those of previous years (Silver Class in 2011, Bronze Class in 2010), we can see that Terna is reinforcing, indeed improving its position in a global top position, coming before some of the best international operators.

### 5-year bond issue for €1.25 billion

On **13 February 2012** Terna launched a bond issue on the market in euros, at a fixed rate, with expiry in 5 years, for a total of €1.25 billion under the scope of its Euro Medium Term Notes (EMTN) programme. This has been assigned an A- Credit Watch Negative rating for Standard and Poor's, A3 Outlook Negative for Moody's and A for Fitch.
The bond expires on 17 February 2017, has an annual coupon of 4.125% and issue price of 99.809%. The security has thus been priced with a spread of 257 basis points as compared with the mid swap. The securities, which will pay one coupon per year, will be listed on the Luxembourg Stock Exchange.
The operation is intended for institutional investors and is placed by a pool of banks comprising BNP Paribas, Credit Suisse, Deutsche Bank, J.P. Morgan, Mediobanca, MPS Capital Services, Natixis and Unicredit Bank AG as joint-lead managers and joint-bookrunners; it closed successfully that same day and was 4.5 times oversubscribed compared to the offer, 80% of which came from abroad. The bond is intended to finance the grid development investments envisaged in the Company's business plan.

### Renewed Supervisory Body 231/2001

On **31 January 2012**, Terna's Board of Directors appointed the members of the Supervisory Body pursuant to Italian Legislative Decree no. 231/2001, which had expired in financial year 2011. Prof. Bruno Assumma was confirmed Chairman, while Mr. Ernesto Calaprice, Mr. Massimo di Noia, Mr. Alberto Bianchi and Ms. Filomena Passeggio were appointed members. The Board also resolved that Mr. Fulvio De Luca will act as secretary of the Supervisory Body, together with the audit function.

### Terna Cnra Gora share capital increase

On **10 February 2012**, Terna subscribed a share capital increase of the subsidiary Terna Cnra Gora for €5 million, in order to provide the company with the resources necessary to develop the business.

### Terna rating

On **30 January 2012** Fitch Ratings revised the rating for senior unsecured debt of Terna S.p.A. from A+ to A following the downgrading of the Italian Republic from A+ to A- with negative outlook. At the same time, Fitch confirmed both the long-term rating of the issuer at A with negative outlook and the short-term rating at F1.
On **8 March 2012** S&P confirmed the long and short-term rating of Terna S.p.A. as A- and A-2 respectively and the senior unsecured debt rating at A-. In line with the Agency method for government related entities, these levels had been assigned to the Company on **20 January 2012**, following the downgrading from A to BBB+ of the Italian Republic. At the same time, the Agency removed the "CreditWatch" status with negative implications, the long-term rating of the Company and the rating of the senior unsecured debt, a status assigned by the agency in December 2011. Outlook is negative.

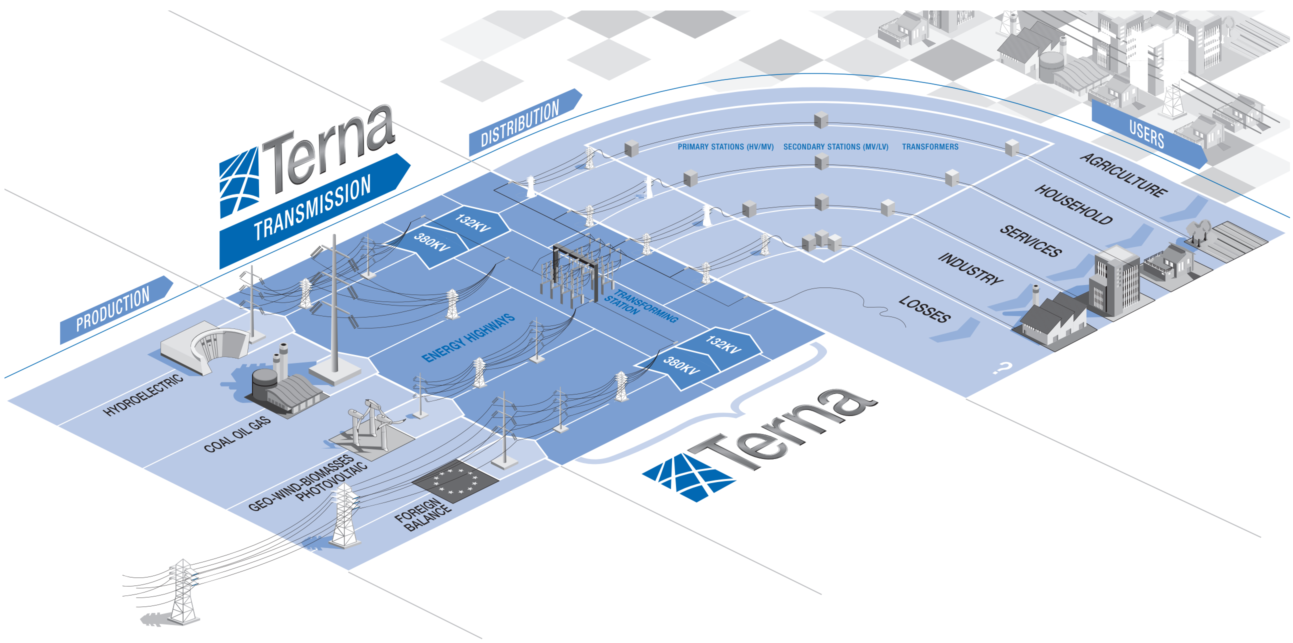
## Outlook

Financial year 2012 will see the Company committed to implementing the actions under the 2012-2016 business plan, approved by the Board of Directors on 20 March 2012, with total investments in line with the financial year just ended.
More specifically, the Group will be committed to completing the implementation of the new corporate and organisational structure more focused on non-core business.
With reference to the business plan, the Company will continue to develop and construct inter-connections with abroad (Montenegro and France), to reduce grid congestion and guarantee the connection of generation plants from renewable sources.
Additionally, in 2012, preliminary activities will be started connected with the development of the "accumulation systems" planned and presented in the business plan.
Revenue is expected to increase in relation to the regulated transmission fees associated with investments made in 2010 and impact of the recent review of the tariffs.
In continuity with previous years, the Company will pursue the rationalisation of processes and efficiency of operating expenses, at the same time ensuring maximum quality of the dispatching and transmission service.
With reference to financial management, the recent bond issue has guaranteed the resources usable for to the business activity until 2015.

# The business

## National Transmission Grid

The Italian electrical system chain consists of four segments: the production, transmission, distribution and sale of electricity. **In this chain, Terna's activities refer to the transmission of electricity on the high voltage grid**; in particular, the Group deals with the management of the electrical system through the operation of the grid, maximum efficiency of infrastructures and excellence of their maintenance through engineering and management of plants and grid development.




The main stages of the production process of the transmission service are as follows.

### Operation

In grid operation, it is essential **to ensure a balance of deliveries and withdrawals at all times**, i.e. between the supply of energy, produced domestically and imported, and consumption by end users. This function is called dispatching.
Preparation to operation in real time includes the **programming of unavailability** (of grid or production plants) with different time frames, the forecast domestic electricity demand, its comparison in coherence with the programme of production determined as the result of the free energy market (Power Exchange and off-Power Exchange contracts), the acquisition of resources for dispatching and the verification of transits of power for all transmission grid lines.
During the **real time control** stage, the national control centre, coordinating other centres on the territory, monitors the electrical system and carries out dispatching, intervening, where differences are seen in the structure forecast for production plant failures or grid elements failures or for a trend in demand that differs from forecasts, with commands to producers and remote operation centres, in order to modulate the supply and grid structure. To avoid the risk of grid degeneration and extensive power failures, it may intervene in an emergency, also to reduce the demand.

### Grid development planning

The analysis of electricity flows on the grid and the preparation of demand forecasts enable Terna to **identify the critical issues on the grid and the new works that need to be developed** in order that the suitability of the system is guaranteed with respect to the coverage of demand, operating security, the reduction of congestion and improved quality and continuity of service.
The new works to be developed are included in the Development Plan of the National Transmission Grid presented every year to the Ministry for Economic Development for approval; Terna then follows the authorisation process, from the prior agreement of local entities through to the authorisation to develop the works.
Finally, Terna develops, by means of an analysis of the grid situation, the **very best transmission grid connection methods** for all operators so requesting for their plants.

## Construction

Terna defines the engineering standards for the plants connected to the grid. More specifically, it defines the construction standards and performance required of equipment, machinery and components of long-distance power lines and stations. In terms of the construction of the plants, **Terna prepares projects for constructing the authorised works**. More specifically, it defines the need for external resources and the budget for the projects, establishing the working methods and technical specifications of components and materials to be used in the construction of new lines or stations, also adopting innovative methods.
New plant construction is generally outsourced.

## Maintenance

Terna **maintains long-distance power lines and stations** through eight Transmission Operative Areas by which most – just under 70% – of the Company's human resources are employed.

## Number of plants

The following table provides details about the number of Terna Group plants at 31 December 2011:

| | Terna Group | | |
|---|---|---|---|
| | 31.12.2011 | 31.12.2010 | Change |
| Stations | 454 | 431 | + 23 |
| Transformers | 643<br>126,765 MVA | 634<br>125,571 MVA | + 9<br>+ 1,194 MVA |
| Bays | 4,936 | 4,825 | + 111 |
| Lines | 57,651 km | 57,638 km | + 13 km |
| 3-phase power lines | 4,043<br>63,626 km | 3,981<br>63,578 km | + 62<br>+ 49 km |

## Number of plants - Terna

The number of plants of the Parent Company, Terna, at 31 December 2011, compared with the situation at 31 December 2010, is reported below:

| | Terna | | |
|---|---|---|---|
| | 31.12.2011 | 31.12.2010 | Change |
| Stations | 435 | 412 | + 23 |
| Transformers | 636<br>126,303 MVA | 632<br>125,251 MVA | + 4<br>+ 1,052 MVA |
| Bays | 4,846 | 4,706 | + 140 |
| Lines | 41,121 km | 40,805 km | + 316 km |
| 3-phase power lines | 2,312<br>46,069 km | 2,247<br>45,707 km | + 65<br>+ 362 km |

## Stations

In relation to stations, please note the activation of 23 new stations:
- 6 at 380 kV: Maleo (LO), Chignolo Po (PV), Le Rose (FI), Aprilia (LT), Deliceto (FG) and Troia (FG);
- 3 at 220 kV: Salvemini (TO), Gerbido (TO) and Turin North (TO);
- 15 at 132-150 kV: Lovero (SO), Olevano Lomellina (PV), Merate (LC), Canaro (RO), Populonia (LI), Sant'Alberto (RA), Alfonsine (RA), San Vittore (FR), San Martino in Pensilis (CB), Ginestra degli Schiavoni (BN), Castelpagano (BN), Marianopoli (CL), Cammarata (AG), Patti (ME) and Serramanna (VS);
- disposal of the 132 kV station of Contarina (RO).

## Transformers

In relation to transformers, an increase by 4 units is noted compared to 31 December 2010, with an increase in total transformation capacity in operation of 1,052 MVA; more specifically, please note the activation of:

- new 220 kV phase shifting transformer of 450 MVA in Camporosso station;
- 5 new 380/150 kV machines (for a total of 1,250 MVA) in the stations of Deliceto, Troia and South Brindisi;
- 2 new 380/132 kV machines (for a total of 500 MVA) in the stations of Maleo and Flero;
- the two existing 220/132 kV machines (for a total of 267 MVA) were strengthened with the addition of two new machines (for a total of 410 MVA) in the stations of Bussolengo San Salvar and Castelbello;

net of disconnection from the grid of 2 380/220 kV machines (for a total of 800 MVA) in the station of Poggio in Caiano and the disposal of 6 220/132 kV machines (for a total 488 MVA) in the stations of Este, Tavarnuzze, Tavazzano West, Colà and Marghera Station 1.

## Long-distance power lines

In relation to long-distance power lines, the total length of the three-phase line has increased by 362 km as compared with 31 December 2010, whilst that of the power lines by 316 km; more specifically, please note that in addition to the acquisition from Terna Rete Italia of 25 lines for a total of 279.8 km, there was the entry into operation of 5 new lines for a total of 62.7 km: Chignolo Po-Maleo 380 kV, Gerbido-Salvemini 220 kV, Salvemini-Turin West 220 kV, Villa di Tirano-Lovero 132 kV.

## Number of plants - Terna Rete Italia

The number of plants of the company Terna Rete Italia, at 31 December 2011, compared with the situation at 31 December 2010, is reported below:

| | Terna Rete Italia | | |
|---|---|---|---|
| | 31.12.2011 | 31.12.2010 | Change |
| Stations | 19 | 19 | - |
| Transformers | 2<br>320 MVA | 2<br>320 MVA | -<br>- |
| Bays | 81 | 119 | - 38 |
| Lines | 16,528 km | 16,833 km | - 305 km |
| 3-phase power lines | 1,728<br>17,556 km | 1,734<br>17,871 km | - 6<br>- 314 km |

The change in the number of plants of Terna Rete Italia for the most part refers to the category of **long-distance power lines** and mainly derives from the combined effect of the following factors:

- sale to Terna of 25 lines for a total of 279.8 km;
- modifications, rigid derivations and/or changes in the line with a total reduction of 6.2 km of the three-phase circuit;
- disposal and/or joining of operating lines with a total decrease to 3 three-phase power lines for a total of 43.2 km;
- partial restructuring of the grid south of Naples, with a total decrease to 1 three-phase line and 20.6 km;
- entry into operation of 4 new lines for a total of 5.9 km: Torre Centrale-Torre Nord 150 kV, Siniscola 2-Buzzi Unicem 150 kV, Sarroch-Air Liquide 150 kV, CP Imperia-Imperia RFI 132 kV;
- development of 16 incoming-outgoing derivations on the same number of operating lines with a total increase of the same number of three-phase lines and 6.9 km.

## Number of plants - SunTergrid

The number of plants of SunTergrid at 31 December 2011 is given in the table below:

| | SunTergrid 31.12.2011 |
|---|---|
| Stations | - |
| Transformers | 5<br>143 MVA |
| Bays | 9 |
| Lines | 1.4 km |
| 3-phase power lines | 3<br>1.4 km |

The number of plants of SunTergrid is specifically represented by photovoltaic production connection plants:

- Lanuvio and Torretta (2 150 kV bays and 1 150 kV / MV transformers, each 25 MVA);
- Galatina West (2 150 kV bays and 1 150 kV / MV transformer of 16 MVA);
- Cancarro (2 150 kV bays and 1 150 kV / MV transformer of 14 MVA);
- Alfonsine 2 (1 132 kV bay and 1 132 kV / MV transformer of 63 MVA).

Please also note 3 short cable lines of 150 kV creating the connections between Cancarro-Troia, Galatina West-Galatina and Torretta-Deliceto.

## National Transmission Grid Development Plan

On 28 January 2011, as required by Ministerial Decree of 20 April 2005, the 2011 Development Plan was sent to the competent Authorities for approval.
The same Development Plan (DP 2011) was approved by Terna Board of Directors on 16 December 2010, having already been favourably received by the Users' Advisory Committee (11) (which on 4 November approved the new development initiatives included in the Plan and on 15 December 2010 approved the Plan in its entirety).
The latest version of the Development Plan takes account of the instructions that the Ministry for Economic Development attached to its final resolution of the 2010 Development Plan (12).
The 2011 Development Plan adopts the structure of the previous year's version and is divided into two sections: 2011 Development Plan - Section I, contains the new development demands seen in 2010 (this section, in accordance with Italian Legislative Decree no. 152/06, is subject to Strategic Environmental Assessment which began on 18 October 2010); Progress on Previous Plans - Section II where the progress made on the interventions envisaged by previous Development Plans, already approved and confirmed in this Plan, is explained.
In particular, the first section contains a specific paragraph devoted to the grid development to encourage production from renewable sources (in accordance with the National Plan of Action) and the expansion of the European grid.
The ten-year Development Plan of the European electricity grids (TYNDP, 2010 edition) was prepared as part of the ENTSO-E project in which Terna is directly involved in the following Regional Forums: Continental Central South (for which Terna is coordinator and member) and Continental South East (member only). 2012 will see the publication of the TYNDP, 2012 edition, complete with the Regional Investment Plans and the document on the suitability of the European electricity grid, in addition to the "pilot" edition of the European Network Code, according to that established in the European Community Regulation in relation to the "Third Energy Package".
The 2011 Development Plan envisages investments of around €3.8 billion in the period 2011-2015 and €3.7 billion in the five years thereafter. The implementation of the Development Plan will increase the size of the NTG by adding around 5,400 km of new lines and 141 new stations with a transformation capacity of around 44,800 MVA.



(11) The Users' Consultative Committee, established by Prime Minister Decree of 11 May 2004, expresses a non-binding opinion on the Development Plan as required by Competition Authority Decision no. 14542 of 4 August 2005.
(12) On 15 March 2011, the Ministry for Economic Development approved the 2010 Development Plan pursuant to Legislative Decree no. 152 of 3 April 2006, and subsequent amendments and additions, publishing its final decision in Italian Official Gazette no. 62 of 16 March 2011.

### Supplementary document to the 2011 Development Plan

On 1 July 2011, the Ministry for Economic Development was sent the supplementary document to the 2011 Development Plan in relation to the diffused electricity accumulation systems drawn up in accordance with Italian Legislative Decree no. 28 of 3 March 2011, which establishes that the interventions envisaged by Terna may include diffused accumulation systems of electricity with a view to facilitating the dispatching of non-programmable plants.
This document describes the reference framework, the forecasting scenarios and the new development demands, with particular attention paid to the installation of diffused accumulation systems able to provide maximum input to the system security and the reduction of congestion on the portions of grid to which the non-programmable renewable sources refer, with specific reference to the critical issues seen on the portions of grid most affected by the repeated development of the non-programmable renewable sources and the potential critical issues that may involve specific portions of grid in the short and medium term.
The supplementary document to the 2011 Development Plan forecasts investments for approximately €0.4 billion.

### Strategic Environmental Assessment of 2011 Development Plan

The consultation phase of the Development Plan and preparation of the related Environmental Report commenced on 18 March 2011.
On 1 October 2011, the Ministry for Economic Development began consultation on the "2011 Development Plan - Supplementary document in relation to the diffused accumulation systems of electricity".
The process for obtaining approval from the Ministry for Economic Development requires the release of a reasoned SEA opinion from the Ministry for the Environment together with the Ministry for Culture. As soon as final approval is given, the Ministry for Economic Development must also issue a Summary Statement outlining whether and how it intends to act on any comments that may have been included in the reasoned opinion from the Ministry for the Environment.

### Work carried out in period

The most important work – still in progress – carried out during 2011 involved activities to reduce network congestion, connect new generating plants (especially those using renewable energy sources) and increase the reliability of the NTG with ever greater attention to environmental and security issues.
Below is a summary of the main works in progress and the main work concluded in 2011:

- new 380 kV "Sorgente-Rizziconi" underwater connection: work sites have been opened and the civil works involved for the stations of Scilla (Calabria) and Sorgente (Sicily) are at an advanced stage; site work has begun and the site is being organised for the station of Villafranca (Sicily). The works relating to the three 380 kV stations specified above are at an advanced stage. For Scilla in particular, electro-mechanical and electrical assembly are at an advanced stage, whilst at the 380 kV power station of Rizziconi expansion works are underway. The first of the six underwater cables between Villafranca and Favazzina has been installed for the construction of the 380 kV connection in double three-phase line. Preliminary works have been completed on the construction of the Favazzina tunnel. Construction of the 380 kV long-distance power lines (overhead part), Calabria side, are at an advanced stage.
- 380 kV stations to connect renewable-resource fuelled plants: from 2009 to 2010, sites were opened in relation to 380 kV stations functional to reducing congestion and the connection of new production plants from a renewable source in the areas of Maida, Bisaccia, Deliceto, Troia, Brindisi South, Castellaneta, Tuscania and Rotello. In 2010, works were concluded in the stations of Maida and Bisaccia. In 2011, works were completed in the stations of Deliceto and Troia and the second stage of the Brindisi South station was activated.
- 380 kV rationalisation in the province of Lodi: two new 380 kV electrical stations were started-up in Chignolo Po and Maleo and the new double three-phase line connection between the stations was constructed.
- Val D'Ossola South-cavi di Borgomanero: microtunnelling, the installation of cables and accessories for both lines were completed.
- Construction works have begun on the new 380 kV double three-phase electric main joining the 380 kV stations of Trino in the province of Vercelli and Lacchiarella in the province of Milan, measuring more than 100 km in length.
- Installation is currently underway of two PST (System Phase Shifter) machines, one in the electrical station of Foggia and the other in Villanova.

# Power generation

## Energy demand in Italy

According to provisional data, the demand for electricity during 2011 amounted to 332,274 GWh, up by 0.6% with respect to 2010 (see the table below).
Comparison of the results for 2011 with the data for the prior year, leaving constant the number of days and the temperature, involves considering two separate factors. First and foremost, the different calendar that caused 2011 to record 252 working days, three fewer than 2010. As concerns atmospheric temperatures, vice versa, in the two years compared, similar climate conditions were recorded in the respective 12-month periods. In conclusion, taking account of the number of days and temperature, the change in electricity demand amounted to +0.9%.

ENERGY BALANCE IN ITALY

| | Balance | | | |
|---|---|---|---|---|
| GWh | 2011 (*) | 2010 | Change | % |
| Net production | 289,166 | 290,748 | (1,582) | (0.5%) |
| Imports | 47,349 | 45,987 | 1,362 | 3.0% |
| Exports | 1,723 | 1,827 | (104) | (5.7%) |
| Pumping | 2,518 | 4,454 | (1,936) | (43.5%) |
| **Total demand** | **332,274** | **330,455** | **1,819** | **0.6%** |

(*) Provisional data as of 23.01.2012.

## Electricity generation

According to initial estimates, in 2011 net domestic power generation (see table below) decreased slightly by 0.5% year on year. Analysing the various main sources of energy, net of ancillary services, thermal generation showed a 1.6% drop in 2011 compared with 2010.
In 2011, hydroelectric production reduced sharply with regard to 2010, recording a decrease of 11.4%, net of consumption for auxiliary services.
Once again, the net production from wind, solar and geothermal energy soared strongly in 2011 compared with the previous year, climbing by 51.1% overall.

DOMESTIC POWER GENERATION

| | Production | | | |
|---|---|---|---|---|
| GWh | 2011 (*) | 2010 | Change | % |
| Net hydro generation | 47,672 | 53,795 | (6,123) | (11.4%) |
| Net thermal generation | 217,369 | 220,984 | (3,615) | (1.6%) |
| Net geothermal generation | 5,307 | 5,047 | 261 | 5.2% |
| Net wind generation | 9,560 | 9,048 | 512 | 5.7% |
| Net photovoltaic generation | 9,258 | 1,874 | 7,384 | 393.9% |
| **Total net generation** | **289,166** | **290,748** | **(1,582)** | **(0.5%)** |

(*) Provisional data as of 23.01.2012.

# Dispatching and trade

## Electricity business

Based on operating figures, Italian electricity demand for 2011 came to 332,274 GWh, a rise of 0.6% on the previous year. The demand for electricity has been met as reported in the table below.

- 86.3% (86.6% in 2010) from domestic production, where the term domestic production is used for production net of consumption of auxiliary services and pumping.
- 13.7% (13.4% in 2010) from foreign trade, amounting to 45,626 GWh (44,160 GWh in 2010). Foreign trade is calculated as the difference between energy received from foreign suppliers and energy sold to foreign customers, which recorded an increase of 3.3%.

ENERGY BALANCE IN ITALY

| GWh | Jan-Dec 2011 (*) | Jan-Dec 2010 | Change | % |
|---|---|---|---|---|
| Net production | 289,166 | 290,748 | (1,582) | (0.5%) |
| Imports | 47,349 | 45,987 | 1,362 | 3.0% |
| Exports | 1,723 | 1,827 | (104) | (5.7%) |
| Pumping | 2,518 | 4,453 | (1,935) | (43.5%) |
| **Total demand** | **332,274** | **330,455** | **1,819** | **0.6%** |

(*) Figures for the financial year.

Net production was met by means of the plant types described below.

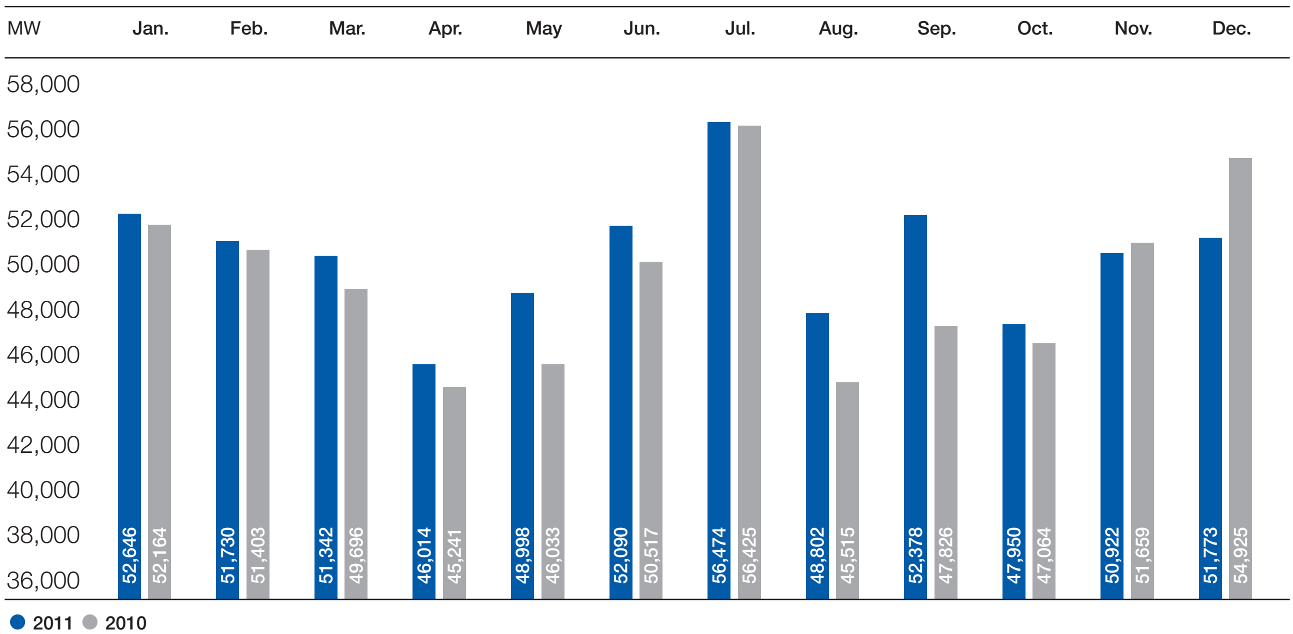
DOMESTIC POWER GENERATION

| GWh | Jan-Dec 2011 (*) | Jan-Dec 2010 | Change | % |
|---|---|---|---|---|
| Net hydro generation | 47,672 | 53,795 | (6,123) | (11.4%) |
| Net thermal generation | 217,369 | 220,984 | (3,615) | (1.6%) |
| Net geothermal generation | 5,307 | 5,047 | 260 | 5.2% |
| Net wind and photovoltaic generation | 18,818 | 10,922 | 7,896 | 72.3% |
| **Total net generation** | **289,166** | **290,748** | **(1,582)** | **(0.5%)** |

(*) Figures for the financial year.

The maximum power demand recorded in 2011 amounted to 56,474 MW (13 July 2011 at 12.00 pm) and is comparable (+0.1%) with the maximum value recorded in 2010 of 56,425 MW (16 July 2010 at 12.00 pm).
The maximum power demand recorded in each month of 2011 exceeded that of the months of the previous year, with the exception of November and December.

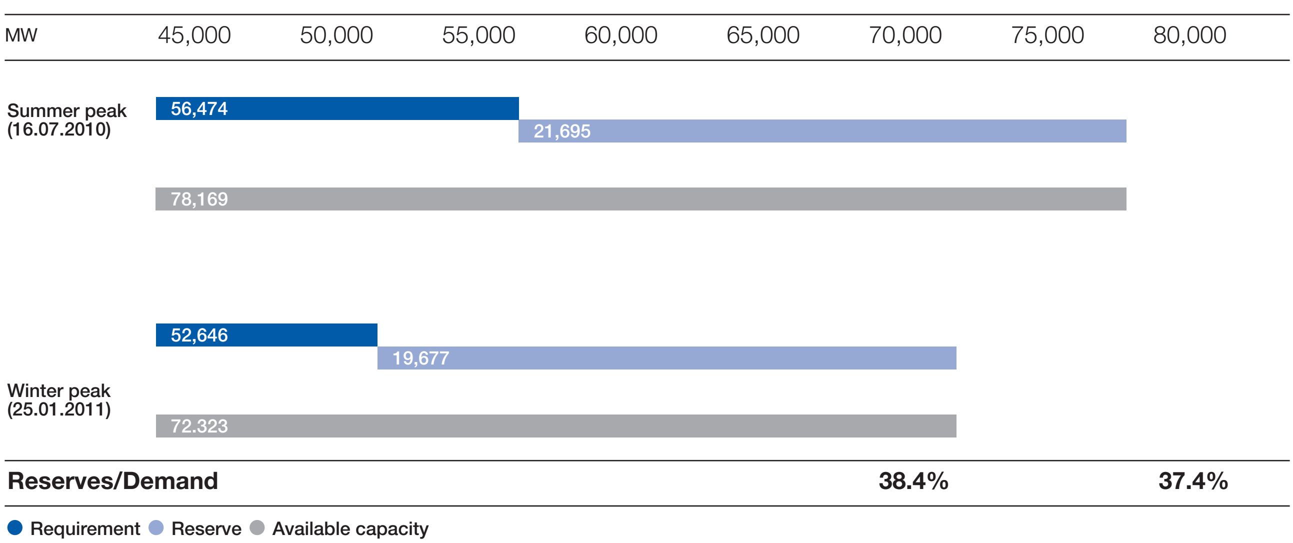
MAXIMUM POWER VALUES




## Coverage of demand

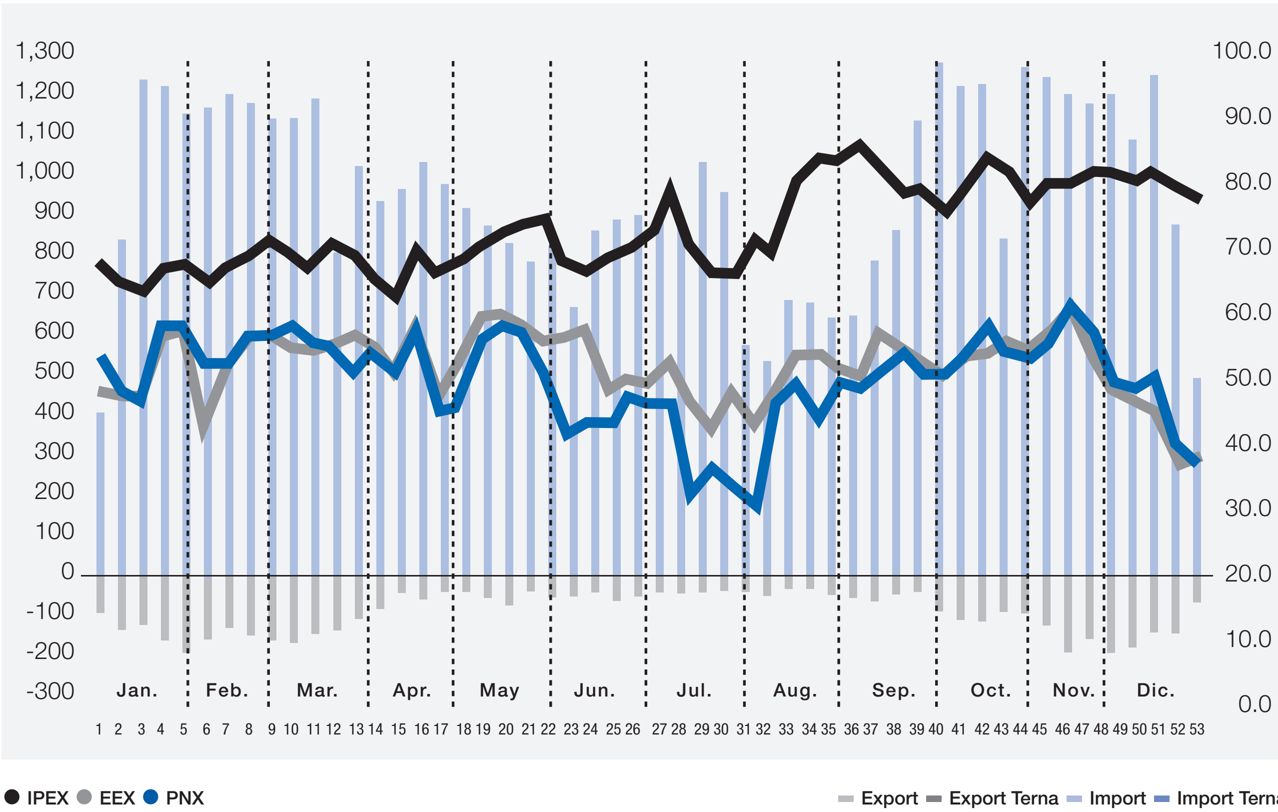
Coverage of power demands in 2011 was guaranteed with suitable margins, by means of scheduled maintenance work on the grid and by coordinating maintenance with the unavailability of power generation from Terna and also following the entry into operation of new generation plants, also distributed.

RESERVE MARGINS AT PEAK




In Sardinia, the demand coverage margins increased thanks to the doubling of the submarine connection between the mainland and Sardinia (SA.PE.I.)
In Sicily, demand coverage margins were found to be adequate, with 329 hours per year also using the Termini Imerese 4 plant (production unit normally unused, whose production can be requested by Terna in the event the security of the grid in Sicily is expected to be at risk).

Foreign trade showed an increase in import as compared with the previous year of approximately 1.1 TWh. This is also due to the 23% increase in the difference between the energy price of the Italian energy market and that of French and German markets (€22/MWh vs. €18/MWh).




## Provisioning of dispatching resources

The reform of the Market for Dispatching Services, which had begun in 2010 in accordance with Italian Law no. 2/2009, with a view to increasing the efficiency of the power market, continued in 2011 with the updating of the rules for dispatching and the introduction of the following news.

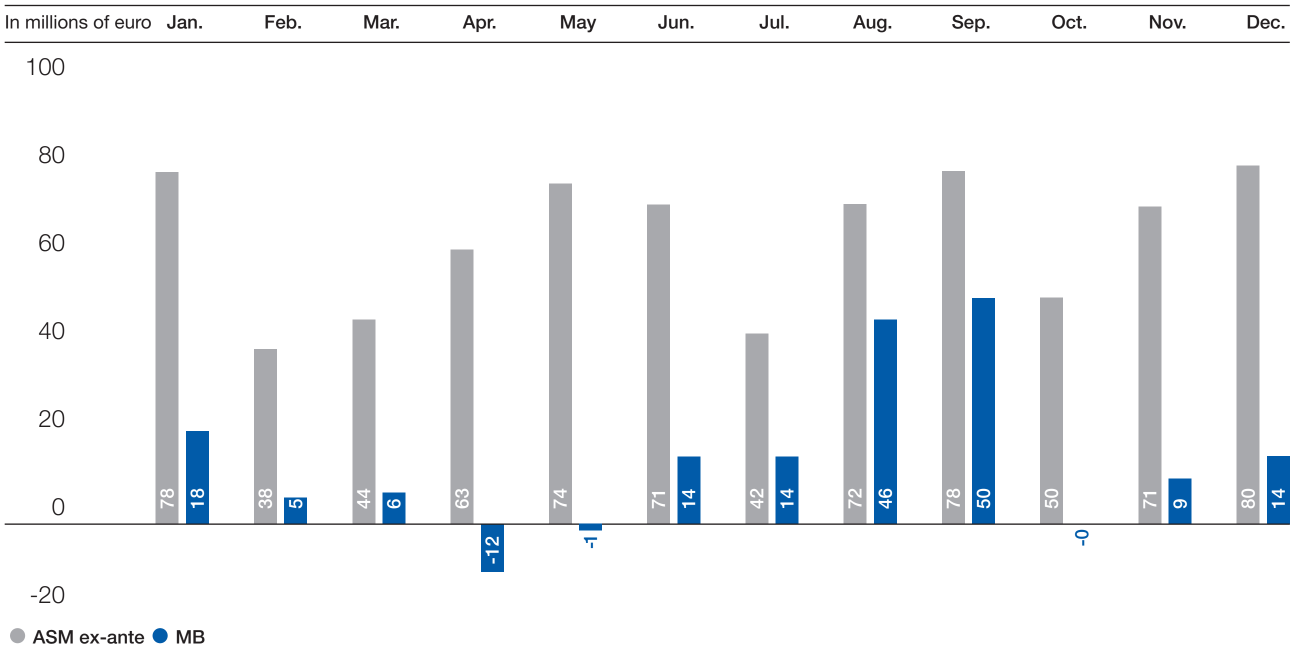
- Introduction of power market sessions on the flow day, to which the reductions refer (the "Infra-day market").
- Introduction of new Market for Dispatching Services sessions on the flow day, to verify the meeting of the demand for dispatching services following infra-day market sessions.
- Elimination of revocations between stages of the Market for Dispatching Services, pursuant to AEEG Resolution no. 165/05, whereby actions prepared by Terna on the Market for Dispatching Services during programming (the "ex-ante Market for Dispatching Services") and cancelled prior to execution on the Balancing Market (the "MB"), the costs of which were compensated, instead become actions at the expense of the system. The elimination of the revocations has entailed the preparation in protection of the suitability and security of the system at a minimum advance, on the basis of forecasting as closely as possible to implementation and therefore less uncertain.
- Offer structure on the Market for Dispatching Services that is more cost-reflective of production costs with the introduction of the start-up token remunerating the start-up costs of thermoelectric plants of a type other than open cycle turbogas.

Given the alterations to the energy regulatory framework for 2011, the dispatching process and the methods and instruments in support of it have been modified, also to the benefit of the efficiency of procurement on the Market for Dispatching Services.

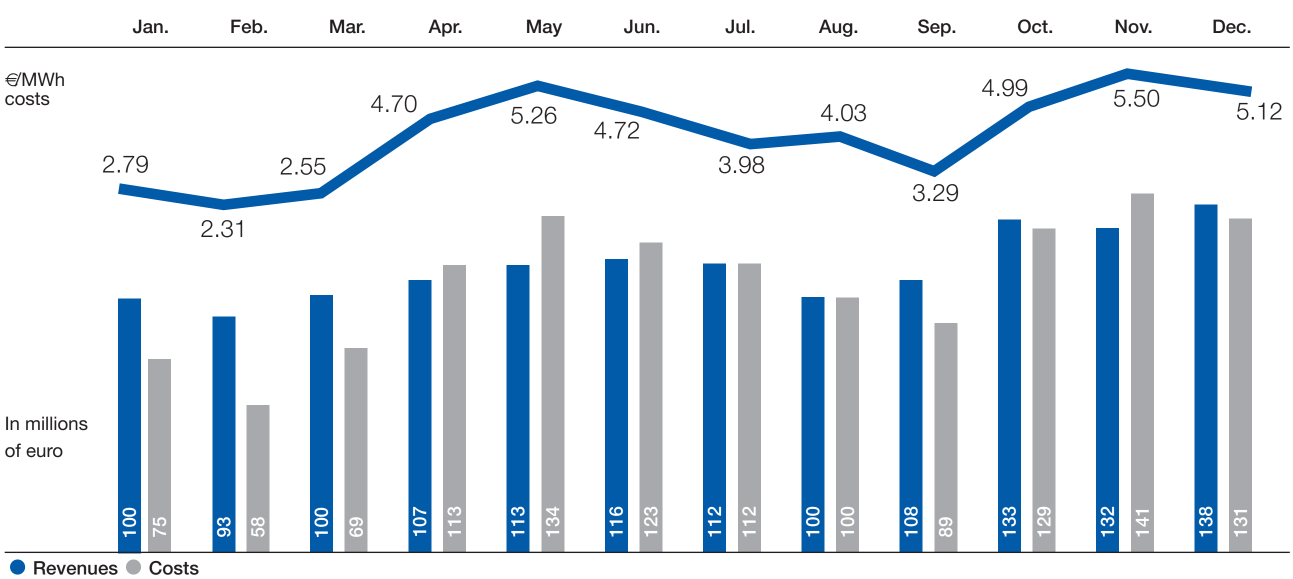
In 2011, Terna procured resources on the Market for Dispatching Services, purchasing and selling energy for 8.6 TWh (-38% yoy) and 17.2 TWh (-25% yoy) respectively for a total net expense amounting to €923 million (-27% yoy).

Volumes and expenses were divided up as follows between the Market for Dispatching Services stages:

- ex-ante Market for Dispatching Services, purchases and sales for 4.7 TWh and 4.9 TWh with a total net outlay amounting to €761 million;
- MB, purchases and sales for 3.9 TWh and 12.3 TWh with an outlay amounting to €162 million.




The net expense resulting from the purchases and sales on the Market for Dispatching Services, from the valuation of the imbalances and the balance of other energy items, is billed on a pro-rata basis to users of the dispatching services (withdrawals) with the uplift fee in relation to the procurement of resources on the Market for Dispatching Services, as per Art. 44 of Resolution no. 111/06 as subsequently amended.




The uplift fee is calculated considering the following elements: balance of other energy items such as the transmission capacity usage fee (the "CCT"), the contracts hedging the risk of volatility of the fee for the assignment of the rights of use of transmission capacity (the so-called "CCC" and "CCP"), the right of transmission of use of transmission capacity on foreign interconnectors (the "DCT"), the virtual importation service (interconnectors and shippers), and the difference between actual, estimated and billed uplift fees for each quarter.

## Interconnectors and shippers

In accordance with Law 99/2009 and Resolution ARG/elt 179/09, Terna selects the parties willing to finance the interconnection infrastructure with abroad in the form of interconnectors and derives the economic benefits from the importation of energy from abroad via assignment of the virtual importation service (shipping) on a tender basis.

In December 2011, Terna assigned the virtual importation service for 2012 for a total capacity amounting to 2,431 MW, divided as follows between cross-border countries:

- 2,342 MW France (26 parties selected);
- 89 MW Germany (9 parties selected).

| | France 2011 | Germany 2011 | France 2012 | Germany 2012 |
|---|---|---|---|---|
| Number of shippers (no.) | 7 | 21 | 26 | 9 |
| Capacity assigned (MW) | 27 | 2,455 | 2,342 | 89 |

### Interruptibility service

By Resolution ARG/elt 187/10 (subsequently amended by Resolution ARG/elt 212/10) and the Regulation for the management of the assignment of the interruptibility service prepared with reference to the three-year period 2011-2013, Terna assigns the interruptibility service by means of tenders:

- on a quarterly basis, for the instantaneous and emergency interruptibility service and for any non-assigned power. The interruptibility service assigned runs from the first day of the month after that of assignment, up to 31 December 2013;
- on a monthly basis, for the instantaneous and emergency interruptibility service and for any available power on a monthly basis, following the release of power by assignees or following the termination of contracts. The duration of the assignment is monthly. The assignments are made the month prior to the starting date of the assignment.

In December 2011, Terna assigned:

- power for the instantaneous interruptibility service amounting to 3,791 MW (of which 212 MW assigned on a monthly basis) with an annual price amounting to €150,000/MW;
- power for the emergency interruptibility service amounting to 20 MW (of which 1 MW assigned on a monthly basis) with an annual price amounting to €100,000/MW.

| | Interruptible customers at 01.01.2011 | Interruptible customers at 31.12.2011 | Contractually-agreed power at 01.01.2011 | Contractually-agreed power at 31.12.2011 |
|---|---|---|---|---|
| Instantaneous | 144 | 156 | 3,430 | 3,791 |
| Emergency | 4 | 4 | 25 | 20 |
| **Total** | **148** | **160** | **3,455** | **3,811** |

### Instant reduction service in withdrawals on the major islands

In application of Resolution ARG/elt 15/10 (subsequently amended by Resolution ARG/elt 75/10) and the Regulation for the management of the assignment of the instantaneous reduction service in withdrawals in the major islands prepared for the three-year period 2010-2012, Terna assigns, on a quarterly basis, the interruptibility service in Sardinia and in Sicily for a power of up to 500 MW. The service assigned runs from the first day of the month after that of assignment, up to 31 December 2012.

In 2011, Terna assigned:

- 10 MW in Sardinia and 14 MW in Sicily for the period running from 1 September 2011 to 31 December 2012;
- 6 MW in Sicily for the period running from 1 December 2011 to 31 December 2012.

The table below shows the movement in the power assigned under contract throughout 2011 for the instantaneous reduction service in withdrawals.

| | Customers with instantaneous reduction service withdrawals at 01.01.2011 | Customers with instantaneous reduction service withdrawals at 31.12.2011 | Contractually-agreed power at 01.01.2011 | Contractually-agreed power at 31.12.2011 |
|---|---|---|---|---|
| Sardinia | 7 | 9 | 375 | 473 |
| Sicily | 4 | 10 | 24 | 78 |
| **Total** | **11** | **18** (*) | **399** | **551** |

(*) One customer has contracts with reference to both the major islands.

### Service quality and unsupplied energy

Transmission service quality in 2011 recorded figures for Regulated Energy Not Supplied (RENS) and the Number of Supply Failures per User (NSFU) in line with last year, specifically: RENS of 1,210 MWh vs. quality target of 1,369 MWh and NSFU of 0.179 vs. quality target of 0.209.
The events that resulted in user power failures can be traced to accidents and failures not related to the procurement of dispatching resources.
Please refer to the "2010 Annual report" published on the Terna website in the section "Electrical system/Transmission service quality" for further details.
Finally, below are the reference indexes for the "quality of service and conduct of Terna NTG plants" pursuant to AEEG Resolution no. 250/04 and the Terna Network Code, which, in 2011, were above or in any case comparable with their respective targets.

- AIT (Average Interrupt Time attributable to Terna) = 0.49 min/year with target = 1.00 min/year;
- SAIFI + MAIFI (System and Momentary Average Interruption Frequency indexes per user directly connected to the Terna NTG, attributable to Terna) = 0.14; target = 0.22;
- ENS (Energy not supplied attributable to Terna) = 306 MWh; target = 550 MWh;
- ASA (Average System Availability of Terna network elements) = 99.32%; target = 99.05%.

## Terna and the new businesses

In order to use and safeguard its resources as far as possible and maximise the profitability of its assets, towards the end of 2011, Terna started a reorganisation of its operating assets with aims to group non-regulated activities into a single entity with a view to taking development opportunities in the best possible way.
With this goal in mind, Terna has incorporated the company Terna Plus that endowed with a corporate organisation which meets the needs of functional and accounting separation from the Parent Company and ensures compatibility with the Articles of Association and the concession of Terna S.p.A., and complies with the provisions of Legislative Decree no. 79/99 (the "Bersani Decree").
The development of non-core business will pursue the objective of enhancing further the assets held and Terna's distinctive competences in the construction and management of infrastructures, in particular high voltage, in Italy and abroad.
Products held in the portfolio include the construction and long-term management of non-NTG electrical assets functional to the connection of production plants from renewable sources to the electricity grids, the support to the operation and maintenance of renewable source production plants and the development and management of optic fibre grids.

# Risks, organisation and corporate social responsibility

## Risks and uncertainties to which Terna and the Group are exposed

Terna has always paid careful attention to the prevention of risks of all natures that could affect or limit the company's results. This section aims to provide a clearer, more complete representation of these risks which are summarised along with the uncertainties to which the company is exposed, as indeed known to the market and shareholders, considering their presentation in the financial statements and financial prospectuses published in the past.

### Regulatory risk

About 96% of the Group's consolidated revenue comes from annual fees paid for the provision of services regulated by the Italian Energy Authority. By Resolutions nos. 199/11, 204/11 and 197/11 for the regulatory period 2012-2015, the Authority for Electricity and Gas (AEEG) has established remuneration for the supply of electricity transmission, distribution and metering services, prices for dispatching and the regulation of the quality of the transmission service for the fourth regulatory period (2012-2015), in addition to the ways in which they are updated in subsequent years.
Within the scope of such regulations, there are a number of variables that could have an impact on performance.

#### Volume effect

The revenue of Terna and Terna Rete Italia attributable to the operation, functioning and development of the National Transmission Grid, and to the management of dispatching activities, are regulated by tariffs set by the AEEG. The unit tariffs are applied to the overall volume of energy transmitted using the NTG. These volumes depend on factors that are beyond the control of the Group.
For 2012, the volume mitigation mechanism still applies; according to this mechanism no impact is expected from the trend of electricity demand on the Company's revenue that is limited within a range of +/-0.5%. As from 2013, with a view to stabilising revenue flows, reducing volatility connected with energy volumes, the tariff becomes binomial and will be calculated on both the net energy taken from the NTG and on the power available on interconnection points. Although this is considered to be less subject to the fluctuations in energy demand with an overall improvement for Terna we cannot be certain that revenue flows will be stabilised, given that no historical data is available on the power available on interconnection points.

#### Bonuses and penalties

At present, a mechanism is also in place for the calculation of bonuses and penalties on the quality of the transmission service together with a three-year incentive mechanism linked to the reduction of the quantities provisioned on the Market for Dispatching Services, as extensively described in the 2010 Annual report, to which we would refer.
**Resolution 197/11** on the regulation of the **quality of service** confirms the framework of the previous regulatory period, based on a premium/penalty mechanism. Grid availability is now only monitored by the energy not supplied index. With this mechanism, the maximum potential impact is estimated for the Terna Group as ranging between -€12/+€30 million per year.
Resolution 199/11 sets the eligibility for investments under category I3, for which an extra remuneration of 2% is envisaged for 12 years, provided that Terna conforms to the incentive system to accelerate the development of investments and the related premium/penalty mechanism. The risk for Terna deriving from said adhesion is linked to the potential penalties deriving from delays in the date of entry into operation of I3 investments with respect to the expected date.

### Domestic legislative risk

#### Laws on environmental protection

The activities of the Group are conditioned by the Italian and European environmental legislation also governing electromagnetic fields. The Group may incur additional costs to implement environmental regulations requiring preventive measures to be taken or reparations to be made on the basis of the definition of the regulation established by current legislation.

#### Laws on employment

More onerous regulations governing health and safety in the workplace might have an adverse effect on the economic/financial performance of the Group. Throughout the European Community, a review has begun of the Directive on worker exposure to electromagnetic fields.

#### Laws on the consolidated energy market

Adoption is envisaged of provisions concerning the electricity sector in implementation of Italian Legislative Decree no. 93/11 on the single market of electricity.

### Operational risks: risks connected with NTG malfunction

The Terna Group's operations are exposed to the risk of unexpected service interruptions caused by external events that are beyond Terna's control, such as accidents, defects or breakdowns involving control systems or other equipment, deteriorating plant performance, natural disasters, terrorist attacks and other extraordinary events of this kind. Repairs to the sections of the NTG owned by the Group and any claims for compensation by third parties as a result of such events could, in principle, give rise to charges if the Group is found be responsible. Specific insurance cover has been arranged to mitigate the effect of operational risks.

### Litigation risk

The Terna Group is involved, as both plaintiff and defendant, in a number of legal proceedings involving contracts, employees, the environment, regulatory matters, and public safety issues arising from normal business operations.
In addition, the Group may be involved in new litigation and/or out-of-court disputes raised by interested/entitled parties of various types (by mere and incomplete way of example: suppliers, public entities, etc.)
On this matter, please refer to paragraph "E. Commitments and risks" of the Notes to the financial statements of Terna S.p.A. and the Terna Group.

### Market and financial risks

During the financial year, in going about its business, the Group is exposed to various different financial risks: market risk (namely interest rate risk and inflation risk), liquidity risk and credit risk.
As part of the policies approved by the Board of Directors, the Terna Group has defined responsibilities and operational procedures for the management of financial risk, making specific reference to the tools considered acceptable and setting clear operating limits for their use.
Terna's risk management policies seek to identify and analyse the risks the Company is exposed to, establishing appropriate limits and controls and monitoring risks and compliance with such limits. These policies and related systems are reviewed on a regular basis in order to reflect any changes in market conditions and the activities of the Group.
On this matter, please refer to section "E. Commitments and risks" of the Notes to the financial statements of Terna S.p.A. and the Terna Group for more details.

### Risks connected with financing needs

Even in current market conditions, the Group expects to maintain sufficient capacity to generate financial resources from its operating activities. However, the plan for future investments should lead to an increase in debt. Although the Group continues to enjoy the support of its banking partners for the financing of its debt, it may become necessary to arrange additional loans that, under less favourable market conditions, could result in an increase in financial expense.

### Risk on non-core business in the sector of renewables

A significant part of non-core business is connected with the opportunities offered on the market of the construction and management of high voltage plants functional to the connection of production from renewable sources. Any changes to the legislative or regulatory framework may, moreover, determine a lesser appeal for investment in this sector in Italy and, consequently, a drop in the market opportunity for Terna's non-core business.

## Security

Terna has always tackled the vulnerabilities of the electrical system and critical infrastructure by applying the latest solutions and a high level of technical and organisational skills, which are reflected in the internal processes and systems, as well as in the procedures and instructions applicable to all operators participating in Italy's National Electrical System.
In order to meet the increasing need for security, Terna set itself the goal of significantly enhancing the organisation's security mechanisms and defining a broad-based system for identifying, analysing and monitoring Company risks.
In particular, security efforts are aimed at protecting the Company's physical and technological infrastructures, in part through efforts aimed at preventing and handling corporate fraud. For the real-time monitoring and management of critical issues affecting critical infrastructures, Terna has created a Security Operations Centre (SOC) that is able to tackle and manage critical situations.
Terna's security unit adopts the latest best practices in the areas of critical infrastructure protection and security, which are also in line with the current regulatory framework recently introduced in Europe.

## Security Operations Centre

In 2011, the number of operative company sites monitored for break-ins and by video-surveillance systems increased significantly, thus now covering most of the most sensitive sites as specified in the agreement with the Ministry of Interior. In addition to these, we also have the areas involved by sites, which are monitored by systems that can be relocated, also referred to as VideoBoxes.
In particular, jointly with the Carabinieri police force, the portal "Terna - Control Centre Carabinieri" has been improved to allow for the complete integration of the Terna control centre and that of the Carabinieri.
Through this portal, information, images and videos can be exchanged in real time between the control room and the Carabinieri patrol, equipped with "EVA" devices, sending the records from the monitoring room of the control centre, or the data collected on field by the patrols, thereby allowing for a rapid exchange of information in the event of a break-in.
With regard to the monitoring of information security, in 2011 company ICT resources were integrated further (servers, management platforms, etc.) onto the Security Information and Event Management system devoted to monitoring and relating security events on ICT resources. More specifically, 2011 saw the start-up of the Information Security Incidents Management process, in compliance with international standards such as ISO 27001.
The office of company Registration Authority was also consolidated, through which security services are supplied such as the issue of electronic signature digital certificates via the company platform, digital signature services and certified e-mail, with the use of systems external to the company (Infocert) in addition to services managing applicative qualifications.
These services are in addition to the now consolidated monitoring of spam and viruses on company resources. More specifically, in 2011 it was possible to introduce the new technique for managing e-mail spam. This technique has enabled the management and control of approximately 25 million spam e-mails addressed to Terna e-mail domains.

## Risk Management

### Electricity market risk management

In order to analyse the main risks relating to the electricity market, Terna uses an application called SIMM (Security Index Market Monitor), which represents the key performance indicators (KPIs) that allow us to have an overview of the high level of the trend of the electricity market and to readily identify any differences from the threshold limits established in order to analyse potential critical issues and risks.
Additionally, with its Resolution no. 115/08 ("TIMM") regarding the monitoring of the Wholesale Energy and Market for Dispatching Services, the Authority for Electricity and Gas defined the general principles and criteria of market monitoring for the companies Terna, GME and GSE, calling for each of these companies to establish a specific monitoring office.
Electricity market risk management is Terna's monitoring unit, which is responsible for the TIMM data warehouse and sees to the acquisition, organisation and storage of data in order to monitor the volumes and indicators related to the Market for Dispatching Services.
The activity in question is particularly important under the scope of the Terna incentives scheme envisaged by Authority Resolution no. 213/09 in relation to the procurement of resources for the dispatching service.
In 2011, new developments were implemented on the TIMM following the 2011 reform of the Market for Dispatching Services, which entailed a major review of the TIMM and which were successfully completed within the terms envisaged.

### Electricity system risk management

Terna is responsible for the efficient, effective and coordinated operation of the entire electrical system, even if it only directly manages the National Transmission Grid. It therefore follows that the share of internal vulnerability, mainly a function of the reliability of the systems and components, can be associated with additional threats due to the inadequate function of the plants connected that are not managed by Terna. The action taken to maintain risk levels at acceptable values is therefore twofold and it uses both investigation and diagnostic tools on electrical system equipment, to prevent failures on the basis of plant monitoring and the monitoring of events observed, and the supervision of the onset of any exogenous events such as breach of the Network Code by plants connected to the National Transmission Grid. Recently, the connection of plants with innovative characteristics, such as those with non-programmable renewable sources, not entirely regulated by the Network Code has required: analyses, studies and agreements with constructors, producers and distribution companies to ensure conditions that will result in amendments and supplements to Terna's instructions for the secure connection to the transmission grid.

### Fraud Management

In 2011, the Fraud Management Unit continued with its control of company fraud, taking all actions needed to prevent its occurrence. Under this scope, the company has implemented specific procedure for certain critical processes, which are able to define management methods and criteria focussed on maximising efficiency and effectiveness and preventing unlawful conduct. Together with the activities involved in preventing crime, the Fraud Management Unit also carried out:

- activities to support the Company's other units, such as in the analysis and assessment of counterparties, so as to limit the risks deriving from transactions with others;
- compliance activities focusing on cooperating with and supporting the Company's management and its various offices, aimed at ensuring compliance with laws, regulations, procedures, codes of conduct, and best practices, as well as at reducing and/or preventing the risk of sanctions and safeguarding the Company's image.

### Supplier qualification

Terna uses a business qualification system instituted in accordance with European Community Directives (Italian Legislative Decree no. 163/2006 "Code of contracts for public works, services and supplies" as subsequently amended and supplemented) for all main core segments of supplies, works and services.

In 2011, in compliance with the provisions of Italian Legislative Decree no. 205 of 3 December 2010 as subsequently amended and supplemented, incorporating the regulation of the waste traceability system – SISTRI – the supplier qualification unit created a new merchandising sector called "Waste management", which defines the technical and qualitative requirements that businesses must meet in order to be qualified and included on the list of suppliers. The activity in question concerns the collection, transport, storage, recovery and disposal of special hazardous and non-hazardous waste produced by Terna.

Another important project begun in 2011 by the Supplier qualification unit concerned the creation of a single portal called UPQ - Unification of Qualification Portals, including two systems currently used, the AQF portal for the management of qualification applications and PQI, relating to staff training, as well as a newly developed section devoted to business monitoring.

Additionally, in collaboration with the Safety unit, the Supervision unit on the Organisational Model, under Legislative Decree 231/2001, the Management and Fraud Systems Supervision unit, activity has been undertaken concerning the inspection of Terna sites, in order to assess the correct action of the businesses on the list. Following the results of checks carried out at Terna sites, the need has arisen to populate the Roll of Professionals, with specific reference to the merchandising segment "Security-related appointments", relating to the professional figures of Coordinators for the design and execution of works (CSP and CSE).

Finally, in implementing a constant compliance with safety in the workplace, with the obligation by the businesses to present the certificates relating to the training of professional figures such as the accident prevention and protection service manager (RSPP, *Responsabile del Servizio di Prevenzione e Protezione*) and the workers' safety representative (RLS) has been introduced in both the general regulations on the portal and included among the basic requirements for qualification.

### Monitoring of the Organisational Model under Legislative Decree 231/2001

In 2011, following the introduction of environmental crimes as new crimes envisaged under the scope of Legislative Decree 231/2001, the assessment of "environmental risks" has been started and concluded (through the evaluation of the reference legislation – Italian Legislative Decree no. 121/2011 – the as-is gap analysis, the interviews with the management, the identification of areas at risk and connected with risk activities and the assessment of the internal control system). Following these activities, the new special part of the model was prepared in relation to the environmental crimes both for Terna S.p.A. and for its subsidiaries SunTergrid and Terna Rete Italia (formerly TELAT).

Terna also belongs to a work group established to adapt the Confindustria Guidelines to the new demands of the businesses and, by virtue of this, to enable a correct interpretation and application of the regulations on environmental crimes.

In training/information terms, the sensitisation campaign calibrated according to the areas at "risk of crime" has been concluded, in which everyone finds themselves operating; a "Manual on the Organisational and Management Model" has been prepared and diffused, intended for Terna S.p.A. staff, in order to encourage a simplified reading of the Model that, however, is also complete in its fundamental elements; in collaboration with the other management areas (Safety, Qualification, Monitoring of Fraud Management Systems), activity was then undertaken concerning the inspection of sites in order to guarantee an all-round analysis of documentation by means of the preparation of specific check-lists and the assessment of all probable effects under the scope of Legislative Decree 231 and suggesting any possible corrective action.

### Control of Management Systems

In 2011, through an audit by the Certifying Body (IMQ), Terna obtained certifications UNI EN ISO 9001:2008, UNI EN ISO 14001:2004 and BS OHSAS 18001:2007.

On 14 September 2011, Terna also obtained ISO/IEC 27001:2005 certification of the TIMM (Integrated Text for the Monitoring of the Electricity Market) applications and the Management Systems Monitoring unit contributed to the project, implementing and managing its business.

In 2011, to comply with recent applicable legislation, support was begun for the ISO/IEC 17025 certification of the calibration and test laboratories for the equipment used in powered works.

In the environmental field, a work group was instituted with a view to implementing an energy management system compliant with standard ISO 50001:2001 by means of which the company will be able to implement the processes necessary to analyse the consumption of energy, activate plans, objectives and energy performance indicators to reduce consumption and identify opportunities by which to improve energy performance. Subsequently the opportunity will be assessed of having an external body certify the energy management system implemented.

### Physical security

Terna has established new surveillance and protection systems that are in line with their importance to the functioning of the electrical system and suited to the number and type of actual or potential threats they are designed to face.
With this goal, and for the first time in Italy, Terna has adopted risk assessment methodology for each of the stations concerned in order to analyse the related physical risk - concerning both actual and potential attacks - and electrical risk. Based on the “role” that each system plays in the functioning of the national electrical system, determined by assigning a risk index to each station based on their respective critical importance, a long-term action plan has been developed.
The project, which began in 2009, today sees 102 electrical stations equipped with anti break-in and video surveillance systems. The anti break-in dual technology systems come in addition to 60 VideoBox systems set up to protect the material deposit areas circumscribed within the power stations. Additionally, the T-Guardian project is currently being completed, which consists of supplying those on call with a palmtop and software enabling them to connect, in the event of an alarm, with the sites concerned and interface on-line with the police force for all relevant intervention.

### Information security

In terms of activities carried out to improve the security of the “company computer systems and information” and to align with the obligations and dynamics of the applicable legislative framework, which evolves continuously, in 2011 the main initiatives concerned not only a further campaign stage for the diffused growth of awareness and sensitivity, but also (I) the move from an “events” based approach to a systematic action in making effective verifications available on ICT security proceedings applied to systems and (II) the strategic value goal of certification ISO/IEC 27001, scope of challenge and comparison with the world’s most popular international standard in terms of information security.
Able to rely on an internal regulatory framework in terms of complete, detailed rules and policies, the focus of verifications pursuant to point (I) has easily moved towards information security assessment activities on ICT systems and infrastructures that are most critical to the business’s success, with the twofold objective of both measuring the level of exposure to the potential risk and verifying the level of conformity with the model established in Terna, launching any plans of action as necessary (also referred to as “recovery plans”) aimed at eliminating or reducing technological, operative or organisational weaknesses revealed by the analyses.
Following on from a programme established at the start of the year on the basis of priority considerations and exploiting a technological platform of very advanced vulnerability analysis acquired by Terna and managed entirely by specialised in-house resources, during the year, numerous, repeated security assessments were performed on specific ICT environments, clarifying the level of application of the governance model and the presence of severe or serious fragilities or deficiencies of various types.
This type of approach naturally has value only if it gives rise to, albeit in a gradual, sustainable manner, a virtuous cycle that increases production levels for the company technological infrastructures (and the related information) from the most common threats, with specific reference to those originating from cyberspace: hence in each action, reporting has always been ensured and prepared in great detail, able to guide or suggest any corrective action.
In compliance with the company’s ethical objectives, the same programme also pursues the search for conformity with the entire framework applicable to the matter, which is constantly evolving according to the importance that “information”, as an asset, is assuming in a company that is “always connected” and consequently in the business processes of companies and other organisations with a high technological content.
Under the scope of the initiative pursuant to point (II), useful to enriching the panel of Terna’s certifications and also with the broader aim of improving the underlying data and system security processes, in July 2011, the path was successfully completed culminating in certification with standard ISO/IEC 27001:2005 in relation to the scope of TIMM (Integrated Market Monitoring Text) applications, a route originally shared with the Authority for Electricity and Gas.
Strictly with regard to the TIMM service, the certification obtained has represented a major goal, for the confirmation that a third party entity, assessed the way of working of so many different business players involved, recognising that Terna correctly applies security standards of international validity. An objective has also been achieved with benefits to image too, with the new certification calling Terna’s attention to the field of security governance and helping further improve the trust between the company and its stakeholders.
Regardless of any future developments on broader certification scopes, it must be stressed that the preparation to the certification stage brought with it benefits that were also extended to other Terna processes connected in various ways with the security of the IT networks and systems.
In actual fact, in order to present the relevant evidence to the certifying body, not only in-company processes were examined in detail and improved as necessary, and those near to the TIMM management cycle, but also processes that

although distant in terms of information security (e.g. the process for acquiring external resources, HR management, the provision of building services, etc.), in actual fact make an essential contribution to the final result demanded by the standard. Many of the controls envisaged by the standard and seen during certification do not, in fact, have effects that are limited to the scope of TIMM but rather which go across the company as a whole, with clear added value for the protection of the entire company information assets.

## Corporate social responsibility

Terna plays an essential, irreplaceable role in the Italian electrical system. The greatest social and economic impact of the company's business lies in its capacity to ensure the general public a reliable, efficient electricity service. The commitment to service is therefore the main point of reference also of the approach to matters of sustainability, of which, in particular, respect for the environment and territory and attention to safety at work and staff training, are particularly important. In general, Terna's intent, as sanctioned in its Code of Ethics, is to construct and develop relationships based on trust with stakeholders, which are able to create value for the business, the company and the environment.
In this context, the matter of anticipating the specific risks linked to the social and environmental impacts and, more general, to relations with stakeholders, is particularly important. In this sense, the presence of a Corporate Social Responsibility department that helps define, in collaboration with all company management and with reference to best practices, the company's sustainability objectives from an ethical, social, environmental and governance of sustainability viewpoint and the communication of objectives and results of corporate social responsibility, becomes even more important. The department also constantly monitors the risks connected with sustainability aspects, which entail potential negative fallout on the company's reputation and intangible value, through the analysis of the ratings of the main agencies (such as, for example SAM - Sustainable Asset Management; Vigeo; Eiris), which process regular sustainability assessments.

In 2011, Terna reported significant progress in all areas of sustainability.
In the area of **environmental responsibility**, we can distinguish between:

- completion of the environmental compensation and mitigation interventions in three WWF oases, which represent a first development of the plan of action for the sustainability of the development of the National Transmission Grid (NTG) envisaged by the Terna-WWF strategic partnership agreement signed in 2009;
- the signing of a Memorandum of Understanding with Legambiente to promote a culture of energy sustainability that combines the development of the electrical system with that of renewable sources. Terna and Legambiente undertake to promote and spread awareness of the world of energy and start-up shared action for the environmentally sustainable energy transport, starting with the reduction of $CO_2$ in the atmosphere;
- the finalisation of guidelines for energy efficiency in Terna buildings.

In the area of **social responsibility**, we would point out:

- the adaptation of the monitoring instruments envisaged by LBG - The London Benchmarking Group methodology to the Italian context and to the specific needs of Terna, for a full measurement of contributions (in money, work time, kind) destined for initiatives in the communities and effective social results achieved;
- the definition of rules for the planning, development and monitoring of the free transfer of company equipment and machinery – no longer able to be used by Terna but still usable – to non-profit organisations for solidarity projects in Italy and abroad.

We also note the complete review of the "sustainability" section of the institutional website www.terna.it, extended in its contents and completed with a mini website on electromagnetic fields, which has earned Terna a fifth place in the annual "CSR Online Awards" classification prepared by the specialised company Lundquist.
The information on the social and environmental impacts of Terna are detailed in the sustainability report published by Terna every year, after approval of its Annual financial report.
In order to provide an increasingly integrated and complete representation of the operating characteristics, we have here anticipated some indicators on the environment and staff.
These indicators have been identified in accordance with the indications given by the Consiglio Nazionale dei Dottori Commercialisti e degli Esperti Contabili (CNDCEC, the Italian Accounting Profession) on sustainability in compulsory business disclosures (the directors' report of separate financial statements in view of the new features introduced by Italian Legislative Decree no. 32/2007, CNDCEC, January 2009).
In particular:

- no fatal accidents were recorded in the workplace, nor were there any fatal or serious accidents in previous years for which the Company's liability was ascertained in a final ruling during the year;
- no allegations were recorded regarding workplace bullying or work-related illness - regarding current or former employees - for which Terna was held liable in a final ruling;
- no cases of environmental damage were registered for which Terna was held culpable in a final ruling;
- no final penalties or sanctions were levied against the Parent Company for environmental damage.

## Information Technology

Significant benefits were achieved in 2011 as a result of information and communication technology projects and innovation at Terna. The following two main were achieved:
1. benefits for the business deriving from the completion of important initiatives;
2. achievement of management efficiency and efficiency benefits.

### 1. Benefits for business deriving from the completion of important initiatives

- **Enhancement of National Electricity System security** - National Electricity System security was enhanced through a series of interventions to improve the effectiveness of the control and operation system as regards the observed grid perimeter (extended in 2011 to 100% of the primary distribution stations) and real-time output plants (with more than 2,700 MW added).
  The efficiency of the Defence System has been improved thanks to the extension of the scope with reference to sections referring to renewable generation, the interconnection on the Northern Frontier and the connection of Continental Italy and Sardinia.
  Activities have begun aimed at analysing the impact on security of the electrical system deriving from the diffusion of renewable and distributed generation, also with a view to the recent growth of wind and photovoltaic power installations in Italy and, in general, in the interconnected European system.
  Security and reliability of the control rooms in the territory have been improved in terms of logical segregation and the raising of the protection level of ICT consoles in support of the shift operators.
  Finally, the disaster recovery solution has been enhanced through the rationalisation of flows and the automation of the activation procedures. In December, a full DR test was completed with great success, that enabled the measurement of the capacity and reaction times of people, processes and IT instruments in the event of a disaster at the National Control Centre.

- **Improvement of efficiency** - Following AEEG Resolution ARG/elt 351/07, in which Terna is encouraged to reduce the volumes procured on the Market for Dispatching Services, the IT instruments and processes supporting programming and dispatching activities in real time underwent important changes. The instruments involved in the forecasting of demand and production from wind sources have been strengthened; new instruments and methods have been introduced to support the Market for Dispatching Services for the continuous verification of electrical system suitability and security conditions with a view to improving the efficiency of procurement. The Energy Management System for system security verifications has been extended in terms of upgrading optimal power flow algorithms, introducing optimal power flow instruments in support of voltage regulation and dynamic security assessment for the continuous simulation of events and to assess the impact of these on the system security.

- **Regulatory adjustments** - The application platform supporting the Market for Dispatching Services and the liquidation of the energy items associated (“settlement activities”) was adjusted to meet the dispatching rules defined for 2011 for the reform of the electricity market, which began in 2010 and informed by Italian Law no. 2/2009. This amendment to legislation has made it necessary to extend the platform for the management of further Energy Market and Market for Dispatching Services sessions to be carried out on flow days, according to the same methods as existing sessions, but with shorter time frames.

### 2. Achievement of management efficiency and efficiency benefits

- The entry into operation towards late 2010 of the Customer Relationship Management (CRM) system enabled, in 2011, the rationalisation and standardisation of information flows towards operators, guaranteeing transparency and traceability in the management of relations between Terna and system operators.

- In 2011, moreover, the new metering platform entered operation, for the management of measurements of the Production Units connected to the NTG. The new platform is able to streamline the relevant processes and automate data exchange with Dispatching Users, thereby ensuring significant benefits in terms of quality of service with regard to counterparties and efficiency internally.

- Finally, the projects to strengthen ICT governance have enabled the improvement of the efficiency of the IT supporting core processes, through the introduction of instruments and procedures to manage and monitor ICT resources (e.g. CMDB, SAL management, performance management, etc.).

### Managerial information technology and services to people

In 2011, software development activities continued in support of the business and pre-existing technology was consolidated in the design rooms and on the 3,700 work stations with a view to maximising security of information and guaranteeing ever better service levels.

There were a good deal of different technological projects to make secure the work stations. In particular, all major critical security issues of the installations of Microsoft operating systems on clients and servers were first detected and bridged and subsequently the Oracle/SAP platforms were analysed on the relevant technological infrastructures.

Levels of "impermeability" to malware and viruses guaranteed mean that the infrastructures managed by SA-ISP are of "low" risk level with respect to technological "penetration" by external hackers.

Technological infrastructures were introduced that can guarantee a precise, timely detection of Terna IT assets connected and used on a local network by the individual Terna users. This is to manage and best govern the technological renewal of the devices; ill-advised use by "improper" owners has a significant impact on business in the event of server failures with related disservices of the applications supported.

New rules of design, development and operation of application software were defined and implemented, pursuing certification ISO 27001 of the TIMM project in the complete internal client chain (AR), electrical market risk (SA-RME), Power Exchange legacy systems development (DSC-TSP) and SAP systems development (SA-ISP).

The definition of new standards for certification was then extended to new software development projects to guarantee higher overall quality in the delivery of the various applicative technologies.

## Research and Development

To introduce new technological and systems solutions, new instruments and methods aimed at improving the reliability of plants and, therefore, quality of service, Terna mainly uses in-house technicians who base their work on the careful monitoring and analysis of conduct of equipment and plants. Terna also uses the specialised support of constructors, collaboration with universities, RSE S.p.A. (Ricerca Sistema Energetico) and CESI S.p.A., a specialised service company in which it has a 42.406% equity interest. In particular, in 2011 the Terna Group incurred costs of €18.3 million in respect of the associate CESI of which €16 million were capitalised. The accounting treatment of Research and Development expenses is discussed in the "Intangible assets" paragraph of section "A. Accounting policies and measurement criteria" of the Notes to the financial statements of Terna S.p.A. at 31 December 2011.

Studies for the innovation and development of new engineering solutions take place in four main families of research.

| Purpose | Projects and progress 2011 |
|---|---|
| OPTIMISATION OF STRUCTURES AND MATERIALS | |
| **Design of less bulky supports and/or improved environmental integration** | **High-performance single-stem tubular supports**<br>The executive design of the special strain supports for 380 kV lines has been concluded.<br>**International "Pylons of the future" contest**<br>The executive design phase has begun of prototypes in simple and dual circuit with the Dutton-Rosental rewarded support. |
| **Upgrading of transmission capacity of existing lines** | **Innovative high-performance conductors**<br>The experience of the INVAR-ZTAL conductors has been consolidated, characterised by a high thermal limit and reduced lengthening, useful for solving critical issues connected with distances from sensitive places.<br>Feasibility studies have begun for the installation of high temperature conductors of a time other than INVAR-ZTAL.<br>A first type of these conductors has a highly-resistant steel support and aluminium cladding. A second type uses carbon fibre cables as a support. For these conductors, experiments are underway on the whole of the high altitude line. An experimental installation has also been realised with a carbon fibre conductor on a mountain stretch.<br>The study and experimental installation has been completed of an innovative conductor that limits overload by wet snow. |
| **New technology for high voltage cables** | **P-Laser**<br>The new generation HV cable (using technology that has already been consolidated on the MV), completely produced with recyclable raw materials, is currently being experimented. It will ensure a reduction in the environmental impact of grids and, at the same time, a rise in the capacity to transport energy. |
| EQUIPMENT DIAGNOSTICS | |
| **Advance signalling of anomalies** | **New sensors on equipment and machinery**<br>In the Lacchiarella station, installation has been completed on the 380 kV section of new types of sensors positioned on board equipment and machinery. Installation is currently underway of another type on the 132 kV section. These will be observed in view of a potential widespread installation. |
| **Analysis and monitoring of line components** | **Insulator test laboratory**<br>A project is currently being planned for development of an experimental station for the study and monitoring of surface contamination of insulators. At present, the feasibility study has been concluded, which has enabled the identification of the most appropriate sites. |
| **Temperature monitoring on high voltage cables** | **DTS (Distributed Temperature Sensing)**<br>On the cable connections, in order to monitor and exploit transport capacity to the full, a study has begun on temperature monitoring systems available on the market with an analysis of their reliability. The technical specification for the purchase of this technology is being defined. |
| NEW EQUIPMENT | |
| **Reduction of space and development time of electrical stations**<br><br>**Compact stations with rapid installation** | **Integrated compact station equipment (MCI)**<br>This new equipment has been introduced, which, encompassing several functions in a single casing, reduces the space required to develop stations.<br>The installation of this new type of equipment is now consolidated in plants where more compact solutions that are quicker to develop are required.<br>To guarantee a rapid return to service in the event of disaster recovery, a mobile 150kV station has been designed and built, entirely mounted onto three trolleys that can be transferred to the site of use, with no need for special transport.<br>The mobile station has been designed in such a way that inclusion on the 150 kV line is possible quickly through a cable connection to the connector: all assembled and tested in the factory.<br>Given the advantages of this solution, the 380 kV mobile station has also been designed. Contact is currently being made with constructors to assess the possibility of developing it. |
| PLANT SAFETY | |
| **Transformer safety** | **New power transformer project**<br>Due to serious failures on power transformers, a series of improvements have been made to increase safety. More specifically, polymer insulators have been installed, which better tolerate the demands and prevent the projection of fragments in the event of failure, as instead is the case for those in ceramic used as of today.<br>Additionally, a series of reinforcements on the casing and case will be envisaged, to be tested through "short circuit tests", which will be carried out for each type of transformer. Short circuit tests will be repeated on all types, as most of the previous tests date back to several years previous. |

## Human Resources and Organisation

### Organisational structure

In 2011, no significant changes were made to the organisational macro-structure of Terna S.p.A..
However, we should point out the appointment of Giuseppe Saponaro as the new Chief Financial Officer, Control and M&A Director for Terna as from 19 May 2011.
On 9 November 2011, the Board of Directors of Terna S.p.A. approved the start-up of the **project for the new organisational structure of the Terna Group**, aimed at operatively implementing, within the time frame technically required, the provisions of the Company's business plan and maximising efficiency in the management of the Group's activities. The project entails the rent to a company that is a full subsidiary of Terna, of a business unit mainly consisting of employees currently employed by Terna in maintenance works on the National Transmission Grid (and other support activities) and assets (excluding the NTG); Terna will retain ownership of the NTG assets it owns and will continue to be responsible for the work reserved to it by the concession. The project also entails the management of non-core business through a specific company (Terna Plus S.r.l.) in order to meet market and efficiency demands.

### Human resources

Changes in the number of Parent Company employees are shown below.

| | Terna S.p.A. | | |
|---|---|---|---|
| CHANGE IN THE WORKFORCE | 31.12.2011 | 31.12.2010 | Change |
| Senior management | 60 | 59 | 1 |
| Junior management | 490 | 502 | -12 |
| Office staff | 1,966 | 1,890 | 76 |
| Production workers | 977 | 1,017 | -40 |
| **Total** | **3,493** | **3,468** | **25** |

The above figures do not include terminations with effect from 31 December.
Please note that as of 31 December 2011, the subsidiary Terna Crna Gora d.o.o. has 2 local employees, whilst the other subsidiaries have no employees.

### Resource development

Resource development activities carried out in 2011 were organised into two important sectors: performance management and professional development.
The Global Performance System, introduced in 2009, in 2011 saw the second complete closure of an assessment cycle, broken-down into: a) assignment of objectives, b) assessment of performance and Terna organisational conduct, c) feedback by managers. In 2011, a new performance management cycle began with the assignment and communication of new objectives. In order to include new population targets, the number of participants involved in the process was gradually increased, now amounting to approximately 770 (+10% on last year).
With regard to professional development, in 2011, with the support of an external executive search company, an assessment process was completed with the inclusion of the Dispatching and Operations Management, with the aim of training the resources in view of the generational takeover that will involve Terna in the years to come.

### Management incentive plans

Short-term management incentive schemes include an MBO (Management By Objectives) plan for 2011 targeted at senior and middle management, related to the achievement of individual, department and company performance objectives.
As concerns long-term management incentives, at the start of the year the 2006 Stock Option Plan is still in place, the deferral of which to 31 March 2013 was resolved in 2009. We note that during the period, a total of 5,596,300 residual options were exercised and that as of 31 December 2011, a total of 0 options can therefore be exercised.
Long-term cash-based managerial incentives are available to Top Managers and Key People under the cash-based three-year (2011-2013) Long Time Incentive (LTI) Plan, the purpose of which is to generate value and achieve the challenging performance targets set.

## Training

The focus of the 2011 training plan, in connection with the company's strategic objectives, was the development of business and innovation. Under this scope, the first important initiative was an event focussed on all managers and a selection of middle management. The training event, which obtained funding from Fondirigenti, took place as follows: two meetings with international experts in economic macro-scenarios and business evolution, a trip to two excellent companies in terms of innovation through a further meeting with an external witness and a guided tour. Conclusion is scheduled for 2012 with a workshop involving again two excellent external businesses in terms of innovation. Further initiatives included: a laboratory on innovation proposed, in a differentiated version, to a selection of middle managers and white-collar workers; an initiative focussed on problem-solving for the development of the organisational component "innovation and proactiveness", aimed at a selection of professionals and white-collar employees.

The new initiatives come in addition to a wide range of training relating to the Education section, aimed at developing/consolidating managerial and personal competences (soft skills and organisational conduct) further refined with respect to the previous plan. More specifically, two different lines of action aim to support the alignment of resources on all levels, with the Terna organisational conduct expected in performance: review of some projects devoted to managers and middle management and new courses prepared for the target thus far less reached by this type of training (blue and white-collar workers). A great many initiatives follow a logical themed pattern, which, in a differentiated fashion, invests all target addressees. For example, excellence in performance is laid out from the basic level of working for objectives or communication, inter-functional integration and teamwork, involving blue and white-collar workers in initiatives that, moreover, in the case of plant maintenance lines, aim to make an indirect contribution to the culture of working in safety too. Similar operations concerned significant transversal matters such as economics, the method of project management. In short, 2011 completes the optimisation of the offer in educational terms, which has progressively, over the three years (2009-2011) achieved the objective of substantially covering both the areas of intervention (Terna organisational conduct expected in performance) and addressees (to differing extents, all targets are involved: new employees and operative resources); additionally, almost all initiatives are assigned under the scope of the performance management process and/or in relation to managerial responsibilities of the development of collaborators.

More generally, the main driver of the overall training plan was the upgrading and consolidation of the "sharing of knowledge" model which characterises Campus, the logo under which all company training has been reunited since 2008. A great many activities were in fact carried out internally or partially by the Campus Faculty or Terna experts on business model or technical-professional matters relating to owned know-how or that which is distinctive to Terna. These include the basic modules and functional/specialised area of training courses, now fully up and operative, for new employees (graduate employees, high school graduate employees, blue-collar workers) and the routes for resources in service belonging to homogeneous professional families (e.g. real time shift workers) in addition to a great many training-related initiatives.

This section of training offer includes all initiatives aimed at the development of technical-professional, specialised and safety-related knowledge in addition to transversal skills (e.g. I&CT, languages) and again in 2011 saw, with the contribution of internal and external experts, the establishing of many initiatives in support of the necessary updates and alignment to technological and process innovations.

Moreover, starting from the sedimentation work of the know-how realised thus far by the Faculty Campus, during the last quarter of 2011, an offer of new courses on the training catalogue has been prepared, with single themes and of short duration, to be held in 2012. These are focussed on operative resources and have the aim of updating and/or developing/consolidating knowledge and technical-professional skills relating to the subsections under the scope of training: Operation & Maintenance, Development & Construction, Dispatching & Control.

In terms of safety, we should mention the completion of the update campaign on Devices for the Prevention of the Electrical Risk (DPRET) and, in relation to fulfilling the requirements under the Consolidated Law in Health and Savety at Work No. 81 (TU/81), the campaigns held for the training of fire-fighter workers, safe driving on soils not prepared for special vehicles. Additionally, towards the end of the year, a training event was held on safe site management, involving approximately 90 managers and workers during which an important specific and diffused training commitment on the matter was pre-announced for 2012.

Further important initiatives developed in 2011 included:

- a training campaign for all employees, for the training in the use of the on-line system of presence detection and expense notes accessible for the stations equipped on IT islands distributed throughout the territory;
- a route devoted to Management assistants and a pool of secretaries with the aim of updating and developing competences in a key role for management support;
- a diffused training campaign on Information Security in order to promote a widespread sensitisation on the responsibility of each employee with regard to the security of company information and to bring conduct into line with that envisaged by the company's policies and procedures on the matter.

In short, 97% of resources attended at least one course in 2011 (+1% on 2010), with more than 178,000 hours of training actually delivered (+4% on 2010).

### Industrial relations

For 2011, industrial relations featured negotiations with the national trade union secretaries in relation to company or second level contracts.
Two agreements in particular were signed, whereby the new economic-regulatory framework of reference was defined, to apply to the three-year period 2011-2013, respectively in terms of Results Premiums and the Reimbursement of costs when seconded. With this latter agreement, in particular, the pre-existing set-up was superseded, relating to 20 different regional agreements, providing for a gradual convergence - to be completed by 1 January 2013 - towards single amounts nationwide for the individual reimbursement items.
We would also point out that towards the end of the year, preventive discussions were formally started up with the national trade union secretaries, with regard to the project for the new corporate structure of the Terna Group.

### People Satisfaction

With high levels of adhesion, in 2007-2009, Terna carried out surveys on the organisational climate. In 2011, continuing along the route already undertaken of listening to its resources, research was carried out adopting the new investigation method on “Organisational Wellness”. This involved all employees in a survey conducted by means of questionnaire and a significant sample in focus groups taking a more in-depth approach. The results, which were generally positive, were diffused over the company’s intranet at the end of the year. At the start of 2012, work groups will be initiated to develop a plan of action with a view to continuous improvement in relation to the areas of attention that have emerged.

# Other information

## Related parties

Having been determined in 2007 that Cassa Depositi e Prestiti S.p.A. exercises de facto control, related party transactions undertaken by the Group during 2011 consisted of intercompany transactions, transactions with employee pension funds (Fondenel and Fopen), and transactions with companies of:

- the GSE Group;
- the Enel Group;
- the Eni Group;
- the Ferrovie dello Stato Group;

and ANAS S.p.A..

Related party transactions implemented in 2011 were substantively represented by services that fall under the scope of core business and were regulated by market conditions, as is described in greater detail in the Consolidated and separate financial statements at 31 December 2011. In addition, transactions with members of the Board of Statutory Auditors of the Parent Company, and in particular their fees, are detailed in the notes to the “Services” captions of the consolidated financial statements at 31 December 2011, to which reference is made.

The Parent Company’s Report on corporate governance and ownership structures, which are detailed in the Specific Report published with the 2011 financial statements, to which we would refer you, establish the conditions for ensuring that related party transactions are carried out in accordance with criteria of procedural and substantive propriety under the same terms and conditions that would apply to transactions with third parties, above all in the light of the new “Related party transactions procedure” adopted at end 2010 by the Parent Company in implementation of CONSOB Resolution no. 17221 of 12 March 2010, subsequently amended by Resolution no. 17389 of 23 June 2010, which issued the “Regulation incorporating provisions on related party transactions”. The provisions of the Regulation look to regulate transparency in market disclosures and principals of procedural and substantive propriety in implementing transactions with related parties. More specifically, the provisions relating to the public disclosure obligations (immediate and regular) in relation to related party transactions, considered individually, of significant importance, came into effect on 1 December 2010, whilst all other procedural provisions are compulsory as from 1 January 2011.

It is specified that during 2011, no significant transactions were implemented, namely related party transactions identified in compliance with the provisions of Annex 3 to the Regulation, nor transactions subject to compulsory disclosures but concluded by applying the exclusion established by the Regulation, insofar as they are “transactions coming under the scope of the core business of the Company’s continuing operations or those of the subsidiaries or associations or the financial activities related thereto, as long as concluded at conditions equivalent to market or standard conditions”.

Please note that in accordance with new regulations introduced by the CONSOB Resolution no. 18049 of 23 December 2011 published in the Italian Official Gazette no. 303 of 30 December 2011 and in force as from 31 December 2011, the disclosure on fees relating to the "members of the administrative and control bodies, general managers" and other "executives with strategic responsibilities" and on the equity interests held by these, has been included in the annual report on remuneration.

## Significant non-recurring events and transactions, atypical or unusual transactions

No significant, non-recurring, atypical or unusual transactions - with the exception of those described above - were carried out during 2011, either with third parties or with related parties.

## Other information

### Treasury shares

The Company does not hold any treasury shares or shares of Cassa Depositi e Prestiti S.p.A., nor has it acquired or sold any during the year, either directly or indirectly.

### Personal data protection code (Legislative Decree no. 196 of 30 June 2003)

Within the legally prescribed deadline, Terna S.p.A. updated its 2011 Security Policy Document pursuant to the personal data protection code (Legislative Decree no. 196 of 30 June 2003) and to implement the initiatives required to improve management introduced by the new version.
In addition to the current assets outlined as commitments in the stated Security Policy Document, Terna specifically promoted various initiatives aimed at applying the provision of the privacy guarantor of 8 April 2010 to its scope (in Italian Official Gazette no. 99 of 29 April 2010) on the "Measures concerning the processing of personal data and video surveillance", which definitively came into force in April 2011.

### Information on shareholding structure

Information required under Art. 123-*bis*, "Report on Corporate Governance and ownership structures" of the "Consolidated Law on Financial Intermediation" (Italian Legislative Decree no. 58 of 24 February 1998), is presented in a separate report (Annex - Report on corporate governance and ownership structures), approved by the administrative body and published with this Directors' Report, which is available on the website of Terna S.p.A. (www.terna.it in the section "Investor Relations/Report on corporate governance and ownership structures").

### Certifications in accordance with Article 2.6.2 of the Borsa Italiana Regulation with regard to the conditions pursuant to Articles 36 and 37 of the CONSOB Market Regulation (no. 16191/2007)

With regard to the provisions of Article 36 of the CONSOB Markets Regulation (no. 16191/2007 as subsequently amended), Terna S.p.A. does not hold any majority shares relevant in accordance with the mentioned legislation in companies incorporated and regulated by the laws of non-member countries of the European Union.
With regard to the provisions of Article 37 of said CONSOB Regulation, Terna S.p.A. is subject to the de facto control of Cassa Depositi e Prestiti S.p.A., which – as of 31 December 2011 – holds an equity interest amounting to 29.851% in the share capital, according to that verified by Cassa Depositi e Prestiti and disclosed on 19 April 2007. At present, no management or coordination has been formalised or exercised; Terna S.p.A. goes about its business directly or through its subsidiaries with independent management and trading.

# Attachment

# Italy’s regulatory framework

## Regulatory framework

Below is a brief description of the main regulatory measures that affected the Company in 2011.

**Italian Legislative Decree no. 28 of 3 March 2011 incorporating “Implementation of Directive 2009/28/EC on the promotion of the use of energy from renewable sources, amending and subsequently revoking Directives 2001/77/EC and 2003/30/EC”** published in the Italian Official Gazette no. 78 of 28 March 2011.
The Decree is without prejudice to the principle of a single authorisation procedure, with this to include not only production plants but also all works involved in connecting to the grids, functional to more than one plant, as long as included in the connection estimate. It is then established that the transmission grid Development Plan shall contain a specific section dedicated to the grid works necessary to ensure the release of energy produced by renewable source plants already operating. The section may include systems for storing electricity, aimed at facilitating the dispatch of non-programmable plants. The Decree establishes that for these works, the AEEG shall define return on investments.
The Decree also reforms incentives for renewable sources. The tariffs established in the 3rd energy account will apply to the photovoltaic plants entering into operation by 31 May 2011. For plants entering into operation after that date, reference will be made to a subsequent decree by the Ministry for Economic Development.
Again with regard to solar energy, limits are envisaged to access to incentives for plants in agricultural areas: plants with power of no more than 1 MW will have the right to incentives, as long as they are not intended to install plants for more than 10% of the surface area of agricultural land available to the principal. These limits do not apply to plants that have achieved qualification by 29 March 2011 or to plants for which a request has been presented for qualification by 1 January 2011, as long as, in any case, the plant will come into operation by 29 March 2012.
By 29 September 2011, the incentives for renewable sources will have been defined by implementation Decree: a) with the provision for a diversified incentive, up to a value that differs according to source and, in any case, no less than 5 MW; b) for plants of greater power, defining the lowest-bid procedures managed by GSE.

**Law no. 73 of 23 May 2011 published in the Italian Official Gazette of 25 May, enacting Law Decree no. 26 of 25 March 2011 “Urgent measures to guarantee the orderly operation of the companies’ annual shareholders’ meetings”**, published in the Italian Official Gazette no. 70 of 26 March 2011.

**Italian Legislative Decree no. 61 of 11 April 2011 “Implementation of Directive 2008/114/EC establishing the identification and designation of European critical infrastructures and the assessment of the need to improve their protection”**, published in the Italian Official Gazette no. 102 of 4 May 2011.
This Legislative Decree governs the identification of European critical infrastructures, namely those infrastructures which, if damaged or destroyed, would have a significant impact on at least two European Union Member States in implementation of Directive 2008/114/EC. The European critical infrastructures will be designated by decree of the President of the Council of Ministers following an assessment and discussion procedure with the other Member States.
For each infrastructure identified as critical, the principal of the infrastructure must prepare a security plan in compliance with the criteria established by the European Union and described in Annex B to said Decree, within 1 year of designation. Should the designated critical infrastructure already have a Security Plan in accordance with current regulatory provisions, the officials appointed by the competent ministries and the structure responsible shall merely ascertain that said provisions comply with the minimum requirements, informing the responsible prefect.
For each critical infrastructure, a connection officer must be identified, who provides a point of contact with the administrations concerned, including the Ministry of Interior, Civil Guard, Ministry for Economic Development, Prefect and Interministerial Nucleus.

**Decree by the Ministry for the Environment and for the Protection of the Territory and the Sea no. 52 of 18 February 2011 “Regulation establishing the institution of the system for controlling the traceability of waste in accordance with Article 189 of Italian Legislative Decree no. 152 of 3 April 2006 and Article 14-*bis* of Law Decree no. 78 of 1 July 2009 converted, with amendments, by Italian Law no. 102 of 3 August 2009”**, published in the Italian Official Gazette no. 95 of 26 April 2011.
The Decree brings together the regulations on the waste traceability control system for businesses (SISTRI).

**Decree of 26 May 2011 “Extension of the terms pursuant to Article 12, paragraph 2 of Decree of 17 December 2009, establishing the institution of the waste traceability control system”**, published in the Italian Official Gazette no. 124 of 30 May 2011.
The Decree refers the operations of SISTRI for major companies from 1 June 2011 to 1 September 2011.

**Decree of 5 May 2011 issued by the Ministry for Economic Development jointly with the Ministry for the Environment and the Protection of the Territory and the Sea, "Encouraging electricity production from photovoltaic solar plants"**, published in the Italian Official Gazette no. 109 of 12 May 2011.
The Decree (4th Energy Account) regulates the incentive system for photovoltaic plants starting-up from 1 June 2011 to 31 December 2016 and establishes, for these terms, the national objective for installed power of 23,000 MW for an indicative annual cumulative cost of the incentives that is estimated between €6 and 7 billion. The new tariffs will be applied for 20 years, with the level defined at the date on which the plant enters operation.
The Decree draws a distinction between:

- small plants (plants on buildings up to 1 MW, other plants up to 200 kW operating under the spot exchange regime or plants of any power developed on buildings and areas of the Public Administration) which have the right to incentives with no limit to cost;
- large plants (all other plants) for which cost limits apply (for 2011, €300 million; for the first half of 2012, €150 million; and for the second half of 2012, €130 million). For the latter, the obligation has been introduced to register with the GSE Register along with a hierarchy mechanism for accessing the incentives.

**Law Decree no. 70 of 13 May 2011 "European Semester - First urgent provisions for the economy"**, published in Italian Official Gazette no. 110 of 13 May 2011, enacted by Italian Law no. 106 of 12 July 2011, published in the Italian Official Gazette no. 160 of 12 July 2011.
The Law Decree acts on the procedure for landscape authorisation, on the regulations of the special sectors and, in particular, on the advance archaeological verification as well as on tenders and privacy as amended by Italian Legislative Decree no. 196/03.
Finally, it regulates tax credits for scientific research carried out by businesses and for the employment of disadvantaged workers in the south of Italy.

**Italian Law no. 75 of 26 May 2011 enacting Law Decree no. 34 of 31 March 2011**, published in Italian Official Gazette no. 74 of 31 March 2011, establishing **"Urgent measures in favour of culture as concerns crossovers between the sectors of press and television, rationalising the radio electric spectrum, nuclear delay, participation of Cassa Depositi e Prestiti and the entities of the National Health Service of the region of Abruzzi"**, published in Italian Official Gazette no. 122 of 27 May 2011.
By this provision, Italian Legislative Decree no. 31/2010 and the related regulations on the production of energy from nuclear sources and the location of plant are repealed.
The provision establishes that Cassa Depositi e Prestiti may "assume investments in companies of significant national interest in terms of the strategic role played in the sector of operations, of employment levels, of entity of turnover or of fallout on the country's economic-production system". The necessary requisite of the companies concerned by the acquisition is that they "are in a permanent situation of financial, equity and economic balance and characterised by suitable prospects to generate income". By a Decree of the Ministry of the Economy, the quantity and further requirements for classification of the companies of potential acquisition shall be defined. It is also specified that "These investments may also be acquired through special purpose vehicles or investment funds in which CDP S.p.A. invests and by private companies or state-controlled companies or public entities".

**Italian Legislative Decree no. 93 of 1 June 2011, "Implementation of Directives 2009/72/EC, 2009/73/EC and 2008/92/EC in relation to common rules for the domestic market in electricity, natural gas market and a community procedure on the transparency of prices to the end industrial consumer of gas and electricity, in addition to repealing Directives 2003/54/EC and 2003/55/EC"**, published in the Italian Official Gazette no. 148 of 28 June 2011.
Italian Legislative Decree no. 93/11 incorporates European Community regulations on unbundling the manager of the transmission system, establishing that by 3 March 2012, the AEEG must take a decision to certify Terna with respect to the separation provisions.
It establishes that the national transmission system manager "may develop and manage diffused electricity storage systems using batteries" and that it may not "directly or indirectly produce and supply electricity, nor manage, even on a temporary basis, infrastructures or plants for the production of electricity". Within 60 days, or rather by 28 August 2011, the Concession will be revised to implement the prohibition and in order to ensure that "the activities of manager of the national transmission system, different from those of programming, maintaining and developing the grid, do not prejudice respect of the principles of independence, service provision and non-discrimination".
Finally, with reference to the "development and management of pumping hydro electrical production plants included in the National Transmission Grid Development Plan", these "are entrusted by means of transparent, non-discriminatory competitive procedures". Within 90 days of approval of the transmission grid Development Plan, by Decree of the Ministry for Economic Development, having consulted with AEEG, "the methods by which to carry out the procedures are defined".

**Law Decree no. 98 of 6 July 2011 "Urgent provisions for financial stabilisation"**, published in Italian Official Gazette no. 155 of 6 July 2011 **converted by Italian Law no. 111 of 15 July 2011** published in Italian Official Gazette no. 164 of 16 July 2011.
This incorporates rules in tax matters and the access to pension schemes as well as establishing tax and contribution benefit for the part share of the salary of employees linked to productivity.

**Decree by the Ministry for Employment of 22 July 2011 "Postponement of the coming into force of the Decree of 11 April 2011 incorporating regulations of the method by which the regular checks are carried out pursuant to Annex VII of Legislative Decree no. 81 of 9 April 2008 and criteria for the qualification of parties pursuant to Article 71, paragraph 13 of said Legislative Decree"**, published in the Italian Official Gazette no. 173 of 27 July 2011.
With Decree by the Ministry for Employment of 22 July 2011, the effect of the regulations imposing regular checks of work equipment pursuant to the Consolidated Law on Safety at Work (Legislative Decree no. 81/08) set forth by Ministerial Decree of 11 April 2011 has been postponed to 24 January 2012.

**Italian Legislative Decree no. 121 of 7 July 2011 "Implementation of Directive 2008/99/EC on the criminal protection of the environment and Directive 2009/123/EC that amends Directive 2005/35/EC in relation to the pollution caused by ships and the introduction of sanctions for breach"**, published in the Italian Official Gazette no. 177 of 1 August 2011.
Italian Legislative Decree no. 121 of 7 July 2011 on the criminal protection of the environment has been published in the Italian Official Gazette. The Decree, in force since 16 August 2011, supplements the regulations set forth in Italian Legislative Decree no. 231/01 on the administrative liability of the companies, providing for pecuniary sanctions at the company's expense for certain types of environmental crimes, such as: damages to habitats in protected sites, unauthorised discharge of industrial waste water or in breach of the provisions on hazardous substances, soil pollution, etc.

**Legislative Decree no. 119 of 18 July 2011 "Implementation of Article 23 of Law no. 183 of 4 November 2010, delegating the Government to reorder regulations on leave and permits"**, published in the Italian Official Gazette no. 173 of 27 July 2011.
Italian Legislative Decree no. 119/11 on the reorder of regulations on leave and permits has been published in the Italian Official Gazette. Some new features concerned parental leave in the event of adoption and permits to assist the handicapped. In the event of fostering or adoption, the provisions on rest periods apply no longer within the first year of the child's life but rather within the first year of the child's joining the family, regardless of the child's age.

**Law no. 120 of 12 July 2011 "Changes to the Consolidated Law on the provisions of financial intermediation, pursuant to Legislative Decree no. 58 of 24 February 1998 concerning equal access to administrative and control bodies of companies listed on regulated markets"**, published in the Italian Official Gazette no. 174 of 28 July 2011.
The Law establishes that at least one third of the members of the Board of Directors and the Board of Auditors of listed companies must be members of the least represented gender, for three consecutive mandates. By 12 February 2012, CONSOB will establish by Regulation for listed companies with regard to the breach, application and compliance with the relevant provisions. The provisions shall apply "as from the first renewal of the administrative bodies and auditing bodies of listed companies" subsequent to 12 August 2012.

**Law Decree no. 138 of 13 August 2011 "Incorporating further urgent provisions for financial stabilisation and development"**, published in Italian Official Gazette no. 188 of 13 August 2011 and **converted with amendments by Italian Law no. 148 of 14 September 2011** published in the Italian Official Gazette of 16 September 2011.
This envisages the application of additional IRES (the "Robin Hood Tax") to the sectors of electricity production, transmission and dispatch, distribution or marketing, as well as the production of energy from renewable sources and the transport or distribution of natural gas, by 10.5% for the years from 2011 to 2013 (6.5% per annum as from 2014).
The Decree then establishes an increase from 12.5% to 20% of capital income tax (dividends, bond coupons, etc.) and 1% of VAT (from 20 to 21%).
Other provisions concern the reform of the retirement age for women and collective proximity contracts that may except from the national collective contracts and the provisions of the law. Finally, SISTRI is scheduled for coming into force as from 9 February 2012.

**Decree by the President of the Republic no. 151 of 1 August 2011 "Regulation simplifying the regulations of proceedings concerning fire prevention, in accordance with Article 49, paragraph 4-*quater*, of Law Decree no. 78 of 31 May 2010, converted, with amendments, by Italian Law no. 122 of 30 July 2010"**, published in the Italian Official Gazette no. 221 of 22 September 2011.

**Legislative Decree no. 159 of 6 September 2011 "Code of the anti-Mafia laws and measures of prevention in addition to new provisions on anti-Mafia documentation, in accordance with Articles 1 and 2 of Italian Law no. 136 of 13 August 2010"**, published in the Italian Official Gazette no. 226 of 28 September 2011.
The Decree amends and supplements regulations on anti-Mafia documentation.

**Decree of the President of the Republic of 14 September 2011 "List of statistical results coming under the national statistics programme for the three-year period 2011-2013, for which, for 2011, failure to supply data is breach of the obligation to respond, in accordance with Article 7 of Italian Legislative Decree no. 322 of 6 September 1989"**, published in the Italian Official Gazette no. 242 of 27 October 2011.

**Italian Law no. 180 of 11 November 2011 "Rules for the protection of the freedom of business. Business Statute"**, published in the Italian Official Gazette no. 265 of 14 November 2011.

**Decree of the Ministry for Economic Development of 11 November 2011 "Determination of the methods and conditions for the importing of electricity for 2012"**, published in the Italian Official Gazette no. 272 of 22 November 2011.

**Italian Law no. 183 of 12 November 2011 "Provisions for the preparation of the annual and multi-year financial statements of the state" (2012 Stability Law),** published in the Italian Official Gazette no. 265 of 14 November 2011.
The law, in force as from 1 January 2012, establishes provisions on the administrative liability of the entity on employment and tax matters.

**Italian Law Decree no. 201 of 6 December 2011 "Urgent provisions for financial stabilisation", enacted with amendments by Italian Law no. 214 of 22 December 2011**, published in Italian Official Gazette no. 300 of 27 December 2011.
The decree incorporates a measure aimed at encouraging the increase of the share capital of businesses which applies, for the year underway at 31 December 2011, with reference to "own capital existing at the end of the financial year underway at 31 December 2010", constituted, as already established by the decree, by the shareholders' equity resulting from the related financial statements, without considering the profit of the year.
The notional return of the new own capital is measured by applying the percentage rate identified with the decree to be issued by 31 January of each year by the Ministry for the Economy and Finance, considering the average financial returns of the public bond securities, which can be increased by a further three percentage points to compensate for the greater risk. In a transitional manner, for the first three years, the rate is fixed at 3%. The part of the notional return that exceeds the net comprehensive income declared is calculated by increasing the deductible amount from the income of subsequent tax periods. The measure will apply as from the tax period underway as at 31 December 2011.
In terms of IRES and IRAP, it is established that as from the tax period underway at 31 December 2012, an amount may be deducted from IRES equal to the regional tax on production in relation to the taxable share of the personnel costs and similar, net of the deductions due in accordance with IRAP regulations.
With regard to the realignment of tax and statutory values of equity interests, the terms for the instalment payment of substitute tax have been extended to operations implemented during previous tax periods, establishing that "they will also apply to operations implemented in the tax period underway at 31 December 2010 and in those previous. In this case, as from 1 December 2011, interest shall be due on each instalment in the amount equal to the legal rate".
With regard to investments in the energy field, it is established that ISVAP shall regulate, with its own regulation "the methods, limits and conditions that may be used by companies authorised to provide insurance in order to cover technical provisions... assets comprising investments in road, rail, port, airport and hospital infrastructures, telecommunications and energy production and transport and energy sources".
Italian Law Decree 112/2008 is amended to establish that in order to compile the Consolidated Book of works end, rather than by the 16th of the month "it must be completed... for each reference month" by the end of the following month.
The new provision included in the Tenders Code also applies to special sectors, whereby "For works tendered for a basic amount in excess of €20 million, to be awarded with a restricted procedure, the tendering stations shall specify in the tender that a preliminary consultation has been called on the project underlying the tender, guaranteeing a hearing of both parties". Additionally "In order to encourage access by small and medium enterprises, tenderers must, where possible and economically convenient, divide the tenders up into functional lots". The development of major infrastructures, including those covered by the Infrastructure Law "and connected supplementary or compensating works, must guarantee methods by which to involve small and medium enterprises".

**Italian Law Decree no. 212 of 22 December 2011 "Urgent provisions on the settlement of the sovereign debt crisis and regulation of the civil proceedings"**, published in the Italian Official Gazette no. 297 of 22 December 2011.
The decree establishes a transitional provision which, for joint-stock companies, establishes that "boards of auditors appointed by 31 December 2011 shall remain in office until the natural expiry of the mandate resolved by the shareholders' meeting that appointed them".

**Italian Law Decree 216 of 29 December 2011 "Extension of terms established by legislative provisions"**, published in the Italian Official Gazette no. 302 of 29 December 2011.
The decree contains tax provisions.
It is specified that the single rate of 20% introduced by Italian Law Decree 138/11 applies (Art. 29):
- as from 1 January 2012 with reference to interest and other income "deriving from current and deposit accounts held with banks or post offices, even if represented by certificates maturing as from that date" and not, therefore, to interest and income matured previous to that and liquidated as from 2012;
- from the day after the maturity date of the forward contracts stipulated prior to 1 January 2012 and with a duration of no more than 12 months in relation to capital income, such as income deriving from repurchase and forward contracts on securities and currencies and interest and other income from bonds and similar securities pursuant to Italian Legislative Decree no. 239/1996 ("interest, premiums and other income from bonds and similar securities, public and private").

The terms from which the obligation shall apply, introduced by the 2008 Financial Manoeuvre, for tax substitutes to electronically communicate the salary data and information necessary for the calculation of tax withholdings and contributions each month, last established as January 2012, has been extended to January 2014, with experimentation, as from 2013, with methods established jointly by the Tax Authority and the National Social Security Institute.
Finally, the terms for the operations of SISTRI are postponed from 9 February 2012 to 2 April 2012.

**Italian Law Decree 1/2012 "Urgent provisions for competition, development of infrastructures and competitiveness"** (referred to as the "Liberalisation Law Decree"), published in the Italian Official Gazette no. 19 of 24 January 2012.
This establishes that, with a view to facilitating and accelerating the development of grid infrastructures of national interest, the Authority for Electricity and Gas, within 90 days of the Concession holder request, shall define the remuneration in relation to specific assets regulated and existing on the date of the request, with no increase to the overall capital remuneration and tariff with respect to the regulation underway.
For the gas sector, it is established that within 6 months (July 2012), by Decree of the President of the Council of Ministers, the provisions will be defined that will govern the sale "in relation to the equity interest currently held in Snam S.p.A.".
The Decree establishes that without prejudice to the annual nature of the National Transmission Grid Development Plan and the evaluation procedures, public consultation and approval, the plan shall be subjected once a year to verification of subjection to SEA procedures and, in any case, once every three years to SEA procedures.
The Decree then incorporates provisions relating to the systems for the protection and defence of the grids and security devices that must be used on the production plants.
Finally, with reference to production from renewable sources, the Decree establishes that the Ministry for Economic Development, within 120 days (23 May 2012), having consulted with the Energy Authority, shall emanate guidelines and amendments to the regulations, implementing the provisions on the Regulation of the electricity market with a view to limiting costs and guaranteeing the security and quality of the supplies of electricity, in compliance with market criteria and principles.

**Decree by the Ministry for Employment and Social Policy of 20 January 2012 "Deferment of the coming into force of the Decree of 11 April 2011, incorporating: "Regulation of the method by which regular checks are performed pursuant to Annex VII to Italian Legislative Decree no. 81 of 9 April 2008 and criteria for qualifying subjects pursuant to Art. 71, paragraph 13 of the same Italian Legislative Decree"**, published in the Italian Official Gazette no. 19 of 24 January 2012.

## Resolutions of the Authority for Electricity and Gas

### Resolution ARG/elt 148/11

By this provision, the Authority, in addition to approving the draft project for the Consolidated Records Management system of Production Plants and the related units (GAUDÌ), as proposed by Terna and to defining the time frames for the related implementation, recognised costs to the related institution of said system.
These costs will be recognised in the price to cover the costs recognised for Terna's operation (DIS).
Finally, the provision contains amendments to the Consolidated Act on Active Connections (TICA) in order to simplify information flows connected with the function of GAUDÌ.

### Resolution ARG/elt 149/11

By Resolution ARG/elt, the Authority has dictated provisions implementing Article 20 of the Decree by the Ministry for Economic Development, jointly with the Ministry for the Environment and the Protection of the Territory and the Sea, 5 May 2011, in order to encourage the production of electricity from solar photovoltaic plants. More specifically, the Authority has defined the price for the remuneration of certification of works end activities carried out by the grid managers for a fixed price of:

- €2,000 for plants with power ranging between 6 and 10 MW;
- €4,000 for plants with power above 10 MW.

Additionally, the Authority has defined the specific methods by which to regulate this price, establishing that, as from 1 December 2011, said prices must be paid by the party requesting the connection when the communication of completion of the construction of the production plant is sent to the manager. Failure to make payment will mean suspension of the terms for the activation of the connection and, in the event no payment is made, even after demands by the grid manager, it shall notify the GSE, which will suspend disbursement of the incentive.
Should a manager fail to make the check within 30 days as established by the Decree of 5 May 2011, without prejudice to cases of force majeure or causes that can be traced to the applicant or third parties, it must pay automatic indemnity amounting to €20 per working day's delay.

### Resolution AGR/com 153/11

By this provision, the Authority has defined the regulations of the certification procedures of businesses acting as natural gas transport system managers or electricity transmission operators, in implementation of the provisions of Directive 2009/72/EC - as also incorporated by the national legislator with Italian Legislative Decree no. 93/11 - which establishes a timely certification process of the transmission/transport system operators aimed at proving compliance by said parties with the conditions established by European Community Regulations for the three models of separation of the transmission/transport activities from the generation/production and supply activities - the ownership unbundling (OU) the institution of an independent transmission operator (ITO); the institution of an independent system operator (ISO).
The certification procedure, carried out by the Authority on the basis of the information sent by the transmission and transport operators, includes, in short:

a) a preliminary certification decision, taken by the Authority within four months of receiving the data sent by the operators;
b) the opinion of the European Commission on this preliminary certification, to be obtained during the next two months;
c) the definitive decision on certification, which will be made by the Authority within 2 months of receiving the European Commission opinion.

A subsequent "re-certification" procedure is also established if significant changes should be made to the data declared by the operators and, in any case, three years after certification.
The model to be certified, for Terna, is that of ownership unbundling, the option chosen as "preferable" by the European Community legislator.

### Resolution ARG/elt 158/11

By this provision, the Authority approved, under the scope of the more extensive interconnector regulations pursuant to Art. 32 of Italian Law no. 99/09, the Regulation governing tenders for virtual imports for 2012, as proposed by Terna. The provision is issued in accordance with Resolution ARG/elt 179/09, which establishes that each year, by 31 October, Terna shall send the Authority the Regulation for approval governing the tender procedures by which to identify the parties undertaking to provide the virtual importation service for the following year.

**Resolution ARG/elt 162/11**

By this provision, the Authority, also on the basis of that established by the Decree of the Ministry for Economic Development of 11 November 2011 - incorporating terms and conditions for the import of electricity for 2012, by means of the National Transmission Grid, has:

- approved the "Rules for capacity allocation by explicit auction within Central West Europe Region, Central South Europe Region and Switzerland' (Access Rules) prepared by Terna jointly with other grid operators involved in the works of the Regional Initiatives for the Central South and Central West Europe and Switzerland. The new rules for accessing the interconnection grids are, for the first time, basically the same for all interconnections of the Central South and Central West Europe and Switzerland;
- approved provisions on the management of congestion in imports and exports on the Italian interconnection grid with abroad;
- confirmed that the income from the procedures for assigning transport capacity, due to Terna, will be used to reduce the prices for accessing the grid for end users of the national electricity system, through the reduction in the price for the procurement of resources on the Market for Dispatching Services.

**Resolutions ARG/elt 172/11, 176/11, 208/11 and 209/11**

These provisions defined, for 2012, the regulations of the essential units.

More specifically, with Resolution ARG/elt 172/11, the Authority, in addition to approving the proposals sent by Terna with regard to the standard parameters calculated for the essential units defined for 2012, has specified some criteria by which to determine the price of the essential units. By Resolution ARG/elt 176/11, the Authority subsequently defined some aspects in relation to alternative regulations of essential plants with specific reference to the quantities and prices of contracts concerned by the contracts pursuant to Art. 65-*bis* of Annex A to Resolution no. 111/06.

Additionally, with Resolution ARG/elt 208/11, the Authority has upheld the requests made by some dispatching users owning essential units in relation to the admission to the reintegration of costs regime (which establishes the recognition of a price, determined by the Authority as amounting to the difference between the production costs recognised to the plant, considering the revenue it obtains upon inclusion on the list of essential plants at the end of the validity of said list).

Finally, with Resolution ARG/elt 209/11, the Authority has approved, for 2012, the contractual proposals sent by Terna pursuant to Article 65-*bis*, paragraph 65-*bis*-5 of the Resolution no. 111/06, containing the alternative methods by which users of dispatching owning essential units can fulfil their obligations.

**Resolution ARG/elt 177/11**

By this provision, the Authority has determined the amount recognised to Terna to cover the adjusted costs for 2010 and forecast costs for 2012 for the performing of activities associated with the monitoring function pursuant to Article 3, paragraph 3.2 of AEEG Resolution 115/08 of 5 August 2008. More specifically, the final amount of costs adjusted and recognised to Terna for 2010 for carrying out these activities amounts to €662,600, whilst the amount of costs forecast for recognition for 2012 is €920,200.

The difference between the forecast costs pursuant to the paragraph above for 2012 and the income obtained from the difference between costs actually recognised upon adjustment for 2010 and the costs forecast for that same year, is covered by means of the price for the operation of Terna for 2012.

**Resolution ARG/elt 181/11**

By this provision, the Authority updated Resolution 111/06 and Resolution ARG/elt 74/08 (in situ exchange) in order to incorporate the new definition of high performance cogeneration on the basis of the provisions of Ministerial Decrees of 4 August 2011 and 5 September 2011. With reference to Resolution 111/06, the Authority has introduced a definition of a high performance cogeneration unit in order to recognise dispatching priorities, based on the prevalence criteria. In actual facts, considering that the new definition of high performance cogeneration established by the Ministerial Decrees establishes that a cogeneration section or plant may also be partially high performance, the Authority has established that, for the purpose of recognising dispatching priorities, a production unit can be considered a high performance cogeneration unit as long as it complies with the conditions set out by Italian Legislative Decree no. 20/07 and the Decree of 4 August 2011 and the related size $E_{CHP}$ is greater or equal to half the total gross production of electricity by said production unit. Additionally, there is also the option of recognising the qualification of high performance cogeneration unit and consequently dispatching priorities for a part of a year.

The Authority has also amended Articles 56, 57 and 58 of Resolution 111/06 in relation to the admission procedure of dispatching users of cogeneration production units to the recognition of dispatching priorities.

**Resolution ARG/elt 186/11**

By this provision, the Authority has determined the price, to supplement generation costs, in relation to 2009, for the plants owned by Enel Produzione S.p.A., essential to the security under the territorial scopes served by electricity grids with the obligation to connect of third parties, not interconnected with the National Transmission Grid. It has also asked Terna to publish the updated list of essential plants for the security of the electrical system, valid for 2009, including the essential plants above.

**Resolution ARG/elt 187/11**

By this provision, the Authority established amendments and supplements to Resolution ARG/elt 99/08 on the technical and economic conditions for connection to grids with obligation to connect third parties production plants (TICA), upon completion of the process undertaken with Resolution ARG/elt 73/11, aimed at reviewing the instruments, implemented in the Consolidated Act of Active Connections, aimed at overcoming the problem of the virtual saturation of the electricity grids. The main new features introduced by the provision can be summarised as follows:

a. payment for the production plants from renewable sources and cogeneration plants that must be connected to a critical line or a critical area, of a price for the booking of capacity by the applicant, other than the end customer, potentially in the form of bank surety and for the same amount as the product of power for the purpose of connection and €20.25 per kW, to be presented when the estimate is accepted. Alternative to paying the price, a first demand letter of guarantee of the Parent Company is also permitted.
   The price for booking capacity is also paid in the event of connection requests underway at the date of provision adoption, according to the times and methods detailed in the provision;
b. it regulates, in detail, hypothesised requests to alter an estimate that has already been accepted and the related assignment of costs connected with the release of the estimate between the grid operator and applicant;
c. update of the provisions relating to cogeneration to consider the new high performance cogeneration definition introduced by Italian Legislative Decree no. 20/07 and Ministerial Decree of 4 August 2011;
d. new provisions on automatic indemnity and related time frames.

**Resolution ARG/elt 189/11**

By this provision, the Authority positively checked the convention between Terna and the energy market operator and approved the related price and the other prices for 2012 connected with the participation in the market and platforms managed by GME.

**Resolution ARG/elt 196/11**

Review, in force as from 1 January 2012, of the conventional percentage factors of the losses of electricity on the grids with the obligation to connect third parties, pursuant to table 4 of Annex A to the Resolution by the Authority for Electricity and Gas no. 107/09 of 30 July 2009 (Settlement Code).

**Resolution ARG/elt 197/11**

By this provision, the Authority dictated provisions on the regulation of the quality of electricity transmission services for the regulatory period 2012-2015.

The provision confirms the premium/penalty mechanism for Terna already established by Resolution 341/07 for the previous regulatory period, making some changes. The main news concern the gradual application of this mechanism to the entire NTG (including Terna Rete Italia), its simplification through the use of the sole indicator of RENS (Reference Energy Not Supplied) and a different valuation of this. The obligation has also been introduced to monitor new transmission service quality indicators: Energy not supplied to MV or LV users (ENS-U) and energy collected by MV or LV users (ENR-U) following power failures of HV user sites of distributing companies.

Additionally, corrective measures were established in relation to the mitigation services.

**Resolution ARG/elt 199/11**

The provision, incorporating the provision of the electricity transmission, distribution and metering services for the regulatory period 2012-2015 and provision on the economic conditions for the supply of the connection service, contains three annexes:

- Annex A, incorporating the consolidated act of the provisions of the Authority for Electricity and Gas for the supply of electricity transmission and distribution services for the regulatory period 2012-2015 (hereinafter: TIT);
- Annex B, incorporating the consolidated act of the provisions of the Authority for Electricity and Gas for the supply of electricity metering services for the regulatory period 2012-2015 (hereinafter: TIME);
- Annex C, incorporating the consolidated act of the provisions of the Authority for Electricity and Gas of the economic conditions for the supply of the connection service (hereinafter: TIC).

The TIT defines the tariff rules for the fourth regulatory period 2012-2015 and the remuneration due to Terna for the supply of the transmission and metering services. Without prejudice to the recognition of the extra remuneration recognised by the regulation concerning development interventions already entered into operation as at the date of 31 December 2011, the Resolution introduces some changes to the incentive regime of the new NTG development interventions; more specifically, the Resolution recognises extra remuneration amounting to respectively 1.5% and 2% for the development work on the NTG belonging to types I2 and I3, recognised for a period of 12 years as from the date of the entry into operation of the investments, also reducing the scope of type I3 interventions to purely transport capacity development works in relation to strategic projects, namely aimed at reducing congestion between market zones or increasing net transfer capacity (NTC) on the electrical frontiers (in limited cases, previously approved by the AEEG, this type may also include other investment projects, as long as they are of primary strategic capacity) and introduces a new type I4 for investments in pilot projects relating to accumulation systems, for which an extra remuneration is recognised equal to that of type I3. Projects classed as category I4 will be selected according to a specific procedure defined with subsequent AEEG Provision.

With reference to the metering service, the Authority, despite referring to a subsequent provision to be issued during the IV regulatory period, the completion of the rationalisation process of the regulation of that service, has introduced into the TIME some changes with respect to the previous regulation, above all in the matter of assigning service responsibilities, with specific reference to the collection/registration and validation of energy collected from end customers on the NTG and energy exchange on interconnection points in addition to collection of measurements relating to input points on the NTG. To carry out those activities, TIME has consequently reviewed the methods by which this service is remunerated.

Finally, with regard to the TIC, with respect to the previous regulatory period, some news has been introduced in relation to the criteria by which the costs are divided up between grid operators in the event of requests for the development of plants for grid interconnection. In particular, it is established that in these cases, the operator developing the plant for interconnection obtains coverage of the costs incurred by means of the remuneration of investments envisaged by the TIT whilst the operator who does not develop the plant does not incur any costs.

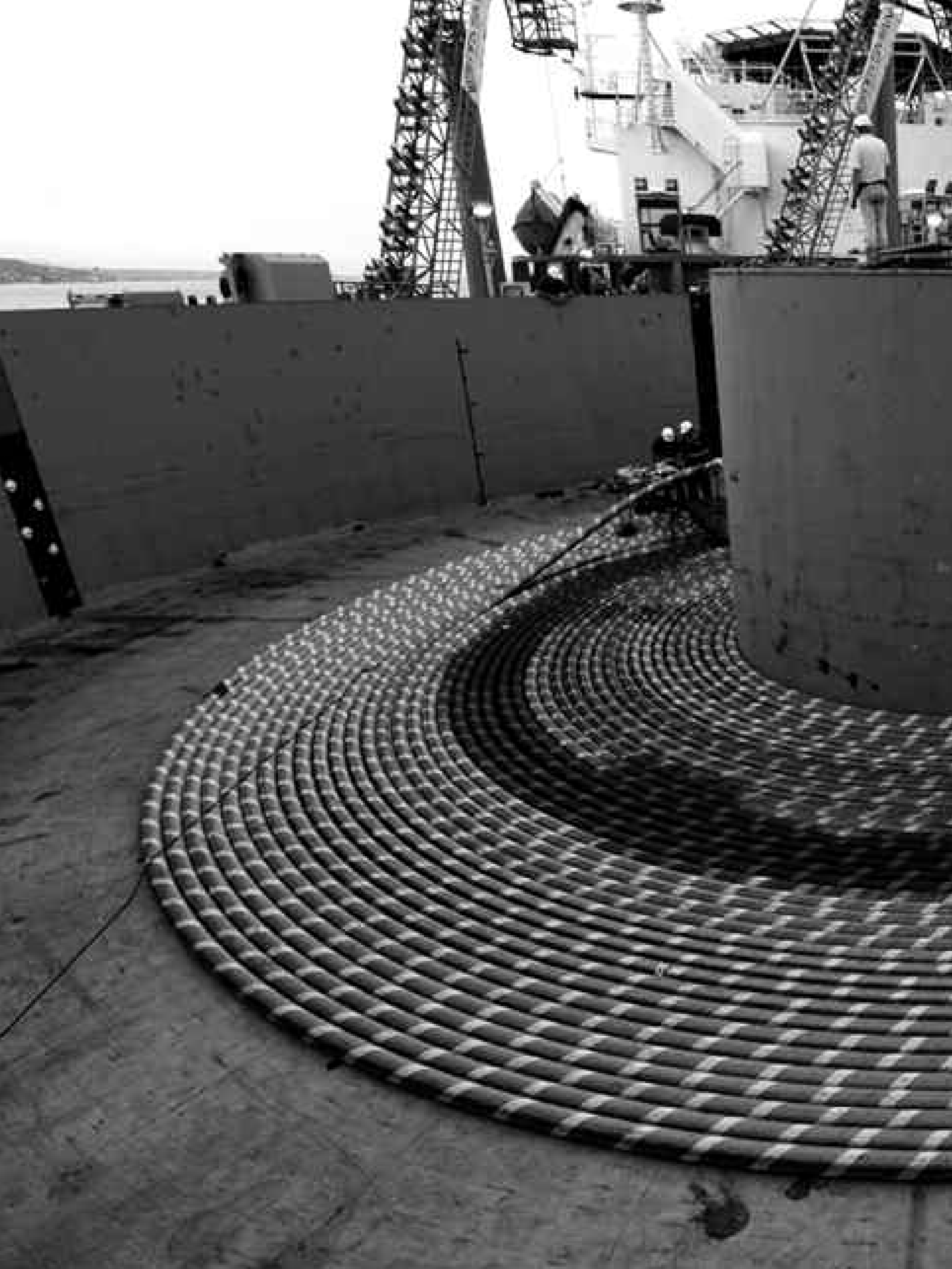
**Resolution ARG/elt 204/11**

By this provision, the Authority issued provisions aimed:

- at updating dispatching prices for 2012;
- at reviewing some provisions of Resolution 351/07 with reference to the methods by which to determine the price to cover costs recognised for Terna's operation for the regulatory period 2012-2015 (DIS);
- at reviewing some provisions of the Settlement Code and Resolution no. 111/06.

The Resolution specifies that the DIS price is calculated for 2012 considering, as specified by the provisions, the premiums (relative to 2010) for the forecasting of demand and forecasting of wind power production and the premiums relating to the incentives relating to the procurement of resources for the dispatching services. With specific reference to the remuneration criteria of the dispatching service, continuity is envisaged with the current regulations in force in the III regulatory period: valuation and remuneration of costs recognised (operating expenses, amortisation and depreciation and invested capital) will take place in accordance with that established for the transmission service.

The resolution in question has also made some changes to Resolution 111/06 and the provisions of the Settlement Code. In particular, the provision has established a change to the regulation of effective imbalances, amending the threshold to below that of imbalances for consumer units measured at MGP price rather than at the effective imbalance prices pursuant to Resolution 111/06. Lastly, with Resolution 204/11, the Authority approved the proposed integration of the Network Code made by Terna with regard to the methods by which to apply the settlement regulation in the event of a change to the ownership structure of the distribution grids.



# Consolidated financial statements

at 31 December 2011

Terna

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# Consolidated financial statements

# Consolidated income statement

| € million | Note | 2011 | 2010 |
|---|---|---|---|
| **A. Revenue** | | | |
| 1. Revenue from sales and services | 1 | 1,591.3 | 1,533.1 |
| *of which: related parties* | | *1,436.7* | *1,359.0* |
| 2. Other revenue and income | 2 | 44.3 | 56.1 |
| *of which: related parties* | | *0.8* | *2.7* |
| **Total revenue** | | **1,635.6** | **1,589.2** |
| **B. Operating expenses** | | | |
| 1. Raw materials and consumables | 3 | 20.7 | 28.2 |
| *of which: related parties* | | *0.0* | *0.1* |
| 2. Services | 4 | 149.0 | 152.2 |
| *of which: related parties* | | *4.2* | *7.5* |
| 3 Personnel expenses | 5 | 211.0 | 212.2 |
| *- gross personnel expenses* | | *278.6* | *276.5* |
| *- personnel expenses, capitalised* | | *(67.6)* | *(64.3)* |
| *of which: related parties* | | *2.8* | *3.6* |
| 4. Amortisation, depreciation and impairment | 6 | 396.3 | 360.7 |
| 5. Other operating expenses | 7 | 23.0 | 21.5 |
| *of which: related parties* | | *0.3* | *0.2* |
| **Total operating expenses** | | **800.0** | **774.8** |
| **A-B Operating profit (EBIT)** | | **835.6** | **814.4** |
| **C. Financial income/expense** | | | |
| 1. Financial income | 8 | 37.0 | 11.2 |
| 2. Financial expense | 8 | (165.4) | (116.3) |
| *of which: related parties* | | *(9.8)* | *(1.3)* |
| 3. Share of profit/(losses) of equity-accounted investees | 9 | 7.4 | 2.6 |
| **D. Profit before taxes** | | **714.6** | **711.9** |
| **E. Income taxes** | 10 | **387.3** | **246.8** |
| **F. Profit for the year from continuing operations** | | **327.3** | **465.1** |
| **G. Profit for the year from discontinued operations** | 11 | **112.7** | **146.9** |
| **H. Profit for the year** | | **440.0** | **612.0** |
| ***Profit for the year attributable to the owners of the Parent*** | | ***440.0*** | ***612.0*** |
| **Earnings per share** | | | |
| Basic earnings per share | 12 | 0.219 | 0.305 |
| Diluted earnings per share | | 0.219 | 0.304 |
| **Earnings per share from continuing operations** | | | |
| Basic earnings per share | 12 | 0.163 | 0.232 |
| Diluted earnings per share | | 0.163 | 0.231 |

# Consolidated statement of comprehensive income

| € million | Note | 2011 | 2010 |
|---|---|---|---|
| **Profit for the year** | | **440.0** | **612.0** |
| Other comprehensive income for the year | | | |
| - Cash flow hedges, net of tax effect of continuing operations | 23 | (34.7) | 25.9 |
| - Cash flow hedges, net of tax effect of discontinued operations | 23 | (16.0) | 16.0 |
| **Comprehensive income for the year** | | **389.3** | **653.9** |
| **Comprehensive income for the year attributable to:** | | **389.3** | **653.9** |
| *Owners of the Parent* | | *389.3* | *653.9* |

# Consolidated statement of financial position
## Assets

| € million | Note | At 31.12.2011 | At 31.12.2010 | At 01.01.2010 |
|---|---|---|---|---|
| **A. Non-current assets** | | | | |
| 1. Property, plant and equipment | 13 | 8,618.2 | 7,802.6 | 6,989.9 |
| *of which: related parties* | | *24.3* | *39.0* | *30.3* |
| 2. Goodwill | 14 | 190.2 | 190.2 | 190.2 |
| 3. Intangible assets | 15 | 280.7 | 280.4 | 267.4 |
| 4. Equity-accounted investees | 16 | 66.8 | 23.6 | 15.5 |
| 5. Non-current financial assets | 17 | 522.4 | 200.8 | 123.2 |
| 6. Other non-current assets | 18 | 6.6 | 6.3 | 5.5 |
| **Total non-current assets** | | **9,684.9** | **8,503.9** | **7,591.7** |
| **B. Current assets** | | | | |
| 1. Inventories | 19 | 16.3 | 11.4 | 11.7 |
| 2. Trade receivables | 20 | 1,690.2 | 1,495.8 | 1,169.1 |
| *of which: related parties* | | *122.5* | *153.7* | *120.8* |
| 3. Current financial assets | 17 | 155.5 | 0.5 | 501.0 |
| *of which: related parties* | | *0.4* | *0.4* | *0.5* |
| 4. Cash and cash equivalents | 21 | 1,114.9 | 150.1 | 0.1 |
| 5. Income tax assets | 22 | 4.4 | 4.2 | 4.2 |
| 6. Other current assets | 18 | 20.5 | 20.3 | 27.6 |
| *of which: related parties* | | *0.0* | *0.8* | *1.5* |
| **Total current assets** | | **3,001.8** | **1,682.3** | **1,713.7** |
| **C. Discontinued operations held for sale** | | **0.0** | **575.8** | **0.1** |
| **Total assets** | | **12,686.7** | **10,762.0** | **9,305.5** |

# Consolidated statement of financial position
## Liabilities

| € million | Note | At 31.12.2011 | At 31.12.2010 | At 01.01.2010 |
|---|---|---|---|---|
| **D. Equity attributable to the owners of the Parent** | | | | |
| 1. Share capital | | 442.2 | 441.0 | 440.2 |
| 2. Other reserves | | 766.9 | 791.0 | 758.7 |
| 3. Reserves for assets held for sale | | 0.0 | 16.0 | 0.0 |
| 4. Retained earnings | | 1,262.7 | 1,073.6 | 671.7 |
| 5. Interim dividend | | (160.8) | (160.4) | (140.1) |
| 6. Profit for the year | | 440.0 | 612.0 | 785.2 |
| **Total equity attributable to owners of the Parent** | 23 | **2,751.0** | **2,773.2** | **2,515.7** |
| **E. Equity attributable to non-controlling interests** | | **0.0** | **0.2** | **0.0** |
| **Total equity** | | **2,751.0** | **2,773.4** | **2,515.7** |
| **F. Non-current liabilities** | | | | |
| 1. Long-term loans | 24 | 6,738.7 | 5,147.5 | 4,199.2 |
| *of which: related parties* | | *500.0* | *0.0* | *0.0* |
| 2. Employee benefits | 25 | 119.2 | 122.3 | 125.1 |
| 3. Provisions for risks and charges | 26 | 193.8 | 171.6 | 149.4 |
| 4. Deferred tax liabilities | 27 | 251.8 | 305.1 | 335.4 |
| 5. Non-current financial liabilities | 24 | 111.4 | 47.1 | 82.6 |
| 6. Other non-current liabilities | 28 | 137.1 | 141.8 | 151.6 |
| **Total non-current liabilities** | | **7,552.0** | **5,935.4** | **5,043.3** |
| **G. Current liabilities** | | | | |
| 1. Short-term loans | 24 | 0.0 | 73.1 | 40.0 |
| 2. Current portion of long-term loans | 24 | 59.7 | 59.7 | 59.7 |
| 3. Trade payables | 29 | 2,029.8 | 1,542.2 | 1,482.0 |
| *of which: related parties* | | *44.9* | *55.7* | *39.3* |
| 4. Tax liabilities | 29 | 116.5 | 69.6 | 44.0 |
| 5. Current financial liabilities | 24 | 40.1 | 24.2 | 25.5 |
| *of which: related parties* | | *2.4* | *2.4* | *1.2* |
| 6. Other current liabilities | 29 | 137.6 | 135.7 | 95.3 |
| *of which: related parties* | | *7.3* | *7.8* | *4.6* |
| **Total current liabilities** | | **2,383.7** | **1,904.5** | **1,746.5** |
| **H. Liabilities from discontinued operations and assets held for sale** | | **0.0** | **148.7** | **0.0** |
| **Total liabilities and equity** | | **12,686.7** | **10,762.0** | **9,305.5** |

# Statement of changes in consolidated equity

| 31 DECEMBER 2011 - 31 DECEMBER 2010 | CONSOLIDATED SHARE CAPITAL AND RESERVES | | | |
|---|---|---|---|---|
| € million | Share/quota capital | Legal reserve | Share premium reserve | Hedging reserve |
| **Equity at 31 December 2010** | **441.0** | **88.0** | **8.6** | **(35.3)** |
| **Profit for the year** | | | | |
| **Other comprehensive income:** | | | | |
| Change in fair value of derivatives and cash flow hedges, net of tax effect | | | | (34.7) |
| **Total other comprehensive income** | **0.0** | **0.0** | **0.0** | **(34.7)** |
| **Comprehensive income** | **0.0** | **0.0** | **0.0** | **(34.7)** |
| **Transactions with equity owners:** | | | | |
| Allocation of 2010 profit | | | | |
| *Retained earnings* | | *0.2* | | |
| *Dividends* | | | | |
| Exercise of stock options | 1.2 | | 11.4 | |
| 2011 interim dividend | | | | |
| **Total transactions with equity owners** | **1.2** | **0.2** | **11.4** | **0.0** |
| Other changes | | | | |
| **Equity at 31 December 2011** | **442.2** | **88.2** | **20.0** | **(70.0)** |

| 31 DECEMBER 2009 - 31 DECEMBER 2010 | CONSOLIDATED SHARE CAPITAL AND RESERVES | | | |
|---|---|---|---|---|
| € million | Share/ quota capital | Legal reserve | Share premium reserve | Hedging reserve |
| **Equity at 31 December 2009** | **440.2** | **88.0** | **1.8** | **(61.2)** |
| **Adjustment of opening balances** | | | | |
| **Equity at 31 December 2009** | **440.2** | **88.0** | **1.8** | **(61.2)** |
| **Profit for the year** | | | | |
| **Other comprehensive income:** | | | | |
| Change in fair value of derivatives and cash flow hedges, net of tax effect | | | | 25.9 |
| **Total other comprehensive income** | **0.0** | **0.0** | **0.0** | **25.9** |
| **Comprehensive income** | **0.0** | **0.0** | **0.0** | **25.9** |
| **Transactions with equity owners:** | | | | |
| Allocation of 2009 profit | | | | |
| *2009 dividend* | | | | |
| *2009 retained earnings* | | | | |
| Exercise of stock options | 0.8 | | 6.8 | |
| 2010 interim dividend | | | | |
| **Total transactions with equity owners** | **0.8** | **0.0** | **6.8** | **0.0** |
| **Other changes** | | | | |
| **Equity at 31 December 2010** | **441.0** | **88.0** | **8.6** | **(35.3)** |

| Equity investments in assets held for sale | Other reserves | Retained earnings | Interim dividend | Profit for the year | Equity attributable to the owners of the Parent | Equity attributable to non-controlling interests | Total equity |
|---|---|---|---|---|---|---|---|
| **16.0** | **729.7** | **1,073.6** | **(160.4)** | **612.0** | **2,773.2** | **0.2** | **2773.4** |
| | | | | **440.0** | **440.0** | | **440.0** |
| | | | | | | | |
| (16.0) | | | | | (50.7) | | (50.7) |
| **(16.0)** | **0.0** | **0.0** | **0.0** | **0.0** | **(50.7)** | | **(50.7)** |
| **(16.0)** | **0.0** | **0.0** | **0.0** | **440.0** | **389.3** | **0.0** | **389.3** |
| | | | | | | | |
| | | *190.1* | *160.4* | *(350.7)* | *0.0* | | *0.0* |
| | | | | *(261.3)* | *(261.3)* | | *(261.3)* |
| | (1.0) | | | | 11.6 | | 11.6 |
| | | | (160.8) | | (160.8) | | (160.8) |
| **0.0** | **(1.0)** | **190.1** | **(0.4)** | **(612.0)** | **(410.5)** | **0.0** | **(410.5)** |
| | | (1.0) | | | (1.0) | (0.2) | (1.2) |
| **0.0** | **728.7** | **1,262.7** | **(160.8)** | **440.0** | **2,751.0** | **0.0** | **2,751.0** |

| Equity investments in assets held for sale | Other reserves | Effect of foreign currency trans. | Retained earnings | Interim dividend | Profit for the year | Equity attributable to the owners of the Parent | Equity attributable to non-controlling interests | Total equity |
|---|---|---|---|---|---|---|---|---|
| **0.0** | **730.1** | **0.0** | **671.7** | **(140.1)** | **771.0** | **2,501.5** | **0.0** | **2,501.5** |
| | | | | | **14.2** | **14.2** | | **14.2** |
| **0.0** | **730.1** | **0.0** | **671.7** | **(140.1)** | **785.2** | **2,515.7** | **0.0** | **2,515.7** |
| | | | | | **612.0** | **612.0** | | **612.0** |
| | | | | | | | | |
| 16.0 | | | | | | 41.9 | | 41.9 |
| **16.0** | **0.0** | **0.0** | **0.0** | **0.0** | **0.0** | **41.9** | | **41.9** |
| **16.0** | **0.0** | **0.0** | **0.0** | **0.0** | **612.0** | **653.9** | **0.0** | **653.9** |
| | | | | | | | | |
| | | | | *140.1* | *(380.5)* | *(240.4)* | | *(240.4)* |
| | | | *404.7* | | *(404.7)* | *0.0* | | *0.0* |
| | (0.4) | | | | | 7.2 | | 7.2 |
| | | | | (160.4) | | (160.4) | | (160.4) |
| **0.0** | **(0.4)** | **0.0** | **404.7** | **(20.3)** | **(785.2)** | **(393.6)** | **0.0** | **(393.6)** |
| | | | **(2.8)** | | | **(2.8)** | **0.2** | **(2.6)** |
| **16.0** | **729.7** | **0.0** | **1,073.6** | **(160.4)** | **612.0** | **2,773.2** | **0.2** | **2,773.4** |

# Consolidated statement of cash flows (*)

| € million | 2011 | 2010 |
|---|---|---|
| **Profit for the year** | **440.0** | **612.0** |
| ***of which from discontinued operations and assets held for sale - Rete Rinnovabile*** | ***50.6*** | ***146.8*** |
| ***of which from discontinued operations and assets held for sale - NRTS*** | ***28.3*** | ***0.0*** |
| **Adjustments for:** | | |
| Amortisation, depreciation, impairment losses/(reversals of impairment losses) on property, plant and equipment and intangible assets (**) | 385.5 | 351.4 |
| Provisions (including employee-related provisions) and impairment losses | 94.1 | 63.5 |
| (Gains)/Losses on disposals of property, plant and equipment | (3.6) | (3.1) |
| Financial (income)/expenses | 129.6 | 99.5 |
| Income taxes | 388.3 | 249.2 |
| **Cash flows generated by operating activities, before changes in net working capital** | **1,433.9** | **1,372.5** |
| Increase/(Decrease) in provisions (including employee-related and tax provisions) | (91.1) | (39.4) |
| (Increase)/Decrease in inventories | (4.9) | 0.3 |
| (Increase)/Decrease in trade receivables and other current assets | (168.2) | (347.7) |
| Increase/(Decrease) in other non-current liabilities | 6.0 | (0.3) |
| (Increase)/Decrease in other non-current assets | (413.2) | (187.0) |
| Increase/(Decrease) in trade payables and other current liabilities | 568.5 | 333.7 |
| Interest income and other financial income received | 91.3 | 109.1 |
| Interest expense and other financial expense paid | (218.5) | (212.1) |
| Income taxes paid | (354.7) | (255.7) |
| **Cash flows generated by operating activities [a]** | **849.1** | **773.4** |
| Investments in property, plant and equipment, net of grants received | (1,166.0) | (1,092.2) |
| Recognition of acquired companies' property, plant and equipment | 0.0 | (43.4) |
| Revenue from sale of property, plant and equipment and intangible assets | 8.6 | 4.7 |
| Investment in intangible assets, net of grants received | (51.1) | (58.1) |
| Construction contracts and assets held for sale | 0.0 | (503.5) |
| Goodwill of discontinued operations and assets held for sale | 0.0 | (1.4) |
| Net deconsolidation of discontinued operations and assets held for sale - Rete Rinnovabile | 404.9 | 0.0 |
| Increase in equity interests in associates | (43.2) | (8.1) |
| Acquisition of equity investments | (0.1) | (0.5) |
| Investment in discontinued operations | 0.0 | 0.1 |
| **Cash flows used in investing activities [b]** | **(846.9)** | **(1,702.4)** |
| Capital increase | 1.2 | 0.8 |
| Increase of reserves | 10.4 | 6.4 |
| Increase/(Decrease) in net income and accumulated losses | (1.0) | (2.8) |
| Dividends paid | (422.1) | (400.8) |
| Equity attributable to non-controlling interests in discontinued operations and assets held for sale - Rete Rinnovabile | (0.2) | 0.2 |
| Change in short- and medium/long-term financial payables (including short-term portions) (***) | 1,772.7 | 981.4 |
| Change in short-term financial investments | (150.0) | 500.0 |
| Deconsolidation of financial debt of discontinued operations and assets held for sale - Rete Rinnovabile | (254,6) | (0.0) |
| **Cash flows generated by financing activities [c]** | **956.4** | **1,085.2** |
| **Increase/(Decrease) in cash and cash equivalents [a+b+c]** | **958.6** | **156.2** |
| ***of which change in cash and cash equivalents for discontinued operations and assets held for sale - Rete Rinnovabile*** | ***(6.2)*** | ***6.2*** |
| Opening cash and cash equivalents | 156.3 | 0.1 |
| Closing cash and cash equivalents | 1,114.9 | 156.3 |

(*) For comments on the Consolidated statement of cash flows, please see the section "Notes to the statement of cash flows" in the "Notes to the financial statements".
(**) Net of set-up grants taken to income statement for the year.
(***) Net of FVH derivatives. The change takes into account the net credit position of Terna S.p.A. towards Rete Rinnovabile S.r.l. at 31 December 2010 (amounting to €254.6 million).

# Notes to the consolidated financial statements

# A. Accounting policies and measurement criteria

## Introduction

Terna S.p.A. has registered offices in Viale Egidio Galbani 70, Rome, Italy. Its consolidated financial statements at and for the year ended 31 December 2011 include its separate financial statements and those of its subsidiaries (the “Group”), as well as the Group’s shareholding in associates and joint ventures. The subsidiaries included within the scope of consolidation are listed below. These consolidated financial statements have been authorized for publication by the Directors on 20 March 2012.
The consolidated financial statements as at and for the year ended 31 December 2011 are available upon request within the registered office of the company Terna S.p.A., Viale Egidio Galbani, 70 Rome or at the website www.terna.it.

## Compliance with IAS/IFRS

The consolidated financial statements as of 31 December 2011 have been prepared in accordance with International Financial Reporting Standards (IFRS), International Accounting Standards (IAS) issued by the International Accounting Standards Board (IASB) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and the Standing Interpretations Committee (SIC), endorsed by the European Commission (IFRS-EU) at that date.
These consolidated financial statements have also been prepared by taking into account the provisions of Legislative Decree no. 38 of 28 February 2005, the Italian Civil Code and CONSOB Resolutions nos. 15519 (“Provisions governing financial statements in implementation of Art. 9, paragraph 3, of Legislative Decree no. 38/2005”) and 15520 (“Amendments to the implementing rules for Legislative Decree no. 58/1998”), both of 27 July 2006, as well as CONSOB Communication no. DEM/6064293 of 28 July 2006 (“Disclosure requirements for listed issuers and issuers of financial instruments that are widely held among the public and pursuant to Art. 116 of the Consolidated Financial Act”).
The consolidated financial statements have been prepared on a historic cost basis, modified where necessary for certain financial instruments, as well as on a going concern basis. The Group has determined that, despite the challenging economic and financial environment, it does not face material uncertainties (as defined in paragraph 25 of IAS 1) that might cast doubt on its ability to continue as a going concern.

## Basis of presentation

The consolidated financial statements are composed of the statement of financial position, the income statement, the statement of cash flows, the statement of changes in equity and the notes thereto.
In the statement of financial position, assets and liabilities are classified on a “current/non-current” basis, with separate reporting of assets and liabilities held for sale. Current assets, which include cash and cash equivalents, are those held for realisation, sale or consumption in the Group’s normal operating cycle; current liabilities are those expected to be settled in the Group’s normal operating cycle or within one year from the close of the financial year.
The income statement is classified on the basis of the nature of costs. The income statement is presented as two statements, the first of which (income statement) presents the components of profit or loss for the year; while the second (statement of comprehensive income) starts with the result for the year and then presents the revenue and expense items (including reclassification adjustments) that are recognised in equity rather than profit or loss for the year.
The statement of cash flows has been prepared using the indirect method.
The consolidated financial statements are accompanied by the Directors’ Report on Operations for Terna S.p.A. and the Terna Group, which as from the 2008 financial year has been prepared as a single document, exercising the option granted under Legislative Decree no. 32 of 2 February 2007, which amended Art. 40 (Directors’ Report on Operations) of Legislative Decree no. 127 of 9 April 1991.
In the balance sheet, assets and liabilities are classified on a “current/non-current” basis, with specific mention of assets and liabilities held for sale. Current assets, which include cash and cash equivalents, are those held for realisation, sale or consumption in the Group’s normal operating cycle. Current liabilities are those expected to be settled in the Group’s normal operating cycle or within one year from the close of the financial year.
These consolidated financial statements are presented in millions of euros, and all figures are shown in millions of euros, unless otherwise indicated.
The financial statements have been prepared using the historic cost method, with the exception of captions that are recognised at fair value in accordance with IFRS-EU, as indicated in the accounting policies for each caption.

It is specified that some comparative balances of the financial statements as of 31 December 2010 have been adjusted to consider the change in the accounting model of the effects arising from the decision taken by Terna S.p.A. in financial year 2009, to adhere to the release of the goodwill established by Italian Law Decree no. 185 of 29 November 2008, converted into Italian Law no. 2 of 28 January 2009. The change from the substitute tax model recorded as an advance on current taxes to the substitute tax model recorded by recognising deferred tax assets has, therefore, entailed the recording as of 31 December 2010 of greater deferred tax assets (classified amongst net deferred tax liabilities) for an amount of €25.2 million and lower tax assets for €12.6 million, with an impact of €14.2 million recorded as retained earnings and €1.6 million as lower result (greater current taxes) under the shareholders' equity as of 31 December 2010.

## Use of estimates

The preparation of the consolidated financial statements requires the use of estimates and assumptions that affect the book values of assets and liabilities and related disclosures, in addition to contingent assets and liabilities at the reporting date. The estimates and associated assumptions are based on previous experience and various factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed periodically and the effects of any changes are recognised in the income statement for the year, if they relate solely to that period. In the case that the revision affects both current and future years, the change is recorded in the year in which the estimate is reviewed as well as in the relative future years.
The critical areas for key estimates and assumptions used by management in applying the IFRS endorsed by the European Commission that could have significant effects on the consolidated financial statements or that could give rise to risks that would entail significant adjustments to the book values of assets and liabilities in subsequent years are summarised below.

### Employee benefits

The liability for employee benefits paid upon or following termination of employment in relation to defined benefit plans or other long-term benefits is recognised net of any plan assets and is measured on the basis of actuarial assumptions, estimating the amount of future benefits that employees have vested at the reporting date.

### Provisions for risks and charges

Accruals to the Provisions for risks and charges are recognised when, at the reporting date, there is a legal or constructive obligation as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the financial effect of the passage of time is material, accruals are measured by discounting the estimated outflow at a pre-tax discount rate that reflects current market assessments of the time value of money and, if applicable, the risks specific to the liability. Any increase in provisions associated with the passage of time is taken to the income statement under "Financial expenses".

### Allowance for impairment accounts

Trade receivables are initially recognised at fair value net of any impairment losses relating to sums considered non recoverable, which are taken to the specific allowance for impairment. Impairment losses are measured on the basis of the present value of estimated future cash flows, discounted at the original effective interest rate.

### Recoverable amount of non-current assets

Property, plant and equipment and intangible assets are analysed at least once a year to check for indications of impairment. If there is an indication that an asset may be impaired, its recoverable amount is estimated.
Recoverable amount is the higher of an asset's fair value, net of costs to sell and its value in use, measured by discounting estimated future cash flows considering available information at the time of estimate and on the basis of subjective assessments of the performance of future variables - such as prices, costs, demand growth rates, production profiles - and discounted at a rate that reflects current market assessments of the time value of money with respect to the investment period and the risks specific to the asset.

## Subsidiaries and the scope of consolidation

The scope of consolidation includes the Parent Company Terna S.p.A. and the companies over which the Parent Company has the power to directly or indirectly govern financial and operating policies so as to obtain benefits from their activities, regardless of the type of ownership. In assessing whether or not the Parent Company has control, potential voting rights that are presently exercisable or convertible are also considered.

The financial statements of subsidiaries are included in the consolidated financial statements on a line-by-line basis from the date when the Parent Company gains control until the date when such control ceases.
The companies included within the scope of consolidation are listed below:

| Company | Registered office | Assets | Currency | Share/quota capital | % held | Consolidation method |
|---|---|---|---|---|---|---|
| COMPANIES CONTROLLED DIRECTLY BY TERNA S.P.A. | | | | | | |
| **Terna Rete Italia S.r.l.** | Rome | Design, construction, management, development, operation and maintenance of high-voltage power lines. | € | 243,577,554 | 100% | Line-by-line |
| **Terna Crna Gora d.o.o.** | Podgorica | Authorisation, construction and management of transmission infrastructures comprising the Italy-Montenegro electrical interconnection in Montenegro territory. | € | 2,000,000 | 100% | Line-by-line |
| **SunTergrid S.p.A.** | Rome | Construction and maintenance of electricity transmission grids and plants for the generation of electricity, including renewables generation, for own use and sale in Italy and abroad. | € | 120,000 | 100% | Line-by-line |
| **Terna Plus S.r.l.** | Rome | Design, construction, management, development, operation and maintenance of plants, equipment and infrastructures including grids and systems, including diffused energy storage, pumping and/or storage. | € | 50,000 | 100% | Line-by-line |
| COMPANIES CONTROLLED THROUGH SUNTERGRID S.P.A. | | | | | | |
| **Rete Solare S.r.l.** | Rome | Construction and maintenance of electricity transmission grids and plants for the generation of electricity, including renewables generation, for own use and sale in Italy and abroad. | € | 10,000 | 100% | Line-by-line |

The **change in the scope of consolidation** since 31 December 2010 relates to:

- on 8 March 2011, the subsidiary SunTergrid S.p.A. incorporated the company named Nuova Rete Solare S.r.l., which, delegated as part of the Terna Group to the development of the new renewable energy investment programme ("New photovoltaic project"), during the period purchased all shares in three companies, again operating in the sector of non-conventional energies: on 18 May 2011, Reno Solar 2 S.r.l.; on 1 June 2011, Lira PV S.r.l.; on 7 June 2011, Solar Margherita S.r.l.. In September 2011, the three companies merged into the subsidiary NRTS. The company was subsequently sold on 24 October 2011, by the subsidiary SunTergrid S.p.A. to RTR Holding III S.r.l. (the "Buyer") - an indirect subsidiary of Terra Firma Capital Partners III, L.P. ("Terra Firma") through RTR Capital S.r.l.. With reference to the general income generated by the sale of NRTS, please refer to note no. 11 to the financial statements "Net profit for the financial year from discontinued operations and assets held for sale";
- the completion of the sale, on 31 March 2011, by the subsidiary SunTergrid S.p.A., of the companies Rete Rinnovabile S.r.l. (hereinafter "RTR S.r.l.") and Valmonte Energia S.r.l. to RTR Acquisition S.r.l. (an indirect subsidiary of Terra Firma Investment (GP) 3 Limited). With reference to the income for the financial year generated by the sale of said companies, please refer to note no. 11 to the financial statements "Net profit for the financial year from discontinued operations and assets held for sale";
- Terna's establishing, on 22 June 2011, of the company named "Terna Crna Gora d.o.o." (hereinafter "Terna CG"), limited liability company incorporated under the laws of Montenegro, in charge of carrying out the activities relating to the authorisation, construction and management of the transmission infrastructures comprising the Italy-Montenegro electrical interconnection in Montenegro territory, with initial share capital of €2,000,000;

- the incorporation by Terna, on 15 December 2011, of a company named “Terna Plus S.r.l.”, limited liability company in charge of designing, constructing, managing, developing, operating and maintaining systems, equipment and infrastructures, including grids and systems, including the diffused accumulation of energy and pumping and/or storage and with share capital of €50,000;
- the resolution on 21 December 2011, by the Shareholders’ Meeting of Terna Linee Alta Tensione S.r.l. (“TELAT S.r.l.”) to change the company name to “Terna Rete Italia S.r.l.”.

### Associates

Investments in associates are those over which the Terna Group has significant influence but which are neither subsidiaries nor joint ventures. In assessing whether or not Terna has a significant influence, potential voting rights that are presently exercisable or convertible are also considered.
These investments are initially recognised at acquisition cost and subsequently measured using the equity method. The profits or the losses pertaining to the Group are recognised within the consolidated financial statements when it begins to exercise significant influence and until that influence ceases.
In the event that the loss pertaining to the Group exceeds the equity interest’s book value, the latter is written off and any excess is recognised in a specific provision in the case that the Parent Company is required to meet the legal or constructive obligations of the subsidiary or, in any case, to cover its losses.

### Joint ventures

Investments in jointly-controlled entities, in which the Group exercises joint control of other entities, are recognised initially at cost and subsequently measured using the equity method. The profits or the losses pertaining to the Group are recognised within the consolidated financial statements when it begins to exercise significant influence and until that influence ceases.
In assessing whether or not the Parent Company has a joint interest, potential voting rights that are presently exercisable or convertible are also considered.

| Company | Registered office | Assets | Currency | Share/quota capital | % held | Consolidation method |
|---|---|---|---|---|---|---|
| ASSOCIATES | | | | | | |
| CESI S.p.A. | Milan | Experimental electro-technical research. | € | 8,550,000 | 42.41% | Equity Method |
| CORESO S.A. | Brussels (Belgium) | Technical centre owned by various electrical energy transmission companies which implements joint TSO technical coordination activities in order to improve and strengthen security and coordination of the electrical system in central/western Europe. It prepares daily forecasts and analyses in real time on energy flows in the region, identifying potentially critical areas and promptly informing any affected TSO’s. | € | 1,000,000 | 22.49% | Equity Method |
| CGES A.D. | Podgorica | Electricity dispatch and transmission operator in Montenegro. | € | 155,108,283 | 22.09% | Equity Method |
| JOINT VENTURES | | | | | | |
| ELMED Études Sarl | Tunis | Analysis and preliminary consulting for the preparation of tender documentation of the Tunisian government for construction tenders and the management of the electricity generation site in Tunisia involved in the project for the interconnection of Italy and Tunisia. | Tunisian Dinar | 2,700,000 | 50% | Equity Method |

## Consolidation policies

All financial statements of subsidiaries used to prepare the consolidated financial statements were drafted as of 31 December 2011, with the exception of the subsidiary SunTergrid, which closed the financial year as of 31 October 2011, and have been approved by their respective assemblies; they have been adjusted, where necessary, to align them with the Parent Company's accounting policies.
During the preparation of the consolidated financial statements, intercompany balances, transactions, revenue and costs are fully eliminated, net of the related tax effect, where material ("consolidation on a line-by-line basis").
Unrealised gains and losses with associates and joint ventures are eliminated in proportion to the Group's holding therein. In both cases, unrealised losses are eliminated, unless they represent impairment.

## Translation of foreign currency items

The financial statements of each consolidated company are prepared using the functional currency for the economic environment in which each company operates.
In these financial statements, all transactions in currencies other than the functional currency are recognised at the exchange rate prevailing on the date of the transaction. Monetary assets and liabilities in currencies other than the functional currency are subsequently adjusted at the exchange rate prevailing at year end. Any exchange rate differences are taken to profit or loss.
Non-monetary assets and liabilities in foreign currency stated at historic cost are converted at the exchange rate prevailing when the transaction was initially recognised. Non-monetary assets and liabilities in foreign currency stated at fair value are converted at the exchange rate prevailing when fair value was measured.

## Translation of financial statements of foreign operations

For the purposes of the consolidated financial statements, profits and losses, assets and liabilities are expressed in euros, which is the Parent Company Terna S.p.A.'s functional currency.
For the purposes of drafting the consolidated financial statements, the financial statements of subsidiaries with a functional currency other than the euros, including goodwill and consolidation adjustments, are converted into euros at the exchange rate prevailing at the reporting date. Income statement figures included in these financial statements are converted at the average exchange rate of the year. Any resulting exchange rate differences are taken to "Other comprehensive income", and are classified separately in a specific equity reserve. This reserve is then released to profit or loss when the shareholding is sold.

## Business combinations

All business combinations, including acquisitions of minority interests in entities over which control is already held, are recognised using the purchase method, where purchase cost is equal to the fair value, at the date of exchange, of assets sold and liabilities incurred or assumed, plus any costs directly attributable to the combination. This cost is allocated by recognising the identifiable assets, liabilities and contingent liabilities of the acquired business at fair value. If the purchase cost exceeds the fair value of net assets acquired and attributable to the Group, this excess amount is recognised as goodwill or, if negative, booked to the income statement, after having verified once again that the current values of assets acquired and liabilities assumed and the purchase price have been measured correctly.
Decreases in non-controlling interests, following sale or dilution, in subsidiaries, without losing control, are booked as capital transactions (or transactions with shareholders in their office as shareholders). In these circumstances, the book values of the majority and minority shares must be adjusted to reflect the changes in their respective interests in the subsidiary. Any difference between the value adjusted for non-controlling interests and the fair value of the price received must be recognised directly to shareholder's equity.

## Property, plant and equipment

Property, plant and equipment are recognised at historic cost, including costs directly attributable to putting the asset in the condition necessary for it to be capable of operating in the manner for which it was acquired. In the event of legal or constructive obligations, cost also includes the present value of the estimated cost of disposal or removal of the asset. The corresponding liability is recognised in the Provisions for risks and charges. Borrowing costs directly attributable to the acquisition, construction or production of an asset that qualify for capitalisation pursuant to IAS 23R are capitalised as part of the cost of the asset. For more information, please see the section "Financial income and expense" below. Costs incurred after purchase are recognised as an increase in the carrying amount of the asset to which they relate if it is probable that the future benefits of that cost will flow to the Company and if the cost can be reliably measured. All other costs are recognised in profit or loss when incurred.
Each element of an item of property, plant and equipment of material value, with respect to the total value of the item to which it belongs, is recognised and depreciated separately.
Certain assets that were revaluated at 1 January 2005 (transition date) or previously are recognised at the revaluated amount, which is considered the deemed cost at the date of the revaluation.
Property, plant and equipment are shown net of accumulated depreciation and any impairment losses, which are measured as described below. Depreciation is calculated on a straight-line basis over the estimated useful economic life of the asset, which is reviewed annually, with revisions applied on a prospective basis. The depreciation of assets begins when the assets become available for use.
Liabilities associated with items of property, plant and equipment are taken to a specific provision as a balancing entry to the related asset. The amount is taken to profit or loss through the depreciation of the asset.

The main depreciation rates calculated on the basis of the related asset's useful life are as follows:

DEPRECIATION RATES

| | |
|---|---|
| Civil and industrial buildings | 2.50% |
| Transmission lines | 2.50% |
| | |
| Transformer stations: | |
| - Electrical machinery | 2.38% |
| - Electrical devices and equipment | 3.13% |
| - Automation and control systems | 6.70% |
| | |
| Central systems for remote management and control: | |
| - Devices, electrical equipment and ancillary plants | 5.00% |
| - Electronic calculation equipment | 10.00% |
| | |
| Solar power plants: | |
| - Buildings | 5.00% |
| - Electrical machinery | 5.00% |
| - Devices, electrical equipment and ancillary plants | 5.00% |
| - Panels and support structures | 5.00% |
| - Inverters | 10.00% |
| - Automation and control systems | 6.66% |

Land, regardless of whether it is free of construction or related to civil and industrial buildings, is not depreciated, since it has an indefinite useful life.
Property, plant and equipment acquired under finance leases – and through which the Group has substantially acquired all the risks and rewards of ownership – are recognised as Group assets at the lower of fair value and the present value of minimum lease payments due, including any amounts to be paid to exercise the purchasing option. The corresponding liability to the lessor is recognised under financial payables. Assets are depreciated using the criteria and rates described above. If the company is not reasonably certain that it will acquire ownership at the end of the lease, the asset is depreciated over the shorter of the term of the lease and the asset's useful life.
Leases in which the lessor maintains substantially all the risks and rewards of ownership are classified as operating leases. Costs related to operating leases are taken in full to profits or losses over the term of the lease.

## Intangible assets

Intangible assets, which all have finite useful lives, are recognised at cost, having obtained, if necessary, the approval of the Board of Statutory Auditors, and shown net of accumulated amortisation and any impairment losses, measured as described below.
Amortisation begins when the asset becomes available for use and is calculated on a straight-line basis over the estimated useful life of the related asset, which is reviewed annually. Any revisions to estimated figures are applied on a prospective basis.

Intangible assets essentially regard the exclusive license to carry out electricity transmission and dispatching activities and other intangible assets. In particular, Terna S.p.A. obtained the license for electricity transmission and dispatching activities in Italy on 1 November 2005 when it acquired the TSO business unit. As established in the Decree issued by the Ministry of Productive Activities on 20 April 2005, this license runs for twenty-five years, renewable for another twenty-five years, from the date of effective transfer of the activities, functions, assets and legal arrangements of the concession from GSE (formerly GRTN) to Terna S.p.A.. This intangible asset was initially recognised at cost, which reflected fair value.

Other intangible assets mainly relate to the following:
- the development and innovation of application software to manage the electricity invoicing process;
- the development and innovation of application software to protect the electrical system;
- software applications related to the development of the Power Exchange, particularly relating to the registration of operators, consumption units and the development of foreign procedures.

Development costs are capitalised by the Group only if all following conditions are met: costs can be reliably estimated and there are technical possibilities and intent to complete the intangible asset so as for it to be available after use; the asset can be used and it is possible to demonstrate that it will generate probable future economic benefits.
Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset pursuant to IAS 23R are capitalised as part of the cost of the asset. For more information, please see the section "Financial income and expense" below.
All other development costs and research expenses are recognised in profit or loss when incurred.
These intangible assets are amortised over their estimated residual useful life, which is normally three years, given their rapid obsolescence.

### Rights on the infrastructure

IFRIC 12 – Service Concession Arrangements (also "Interpretation") came into force on 1 January 2010. IFRIC 12 specifies the accounting treatment of service concession arrangements, not expressly governed by any specific accounting standard, in order to ensure the consistency and comparability of the financial statements of companies that hold concessions for the delivery of public services. More specifically, the interpretation sets out rules for accounting for the infrastructure used to provide the services under concession, for the costs associated with developing and maintaining such infrastructure, and for the revenue generated by the overall provision of the services. IFRIC 12 does not apply to all arrangements. Its scope is limited to service concession arrangements between public bodies and private operators in which the granter: (1) controls the use of the infrastructure and governs which services are to be provided, the manner in which they are to be provided and the prices of such services and (2) controls any residual interest in the infrastructure at the end of the concession period. The interpretation also applies to infrastructure constructed by or obtained from third parties for the provision of services under the concession, and to existing infrastructure that the granter makes available to the operator in order to provide such services. It does not apply to infrastructure owned and accounted for as property, plant and equipment by the operator prior to entering into the service concession arrangement.
Assisted by external consultants, the Parent Company has performed a detailed study of the applicability of IFRIC 12 and the effects of its adoption on the financial statements, identifying that this interpretation does not apply to the transmission activities aspect of the Parent Company's concession. In particular, neither the concession nor related legislation envisage the NTG's return to public ownership, either via the payment of an indemnity or otherwise. Accordingly, the public sector does not control, whether as owner or as holder of beneficial interests or other rights, any significant residual interest in the NTG's infrastructure at the end of the concession period.
By contrast, the Ministry is entitled to reclaim the operating assets employed directly in dispatching activities at the end of the concession. As such, the Group considers that IFRIC 12 does apply to its dispatching infrastructure since the relevant criteria apply: the services provided are regulated and control exists over the residual interest. More specifically, in view of the rate system for dispatching activities, the intangible asset model has been applied. Consequently, the property, plant and equipment and intangible assets employed in the dispatching activities, carried out under concession, are classified as "Intangible assets", in the "Infrastructure rights" caption, with application of the original amortisation schedule.
The revenue and costs relating to the investment in dispatching activities are recognised with reference to the contracts concerned on a stage-of-completion basis; revenue recognised during the construction phase is limited to the amount of

the internal and external construction costs incurred, considering that the fair value of the construction services is equivalent to the construction cost recognised to third-party contractors plus the internal cost of the technical personnel employed on such construction activities.
By contrast, tariff revenue continues to be recognised in accordance with IAS 18 and borrowing costs continue to be capitalised pursuant to IAS 23R.

## Goodwill

Goodwill arising from the acquisition of subsidiaries is allocated to each of the identified Cash Generating Units (CGU).
Goodwill is not amortised after initial recognition. It is adjusted to reflect impairment losses, measured as described below.
Goodwill relating to investments in associates and joint ventures is included in the carrying amount of those companies.
Where negative goodwill arises, it is booked within the income statement at the time of the acquisition.
In the adoption of the IFRS endorsed by the European Commission, the Group decided to restate only those business combinations that occurred after the transition date (1 January 2004). Goodwill arising on acquisitions before that date corresponds to the amount recognised using the previous accounting policies.

## Impairment losses

Property, plant and equipment and intangible assets with finite useful lives are tested at least once a year to check for evidence of impairment. If there is an indication that an asset may be impaired, its recoverable amount is estimated.
The recoverable amount of goodwill and intangible assets with indefinite useful lives, where present, as well as intangible assets not yet available for use, is estimated at least annually.
Recoverable amount is equal to the greater of fair value less costs to sell and value in use. Value in use is measured by discounting estimated future cash flows considering available information at the time of estimate and on the basis of subjective assessments of the performance of future variables, such as prices, costs, demand growth rates, production profiles, and discounted at a pre-tax rate that reflects current market assessment of the time value of money for the investment period and risks specific to the asset. If the intangible asset does not generate cash inflows that are largely independent, the asset's recoverable amount is calculated as part of the CGU to which it belongs.
An impairment loss is recognised in the income statement when the asset's book value, or the net invested capital of the CGU to which it belongs, is greater than its recoverable amount.
Impairment losses of CGUs are first taken as a reduction in the carrying amount of any allocated goodwill and then as a reduction in other assets of the CGU on a pro rata basis. Except for goodwill, impairment losses may be reversed up to the recoverable amount if there is an indication that the impairment loss no longer exists or when there is a change in the methods used to measure recoverable amount.

## Inventories

Inventories are recognised and measured at the lower of purchase cost and net estimated realisable value. Cost is calculated as the weighted average cost, including related charges. Net estimated realisable value stands for the estimated price of sale under normal conditions net of completion costs and the estimated costs to sell.

## Contract work in progress

When the profit or loss on a contract can be reliably estimated, the related contract costs and revenue are recognised separately in the income statement on a percentage of completion basis. Progress is measured based on the work carried out and measured proportionally to the ratio of costs for the works carried out up to reporting date and total cost of the contract (cost-to-cost). Differences between the value of completed contracts and payments on account received are recognised under statement of financial position assets or liabilities, considering any impairment losses on the work carried out so as to take into account the risks of customers' refusal to recognise the work performed. Expected contract losses are immediately taken to profit or loss.
Contract costs include all those costs that relate directly to the specific contract, as well as fixed and variable costs incurred by the Group companies as part of normal operations.

## Financial instruments

### Financial assets
Any financial assets other than financial derivatives that the Company has the positive intention and ability to hold to maturity are recognised at cost at the settlement date, which is the fair value of the initial consideration given in exchange, including transaction costs. They are subsequently measured at amortised cost, using the effective interest method, net of any impairment losses, which are determined as the lower of the asset's carrying amount and the present value of estimated future cash flows, discounted using the original interest rate. Financial assets are derecognised when, following their transfer or settlement, the Group companies are no longer involved in their management and no longer hold the risks and rewards of the transferred or settled instruments.

### Trade receivables
Trade receivables are initially recognised at fair value and subsequently measured at amortised cost, using the effective interest method, and net of any impairment losses due to sums considered non-recoverable, which are taken to the specific allowance for impairment. Impairment losses are measured on the basis of the present value of estimated future cash flows, discounted at the original effective interest rate.
Receivables with due dates that fall under normal commercial terms are not discounted.

### Cash and cash equivalents
Cash and cash equivalents are stated at nominal value. They include monetary items, i.e. amounts that are available on demand or with a very short maturity, subject to an insignificant risk and without collection costs.

### Trade payables
Trade payables are initially recognised at fair value and subsequently stated at amortised cost. If their due date falls under normal commercial terms, they are not discounted.

### Financial liabilities
Financial liabilities other than financial derivatives are recognised at the settlement date and measured at fair value, net of directly related transaction costs.
Subsequently, financial liabilities are measured at amortised cost, using the original effective interest method. If the liabilities are covered by fair value hedges, they are adjusted to reflect changes in fair value with respect to the hedged risk.

### Derivative financial instruments
Derivatives are recognised at fair value at the trade date and classified as hedges if the relationship between the derivative and the hedged item is formally documented and the hedge is highly effective within a range of 80% to 125%, as initially verified and periodically checked. When derivatives cover the risk of changes in the cash flows of the hedged instruments (cash flow hedges), the part of changes in the fair value qualifying as effective is initially taken to "Other comprehensive income" and subsequently to profit or loss, in line with the effects of the hedged transaction. The portion of the fair value of the hedging instrument that does not qualify as effective is taken to profit or loss.
When hedging derivatives cover the risk of changes in the fair value of hedged instruments (fair value hedges), they are recognised at fair value in the income statement. Accordingly, the hedged items are adjusted to reflect changes in the fair value associated with the hedged risk.
Changes in the fair value of derivatives that do not meet hedge accounting requirements in accordance with the IFRS-EU are recognised in profit or loss.
Fair value is measured on the basis of official quotations for instruments traded in regulated markets. The fair value of instruments not traded in regulated markets is measured by discounting projected cash flows along a yield curve of interest

rates at the reporting date, and by converting amounts in currency other than the euro at the year-end exchange rate.
Financial and non-financial contracts (which are not already measured at fair value) are also analysed to identify any embedded derivatives, which must be separated and measured at fair value. This analysis is conducted at the time the entity becomes party to the contract or when the contract is renegotiated in a manner that produces a material change in the original associated cash flows.
The measurement techniques used for derivatives existing at year end did not change with respect to the previous year. Accordingly, the effects in profit or loss and "Other comprehensive income" of these measurements are essentially attributable to normal market developments, as well as new derivative contracts signed during the year.

## Employee benefits

The liability in respect of employee benefits payable upon or after termination of employment relates to defined benefit plans (termination benefits, additional month's pay, indemnity for lack of notice, energy discount, ASEM health benefits and other benefits) or other long-term employee benefits (loyalty bonus) and is recognised net of any plan assets. It is measured separately for each plan on the basis of actuarial calculations that estimate the amount of future benefits that employees have accrued at the reporting date. The liability is recognised on an accruals basis over the vesting period. It is measured by independent actuaries.
Actuarial gains and losses at 1 January 2004 (date of transition to IFRS-EU) were recognised in equity. After that date, unrecognised actuarial gains and losses in excess of 10% of the greater of the present value of the defined benefit plan obligation and the fair value of plan assets are taken to profit or loss for the average expected term of service of employees participating in the plan. Otherwise, actuarial gains and losses are not recognised.

## Share-based payments

The cost of employee service remunerated through Stock Option Plans is measured at the fair value of the options granted to employees at the grant date. The fair value of options granted is recognised under personnel expense over the vesting period, with a corresponding effect on "Other comprehensive income", considering the best possible estimate of the number of options that employees will be able to exercise. Such estimate is reviewed where subsequent information indicates that the expected number of instruments representative of capital that will mature differs from the estimate previously carried out, regardless of achievement of the market conditions.
The measurement method used to calculate fair value considers all the characteristics of the options (term, price and conditions etc.), as well as the price of Terna S.p.A. shares at the grant date, the volatility of the stock and the yield curve at the grant date, in line with the term of the plan.
At the vesting date, the estimate is revised through the income statement to recognise the actual amount corresponding to the number of equity instruments that have actually vested, regardless of achievement of the market conditions.

## Provisions for risks and charges

Accruals to the Provisions for risks and charges are recognised when, at the reporting date, the Company has a legal or constructive obligation towards others as a result of a past event and it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the effect of the time value of money is material, accruals are measured by discounting estimated future cash flows using a pre-tax discount rate that reflects current market assessment of the time value of money and those risks specific to the liability, if present. Where discounting is used, the increase in the provision due to the passage of time is recognised in the income statement as interest expense. If the liability relates to property, plant and equipment (site disposal and restoration, for example), the provision is recognised as a balancing entry to the asset to which it relates. The expense is recognised in profit or loss through depreciation of the item of property, plant and equipment to which it relates.
Changes in the estimate are recognised within the income statement for the year in which the change happens, except for those costs expected for dismantling, removal and reclamation, which come as a result of changes in the timing and use of economic resources necessary to extinguish the obligation or attributable to a material change in the discount rate, which are recognised as an increase or reduction of the related assets and recognised in profit or loss through depreciation.

## Grants

Revenue is recognised when it is probable that the economic benefits deriving from the operation will be used by the enterprise. However, when there is uncertainty concerning the recovery of an amount already recognised in revenue, the non-recoverable value or the amount whose recovery is no longer probable is recorded as a cost.
Grants received in relation to specific assets whose value is recognised under non-current assets are, for plants operating before 31 December 2002, recognised under other liabilities and taken to profit or loss over the depreciation period of the related assets. As of 2003, grants for new plants that have entered operation are recognised as a direct reduction in the value of the related asset.
Grants for operating expenses are expensed in full when the recognition requirements are satisfied.

## Revenue

Revenue is recognised when it is probable that the economic benefits deriving from the operation will be used by the enterprise. Depending on the type of transaction, revenue is recognised on the basis of the following specific criteria:

- revenue from the sale of goods is recognised when the material risks and rewards of ownership of the goods have been transferred to the buyer and their total amount can be reliably determined and collected;
- revenue from services rendered is recognised with reference to the stage of completion of the transaction. If revenue cannot be reliably measured, it is recognised to the extent of recoverable costs;
- revenue accrued during the year in respect of contract work in progress is recognised on the basis of the payments agreed for the progress of works using the cost-to-cost method. In addition to contractual payments, project revenue includes any payments in respect of variations, price revisions and incentives, with the latter recognised where it is probable that they will actually be earned and can be reliably determined. Revenue is also adjusted for any penalties for delays attributable to Group companies;
- when the recovery of an amount already recognised in revenue is uncertain, the non-recoverable value or the amount whose recovery is no longer probable is recorded as a cost, with recognition of a balancing entry in Provisions for risks and charges;
- amounts collected on behalf of third parties, such as the fees paid to non-Terna grid owners, as well as revenue recognised for managing activities related to the balancing of the national electrical system, which do not increase equity, are reported net of the related costs. This reporting method, which reflects the substance of transactions by offsetting revenue with the related costs arising from the “same transaction”, is discussed in full in a specific section of the explanatory notes.

## Financial income and expense

Borrowing costs directly attributable to the acquisition, construction or production of an asset that qualify for capitalisation are capitalised as part of the cost of the asset. The qualifying assets (property, plant and equipment and intangible assets) involved are those that require at least one year before being ready for use. The directly attributable borrowing cost is that which would not have been incurred if the expenditure for the asset had not been incurred.
Where funds are borrowed specifically, costs eligible for capitalisation are the actual costs incurred less any income earned on the temporary investment of such borrowings. Where funds are raised through general borrowing, the eligible amount is determined by applying a capitalisation rate to the expenditure on that asset. The capitalisation rate will be the weighted average of the borrowing costs applicable to the general pool, excluding any specifically borrowed funds. The amount of borrowing costs capitalised during a year shall in any case not exceed the amount of borrowing costs incurred during that year. Capitalisation commences as from the date all the following conditions have been met: (a) expenditures have been incurred for the asset; (b) borrowing costs are being incurred; and (c) activities to prepare the asset for its intended use or sale are in progress. Capitalisation ceases when the activities necessary to prepare the asset for its intended use or sale are substantially complete.
The capitalisation rate used for 2011 amounts to 3.08% and that for 2010 amounts to 2.63%.

Financial income and expense other than capitalised amounts are recognised on an accruals basis in respect of the interest on the net value of the related financial assets and liabilities using the effective interest rate.

## Dividends

Dividends from investee companies are recognised when the shareholders' right to receive payment is established.
Dividends and advances on dividends payable to third parties are shown as changes in shareholders' equity at the date in which they are approved by the Shareholders' Meeting and the Board of Directors, respectively.

## Earnings per share

Basic earnings per share are calculated by dividing the profit or loss for the year attributable to holders of ordinary shares by the weighted average of outstanding ordinary shares during the year.
Diluted earnings per share are calculated by dividing the profit for the year attributable to holders of ordinary shares by the weighted average of outstanding shares, adjusted to consider the effects of all potential ordinary shares that could have a diluting effect.

## Income taxes

Current income taxes are recognised as tax liabilities, net of advances paid, or tax assets where the net balance of the captions is positive. They are based on the estimated taxable income and in accordance with current legislation, taking account of applicable exemptions.
Deferred tax assets and liabilities are calculated on the temporary differences between the carrying amounts of assets and liabilities recognised in the financial statements and the corresponding amounts recognised for tax purposes, using current tax rates or the rates expected to be in effect when the temporary differences reverse, based on current rates or those that are substantially approved at the reporting date.
Deferred tax assets are recognised when their recovery is considered probable, i.e. when future taxable income will be available against which the asset can be used. The recoverability of deferred tax assets is reviewed at each year end.
Deferred tax liabilities are recognised in any case if they exist. Taxes in respect of components recognised in "Other comprehensive income" are also recognised in the same item.

## Discontinued operations and non-current assets held for sale

Non-current assets (or disposal groups) whose carrying amount will be recovered principally through a sale rather than through continuing use are classified as held for sale and reported separated from other assets and liabilities in the statement of financial position. Non-current assets (or disposal groups) classified as held for sale are first measured in conformity with the IFRS/IAS applicable to each asset and liability and subsequently are measured at the lower of their carrying amount and fair value less costs to sell. The carrying amounts of each asset and liability that are not governed by the measurement rules set out in IFRS 5, but are held for sale, are remeasured on the basis of the applicable IFRS before the fair value less costs to sell is redetermined. The individual assets of the companies classified as held for sale are not amortised, whereas financial expense and other expenses attributable to liabilities held for sale continue to be recognised. Any subsequent impairment losses are recognised directly as an adjustment to the carrying amount of the non-current assets (or disposal groups) classified as held for sale through profit or loss. The corresponding statement of financial position values for the previous year is not reclassified. A discontinued operation is a component of an entity that either has been disposed of, or is classified as held for sale, and:

- represents a separate major line of business or geographical area of operations;
- is part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations; or
- is an operation acquired exclusively with a view to resale.

## New standards

### International Financial Reporting Standards taking effect from 1 January 2011

The following international financial reporting standards and related interpretations took effect from 1 January 2011 up to the date of these consolidated financial statements:

### Amendment of IAS 24 – Related Party Disclosures

Issued on 4 November 2009, this amendment simplifies the disclosure requirements for related party for government-related entities (i.e. entities subject to control, joint control or significant influence by a governmental body), and clarifies the definition of a related party eliminating certain application difficulties.

### Amendment of IFRS 7 – Financial instruments: disclosures – Transfers of financial assets

With European Commission Regulation no. 1205/2011 issued on 22 November 2011, the disclosure required on financial instruments in the financial statements is extended. The amendment will allow users of financial statements to better evaluate exposure to risk connected with the transfer of financial assets and the effects of said risks on the entity's financial position. According to that established by the new Regulation, the entity must provide a disclosure that enables users of the financial statements to understand: the ratio of the financial assets transferred and not fully eliminated and the associated liabilities; to assess the nature, and related risks, of the residual involvement of the entity in the financial assets eliminated.
This standard has not had a significant impact on the financial statements at 31 December 2011.

### Improvements to the IFRS (published in 2010)

2010 version of the document that contains minor amendments to the standards already published. This group of amendments was endorsed during the first quarter of 2011 and came into force on 1 January 2011.
The following standards and interpretations have also been endorsed and come into force, and govern circumstances that are not relevant to the financial statements of the Company at the moment:

- amendment to IAS 32 Financial instruments – Presentation: classification of rights issues (or warrants);
- amendment to IFRIC 14: Prepayment of a minimum funding requirement;
- IFRIC 19: Extinguishing financial liabilities – Extinguishing financial liabilities with equity instruments.

### International financial reporting standards endorsed but not yet in force

At the date on which these financial statements were prepared, no international reporting standards had been endorsed by the European Commission that had not yet come into force.

### International financial reporting standards not yet endorsed

For amendments, new standards and interpretations that have not yet been endorsed by the EU, but which address issues that affect or could affect the Group, analyses are currently being conducted of the possible impact of their application to its financial statements, taking account of the date on which they take effect. This assessment covers the standards and interpretations listed below.

### IFRS 9 – Financial Instruments

On 12 November 2009, the IASB published standard IFRS 9 – Financial instruments on the classification and measurement of financial assets applicable no longer as from 1 January 2013 but from 1 January 2015, as proposed by the IASB amendment (currently being endorsed), which postpones the coming into force. The new standard arises from a complex procedure, articulated into various different stages, that aims to entirely replace IAS 39; for the stages currently published by the IASB, the new standard defines the classification criteria of financial assets and liabilities and derecognition of financial assets from the financial statements. More specifically, to determine the measurement criteria of financial assets, it introduces a unique approach that, replacing the many different methods in IAS 39, is based on the methods by which financial instruments are managed and on the characteristics of the contractual cash flow of the financial assets themselves. On the contrary, for financial liabilities, the main change concerns the representation of "Other Comprehensive Income" (OCI) of the effects of changes to the fair value assigned to the credit risk of liabilities measured at fair value, which will no longer be stated on the income statement.
Finally, we stress that the adoption process of standard IFRS 9 is currently suspended in the EU, given that the European Commission intends to proceed with the approval of the standard only upon conclusion of the definitive standard publication by IASB, when the replacement of IAS 39 has been completed.

### New accounting standards on the consolidation

On 12 May 2011, the IASB completed the draft concerning consolidation with the publication of the following 5 standards (IFRS 10, IFRS 11, IFRS 12, IAS 27 Amended, IAS 28 Amended), the first application of which is scheduled for 1 January 2013, with a probable postponement of one year as required by EFRAG. In particular:

### IFRS 10 – Consolidated Financial Statement

The standard introduces a single control model that is valid for all types of entity, superseding SIC 12 – Consolidation of SPE (Specific Purpose Entity) and removing from IAS 27 the part relating to control and consolidation. In particular, the standard introduces a new definition of control, based on the figures of the investee (a company actually or potentially controlled) and the investor (the Parent Company drawing up the consolidated financial statements), which has the control if it is exposed, or has variable returns with respect to its involvement in the investee and has the possibility of affecting these returns through its power over the investee. Additionally, in identifying the investor, both potential yet substantive voting rights must be considered, where the holder has the real possibility of exercising these rights, in addition to actual control, intended as the possibility of unilaterally guiding activities. The first application of the standard will be retrospective.

### IFRS 11 – Joint Arrangements

The new standard introduces important simplifications as it supersedes the 3-type classification as established by IAS 31. The new classification is based on the analysis of the rights and obligations arising from the agreement and establishes only two types: joint operations and joint ventures. The former derive from a non-structured agreement through an SPV that is separated from the parties, which determines rights over the assets and obligations of the liabilities, in accounting terms the controlling share of assets, liabilities and the corresponding costs and revenue is noted. The second, on the other hand, are classified as joint ventures where there are structured agreements through an SPV that is separated from the parties. In this case, the entity must carry out assessments based on the legal form of the “SPV”, the contractual terms and the other facts and circumstances from which the rights over the net assets of the agreement derive. For joint ventures, the standard provides for the elimination of the proportional consolidation method, replaced by the equity method only. The new standard therefore replaces IAS 31 and SIC 13.

### IFRS 12 – Disclosure of interests in other entities

The standard governs the disclosure to be made in the financial statements with regard to the equity interests held in subsidiaries, associates and joint control companies in addition to structured entities, in lieu of the requirements previously included in IAS 27 and IAS 28. The objective of the new standard is to require additional information in the financial statements in relation to the basis for the control evaluation, any limits to consolidated assets and liabilities and exposure to risk deriving from the involvement with the entity.

### Amendment to IAS 27 – Separate Financial Statements

The amendment to IAS 27 has the objective of setting standards to be applied in accounting for investments in subsidiaries, joint ventures and associates when preparing separate (non-consolidated) financial statements. The amendment therefore leaves unchanged the provisions for separate financial statements, and replaces the parts relating to the consolidated financial statements with the prescriptions of the new IFRS 10, to which reference should be made for further details.

### Amendment to IAS 28 – Investments in Associates and Joint Ventures

The amendment to IAS 28 (as amended in 2011) sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures.

### IFRS 13 – Fair Value Measurement

On 12 May 2011, the IASB published IFRS 13, which seeks to increase consistency and comparability in fair value measurements and related disclosures through a “fair value hierarchy”. The hierarchy categorises the inputs used in valuation techniques into three levels. The hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The first application is scheduled for 1 January 2013.

### Amendment to IAS 19

On 16 June 2011, the IASB published an amendment to IAS 19 “Employee benefits”, which introduces changes to the recognition and measurement of employee benefits related and severance indemnity costs and the disclosure on all employee benefits. The amendment has eliminated the option to defer the recognition of actuarial gains and losses using the corridor method and provided for the recognition of the costs connected with work rendered and net financial expenses on the income statement, the recognition of actuarial gains and losses deriving from remeasurements of assets and liabilities to be presented in “Other Comprehensive Income” (OCI). Additionally, the return on the asset included amongst net financial expenses must be calculated according to the liability discount rate and no longer on the forecast return on the asset. Finally, the amendment also introduces new additional information to be given in the Notes to the financial statements. The amendment applies retrospectively from the financial year beginning on 1 January 2013.

### Amendment to IAS 1

On 16 June 2011, the IASB published an amendment to IAS 1 "Presentation of the financial statements". This established, amongst other aspects, to group together items within the "Other Comprehensive Income" (OCI), that may be reclassified to the profit or loss section of the income statement. The first application is scheduled for 1 January 2013.

### Amendment to IAS 12 – Deferred tax: recovery of underlying assets

The amendment affects all the entities that apply IAS 40 – Investment property using the fair value method and that have recognised assets under property, plant and equipment which are not depreciated and which are recorded using the revaluation model established by IAS 16. At present, therefore, the amendment does not cover situations presented in our financial statements.

### Amendment to IFRS 1 – Severe hyperinflation and removal of fixed dates for first-time adopters

Two amendments to IFRS 1 were published: the first one replaces references to fixed transition date of 1 January 2004 with "the date of transition to IFRSs". As a result, entities adopting IFRSs for the first time would not have to restate derecognition transactions that occurred before the date of transition to IFRSs. The second amendment provides specifications on how an entity should resume presenting financial statements in accordance with IFRSs after a period when the entity was unable to comply with IFRSs since its functional currency was subject to severe hyperinflation.

The following standards and interpretations have also been published, governing circumstances currently not relevant to the financial statements of the Company:

- amendment to IAS 32 Financial instruments – Offsetting Financial Assets and Financial Liabilities, provides clarifications on the application of rules by which to offset financial assets and liabilities; it will come into force on 1 January 2014;
- amendment to IFRIS 7 Financial instruments – Disclosures - Offsetting Financial Assets and Financial Liabilities, on the supplementary information to be supplied in relation to the actual or potential effects of the application of rules of offsetting financial assets and liabilities; the amendment will come into force on 1 January 2013;
- IFRIC 20 – Stripping costs in the Production Phase of Surface Mine - accounting treatment of the costs of stripping a surface mine, to be recognised during production.

## B. Operating segments

In view of the characteristics of the Terna Group's business in Italy, the following operating segments have been identified, with reference to continuing operations:

- **regulated activities**;
- **unregulated activities**.

The **regulated activities** segment comprises electricity transmission and dispatching, as well as the measurement, validation and registration activities associated with metering.
These activities form part of a single operating segment since they meet the relevant aggregation criteria based on similar economic characteristics, such as the common economic/regulatory context in which the services are provided, the type of tariffs and the way they are determined, and the public-interest nature of the activities concerned.

The **unregulated activities** mainly regard the management (operation and maintenance) of high-voltage plant owned by other entities, plant engineering services, maintenance of the third-party fibre optic network and housing of TLC equipment. In essence, this segment comprises the specialist services provided by the Terna Group to third-party customers.
These activities are pursued as commercial initiatives that are not regulated by the AEEG: they are pursued in a free market in which the Group leverages its skills and resources to offer specialised services to other companies mainly in the high- and very-high voltage sector and in telecommunications.

The identification of the Terna Group's operating sectors was carried out consistently with the internal management control system adopted by the Parent Company; in particular in the internal reports periodically presented and reviewed by senior management (management control reports) we used the adjusted EBITDA [1] indicator for unregulated activities.

(1) EBITDA (Gross Operating Margin): represents an indicator of operating performance; it is calculated by adding depreciation and amortisation back to the operating results (EBIT).

Below we report the results of the Terna Group's operating sectors in 2011 and 2010, as well as the reconciliation with the Group's results before tax and discontinued operations and assets held for sale.

| | Italy | |
|---|---|---|
| € million | 2011 | 2010 |
| Revenue from regulated activities | 1,568.5 | 1,514.2 |
| Revenue from unregulated activities | 67.1 | 75.0 |
| **Total continuing operations revenue** | **1,635.6** | **1,589.2** |
| Regulated activities adjusted EBITDA | 1,295.2 | 1,245.7 |
| Unregulated activities adjusted EBITDA | 40.6 | 40.7 |
| **Continuing operations: adjusted EBITDA** | **1,335.8** | **1,286.4** |
| Regulated activities adjusted EBITDA margin (%) | 82.6% | 82.3% |
| Unregulated activities adjusted EBITDA margin (%) | 60.5% | 54.3% |

| **Continuing operations total reconciliation** | 2011 | 2010 |
|---|---|---|
| Continuing operations: adjusted EBITDA | 1,335.8 | 1,286.4 |
| Unallocated costs | 106.1 | 111.5 |
| **EBITDA - continuing operations** | **1,229.7** | **1,174.9** |
| Depreciation | 394.1 | 360.5 |
| **EBIT - continuing operations** | **835.6** | **814.4** |
| Financial income/(expense) | (128.4) | (105.1) |
| Share of profit/(loss) of equity-accounted investees | 7.4 | 2.6 |
| **Pre-tax profit from continuing operations** | **714.6** | **711.9** |

For the purpose of measuring adjusted EBITDA of the operating segment, **regulated assets** recognise non-monetary costs (accruals to the provisions for future risks and charges) amounting to €6.9 million.
The information regularly reported to senior management does not make direct reference to sector activities but rather to the measurement and presentation of gross invested capital. The following table reports that indicator relative to continuing operations for the years 2011 and 2010:

| | Italy | |
|---|---|---|
| | 2011 | 2010 |
| € million | Continuing operations | Continuing operations |
| Net non-current assets (1) | 9,163.1 | 8,303.6 |
| NWC (2) | (724.2) | (381.3) |
| Gross invested capital | 8,438.9 | 7,922.3 |
| Investments in associates and joint ventures | 66.8 | 23.6 |

(1) Net fixed assets include the value of the items "Property, plants and equipment", "Goodwill", "Intangible assets", "Equity-accounted investees ", "Other non-current assets" and "Non-current financial assets" for the value of the other equity investments (€0.6 million).
(2) NWC (Net Working Capital) is equal to the difference between current assets, net of liquid funds, and current liabilities net of the short-term portion of long-term financing and other non-current liabilities.

As regards the dependence of Terna Group customers on external customers, in 2010 transactions that generated revenue from individual customers or companies under common control equal to more than 10% of consolidated revenue were represented by transactions with related parties in respect of regulated activities; for more information, please see the section on “Related party transactions”.

With reference to discontinued operations and assets held for sale, the information supplied to senior management provides details of net income deriving from the mentioned sales of Rete Rinnovabile S.r.l. and NRTS S.r.l.. Below are details of the components determining the booked result of discontinued operations and assets held for sale:

| RETE RINNOVABILE (*) | € million |
|---|---|
| Price (EV) | 624.3 |
| Costs incurred | (438.8) |
| Gross contract margin | 185.5 |
| Other components and tax | 19.0 |
| **Comprehensive net income from discontinued operations** | **204.5** |
| Expenses for contractual guarantee net of tax | (8.6) |
| **Total net comprehensive income** | **195.9** |
| ***of which 2010*** (**) | ***145.3*** |
| ***of which 2011*** | ***48.6*** |
| Contribution to the consolidation 1st quarter 2011 | 2.0 |
| **2011 profit from discontinued operations and assets held for sale - RTR** | **50.6** |

(*) The photovoltaic plants sale contract is classed as a construction contract.
(**) The 2010 contract margin amounts to €146.8 million.

| NUOVA RETE SOLARE | € million |
|---|---|
| Price (EV) | 264.3 |
| Investments | (195.4) |
| **Gross capital gain** | **68.9** |
| Expenses for contractual guarantees and other accessory expenses | (31.7) |
| Tax | (10.7) |
| **Net capital gain** | **26.5** |
| Contribution to consolidation 08.03 - 24.10.2011 | 1.8 |
| **2011 profit from discontinued operations and assets held for sale - NTRS** | **28.3** |

The result of discontinued operations and assets held for sale also includes the partial release of the provision allocated in 2009 for €33.8 million, inclusive of the related exchange effect, with reference to contractual obligations, which expired during the financial year, deriving from the sale of the majority equity interest in Terna Participações.

# C. Notes to the consolidated income statement

## Revenue

### 1. Revenue from sales and services - €1,591.3 million

"Revenue from sales and services" for the years 2011 and 2010 is analysed in the following table:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Grid transmission fees | 1,380.8 | 1,309.2 | 71.6 |
| Adjustments for prior year grid transmission fees | 0.1 | (2.9) | 3.0 |
| Other energy revenue | 163.4 | 169.8 | (6.4) |
| Other revenue from sales and services | 47.0 | 57.0 | (10.0) |
| **Total** | **1,591.3** | **1,533.1** | **58.2** |

**Grid transmission fees and related adjustments**

Grid transmission fees largely refer the remuneration paid to the Parent Company for use of the National Transmission Grid (€1,237.6 million). It also comprises the net revenue from the portion of the NTG pertaining to the subsidiary Terna Rete Italia (€143.3 million).

The increase in this caption by €74.6 million mainly derives from the following factors:

- greater revenue of the Parent Company for €64.6 million, essentially due to the following:
  - effects of AEEG Resolution 228/10, which reviewed tariffs for 2011 (€51.2 million, including the incentive on the remuneration of strategic works pursuant to AEEG Resolution 87/10);
  - increased grid transmission fees related to the Defence Plan (€11.3 million);
  - positive impact for the greater net negative grid transmission fees adjustments recognised in 2010 (€2.1 million).
- remuneration of the interest of NTG owned by Terna Rete Italia (€10.0 million) which, amongst others, reflects the revenue relating to the plants of the merged company Rete di Trasmissione Brescia, purchased in August 2010 and not included in the scope of consolidation in the first seven months of the previous financial year.

**Other energy revenue**

This caption comprises the fees paid to the Parent Company by electricity companies for dispatching services (DIS component, €129.3 million), together with the revenue from the construction and development of dispatching infrastructure recognised pursuant to IFRIC 12 (€34.1 million); please note that, as specified in section "A. Accounting policies and measurement criteria", such revenue corresponds to the costs incurred during the same period to purchase raw materials and consumables, services and staff which are included in operating expenses.

The decrease in the item, amounting to €6.4 million, reflects the drop in revenue deriving from the investments made during the financial year in dispatching infrastructures (€4.2 million) and the economic effects connected with the DIS component and which are due to:

- DIS tariff component for €9.9 million;
- regulating providing incentives for the quality of the transmission service (AEEG Resolution 169/08 – €3.2 million);
- adaptation of the measurement of the incentives mechanism associated with the reduction in volumes procured from the Market for Dispatching Services made available under AEEG Resolution 213/09 (€66 million, a negative €11.0 million compared with €77.0 million incentives reported in 2010). More specifically, we would recall that the result achieved is recognised in terms of fair value in consideration of the three-year nature (2010/2012) of the incentive mechanism, as extensively commented in the 2010 financial report, to which we would refer;
- incentives linked to the increasing of the efficiency in the forecast for domestic energy demands and in the forecast production provided by wind power sources (down by €4.3 million).

**Other energy items - pass-through revenue/costs**

This caption includes the revenue and costs "passed-through" by the Group (whose net balance is therefore nil), which relate entirely to the Parent Company. These flows arise with operators active in the electricity market, and involve the daily purchase and sale of energy in order to carry out dispatching activities. To that end, the measurements at each point of input and withdrawal are taken and the differences from the energy market schedules are calculated. These differences (called imbalances) are measured using algorithms established by the regulatory framework. The net charge resulting from the measurement of these imbalances and of the buying and selling transactions executed by the Parent Company Terna on the Market for Dispatching Services are billed on a pro rata basis to each consumer with the uplift fee. It also includes the grid transmission fee which Terna pays to other owners of the grid.

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| **Revenue - Power Exchange:** | | | |
| Revenue - Power Exchange: | | | |
| - foreign market - exports | 0.8 | 1.1 | (0.3) |
| - sale of energy on the Day Ahead Market, Adjustment Market, Market for Dispatching Services and others | 594.7 | 653.4 | (58.7) |
| - unbalancing and other minor items | 1,003.4 | 928.3 | 75.1 |
| - ancillary service resources procurement | 1,261.4 | 1,152.5 | 108.9 |
| - congestion rent - rights for use of transportation capacity (RTC), Res. 288/06 | 693.7 | 821.4 | (127.7) |
| - other items - Power Exchange | 65.2 | 140.4 | (75.2) |
| - interconnector/shipper | 79.0 | 125.6 | (46.6) |
| - Market coupling Res.143/10 | 79.6 | 0.0 | 79.6 |
| **Total revenue - Power Exchange** | **3,777.8** | **3,822.7** | **(44.9)** |
| Revenue components under Res. nos. 168/04 - 237/04 and others | 1,048.9 | 817.3 | 231.6 |
| Other items | 182.7 | 171.4 | 11.3 |
| Revenue from grid transmission fees of other owners and GRTN share CIP/6 | 16.1 | 19.2 | (3.1) |
| **Total revenue from outside the Power Exchange** | **1,247.7** | **1,007.9** | **239.8** |
| **Total pass-through energy revenue** | **5,025.5** | **4,830.6** | **194.9** |
| **Energy purchases:** | | | |
| - on Day Ahead Market and Adjustment Market | 98.5 | 160.3 | (61.8) |
| - to provide the dispatching service | 1,433.8 | 1,664.8 | (231.0) |
| - for unbalancing | 1,270.5 | 902.7 | 367.8 |
| - on the foreign market - imports | 2.7 | 0.5 | 2.2 |
| - Electricity Market Operator fees | 0.8 | 2.7 | (1.9) |
| - congestion rent – RTC, Res. no. 288/06 | 420.1 | 513.9 | (93.8) |
| - other items - Power Exchange | 60.9 | 72.7 | (11.8) |
| - interconnector/shipper | 417.0 | 505.1 | (88.1) |
| - Market coupling Res.143/10 | 73.5 | 0.0 | 73.5 |
| Total costs - Power Exchange | 3,777.8 | 3,822.7 | (44.9) |
| Purchase of electricity market related services | 1,048.9 | 817.3 | 231.6 |
| Other items | 182.7 | 171.4 | 11.3 |
| Fees to be paid to NTG owners, GRTN and other | 16.1 | 19.2 | (3.1) |
| **Total services and fees** | **1,247.7** | **1,007.9** | **239.8** |
| **Total pass-through energy costs** | **5,025.5** | **4,830.6** | **194.9** |

## Other revenue from sales and services

"Other revenue from sales and services" amounted to €47.0 million and mainly relates to revenue from a variety of specialised high- and very-high-voltage services that the Parent Company provides to third-party customers (€35.6 million). The amount reflects revenue from:

- NTG connection services of production plants and property of end users (€5.8 million);
- the contribution due to the Parent Company for coverage of costs incurred for electricity discounts to its employees (€1.5 million);
- line design for inter-connection with abroad (€1.4 million);

The €10.0 million decrease is essential due to the greater orders of the Parent Company for 2010 connected with the development/extension of electrical stations and the related connections to the NTG (€11.0 million).

## 2. Other revenue and income - €44.3 million

"Other revenue and income" for the years 2011 and 2010 are analysed in the following table:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Rental income | 18.4 | 19.9 | (1.5) |
| Sundry grants | 10.7 | 9.5 | 1.2 |
| Insurance settlements for losses | 3.7 | 7.2 | (3.5) |
| Gains on the disposal of plant components | 4.4 | 3.5 | 0.9 |
| Prior period income | 1.2 | 6.7 | (5.5) |
| Sales to third parties | 3.1 | 2.4 | 0.7 |
| Other revenue | 1.0 | 0.6 | 0.4 |
| Contractual penalties at suppliers' expense | 1.8 | 0.3 | 1.5 |
| Gain from purchase at bargain prices | 0.0 | 6.0 | (6.0) |
| **Total** | **44.3** | **56.1** | **(11.8)** |

Other revenue and income, amounting to €44.3 million, mainly refer to the Parent Company for €37.4 million and to the subsidiary Terna Rete Italia for €6.5 million.
Rental income mainly includes rent from the Wind Group for the housing of optical fibre on the grid (€11.4 million) and Enel Distribuzione's use of the Company's infrastructure for power line communication (€1.2 million).
The decrease in Other revenue and income (€11.8 million) is essentially attributable to:

- the recognition in 2010 of gain from bargain purchase (amounting to €6.0 million) with reference to the acquisition of the equity interest in Rete di Trasmissione Brescia;
- lesser revenue for contingent assets (€5.5 million) and insurance repayments for damages mainly to primary plants (€3.5 million);
- positive effect deriving from the penalties charged to suppliers for breach of contract (€1.5 million) and from the release of the share of set-up grants for the year (€1.2 million).

## Operating expenses

## 3. Raw materials and consumables - €20.7 million

This item, amounting to €20.7 million, expresses the value of the consumption of materials and miscellaneous equipment used for the core business of operating and maintaining plants in addition to costs for materials recognised in pursuance of IFRIC 12 and with reference to investments in dispatching infrastructures. The decrease of €7.5 million with respect to the previous financial year (€28.2 million in 2010), mainly attributable to the Parent Company (a negative €6.9 million), essential derives from the lesser investing activities and the development of the dispatching infrastructures for the optimisation on the Service Market in 2010 (a negative €2.4 million) and the lesser consumptions of materials for diversified activities and engineering for third parties.

## 4. Services - €149.0 million

The cost of services totalled €149.0 million, of which €144.6 million related to the Parent Company and €3.9 million was relative to the subsidiary Terna Rete Italia.
The cost of "Services" for the years 2011 and 2010 is analysed in the following table:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Tenders on plants | 33.1 | 34.9 | (1.8) |
| Maintenance and sundry services | 58.8 | 63.0 | (4.2) |
| Insurance | 6.6 | 6.7 | (0.1) |
| Remote transmission and telephone | 13.7 | 14.2 | (0.5) |
| IT services | 24.3 | 21.3 | 3.0 |
| Leases and rentals | 12.5 | 12.1 | 0.4 |
| **Total** | **149.0** | **152.2** | **(3.2)** |

The item "Services" refers to costs for tenders and services for routine maintenance operations and plant maintenance and expenditures for general services (a total of €91.9 million). It also includes costs for IT services (€24.3 million) remote transmission and telephone services (€13.7 million), leases and rentals (€12.5 million), and insurance (€6.6 million). It is specified that the costs relating to remuneration relating to the Board of Statutory Auditors amount to €0.3 million.
The decrease (€3.2 million) is mainly due to investments connected with the development of dispatching infrastructures (lesser costs for €1.9 million) and greater diversified assets and engineering with regard to third parties than the previous financial year.

## 5. Personnel expenses - €211.0 million

"Personnel expenses" for the years 2011 and 2010 are analysed in the following table:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Wages, salaries and other short-term employee benefits | 250.4 | 254.5 | (4.1) |
| Directors' fees | 2.0 | 1.6 | 0.4 |
| Termination indemnities, electricity discount and other post-employment benefits | 16.1 | 15.8 | 0.3 |
| Early retirement incentives | 10.1 | 4.6 | 5.5 |
| **Personnel expenses, gross** | **278.6** | **276.5** | **2.1** |
| Personnel expenses, capitalised | (67.6) | (64.3) | (3.3) |
| **Total** | **211.0** | **212.2** | **(1.2)** |

This caption includes the cost of wages and salaries, social security contributions and other costs incurred by the Parent Company for early retirement incentives, as well as benefits paid to employees who stay with the company and termination indemnities provided for by the current national collective employment contract for the electricity sector.
Total personnel expenses drop by €1.2 million as a consequence of the increase in capitalised personnel expenses (amounting to €3.3 million, as a result of the greater investments made during the financial year), partially offset by the increased gross personnel expenses (€2.1 million).

The following table shows the number of Parent Company employees by category at year end and the average number for the financial year:

| | Average number | | Final number | |
|---|---|---|---|---|
| | 2011 | 2010 | 31.12.2011 | 31.12.2010 |
| Senior management | 60 | 64 | 60 | 59 |
| Junior management | 504 | 495 | 490 | 502 |
| Office staff | 1,949 | 1,897 | 1,966 | 1,890 |
| Production workers | 1,005 | 1,030 | 977 | 1,017 |
| **Total** | **3,518** | **3,486** | **3,493** | **3,468** |

The net change in the average number of employees at the end of 2010 was an increase of 32 units.
As of 31 December 2011, the subsidiary Terna Crna Gora d.o.o. has 2 local employees, whilst the other subsidiaries have no employees.
Reference should be made to section "25. Employee benefits" for the reconciliation of the opening and closing present value of the liability for employee benefits and the main assumptions used in the actuarial estimate.

## 6. Amortisation, depreciation and impairment - €396.3 million

These relate to accruals during the year calculated on the basis of amortisation and depreciation rates that reflect the useful lives of the Group companies' plant, property and equipment and intangible assets (€394.1 million), and related write-downs (€2.1 million).
The following table details the amortisation, depreciation and impairment for the years 2011 and 2010:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Amortisation on intangible fixed assets | 50.8 | 45.1 | 5.7 |
| *of which: infrastructure rights* | *25.1* | *23.7* | *1.4* |
| Depreciation of property, plant and equipment | 343.3 | 315.4 | 27.9 |
| Impairment of property, plant and equipment and intangible assets | 2.1 | 0.2 | 1.9 |
| Impairment of trade receivables | 0.1 | 0.0 | 0.1 |
| **Total** | **396.3** | **360.7** | **35.6** |

The increase in the item, totalling €35.6 million, primarily reflects the growth in depreciation/amortisation (€33.6 million) with respect to 2010, mainly due to:
- the Parent Company for €30.0 million, essentially due to increased property, plant and equipment (€24.7 million) and intangible assets (€5.3 million, of which €1.4 million ascribable to infrastructure rights) which entered into operation during the year;
- the subsidiary Terna Rete Italia, for €3.5 million, of which €3.1 million due to greater property, plant and machinery (€1.3 million relate to greater amortisation/depreciation of the lines of the incorporated Rete Trasmissione Brescia) and €0.4 million to intangible assets.

The changes also suffer the recognition of greater impairment of property, plant and machinery and intangible assets of the subsidiary Terna Rete Italia (€1.8 million).

## 7. Other operating expenses - €23.0 million

"Other operating expenses" for the years 2011 and 2010 are analysed in the following table:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Indirect and local taxes and duties | 6.1 | 6.6 | (0.5) |
| Accruals to provisions for risks and charges | 6.6 | 2.0 | 4.6 |
| Contingent liabilities | 2.1 | 2.7 | (0.6) |
| Power failure charges | 1.6 | 4.0 | (2.4) |
| Losses on the disposal/closure of plants | 0.8 | 0.5 | 0.3 |
| Other operating expenses | 5.8 | 5.7 | 0.1 |
| **Total** | **23.0** | **21.5** | **1.5** |

Other operating expenses are mainly attributable to the Parent Company (€18.1 million) and the subsidiary Terna Rete Italia (€4.8 million).
The change (€1.5 million) mainly derives from the combined effect of the following events:
- accruals made to the provision for risks and charges to be paid to distributing companies for power failures of transformation plants connected to the NTG (pursuant to Resolution 341/07 – €2.7 million, of which €2.3 million attributable to the subsidiary Terna Rete Italia and €0.4 million attributable to the Parent Company) and for the joint participation in indemnities to end users by Terna S.p.A. (€1.1 million). Finally, lesser accruals to the provision for disputes, for €0.7 million;
- lesser contributions for power failures, pursuant to Resolution 333/07, sustained by Terna S.p.A. and Terna Rete Italia during the financial year (€0.8 million and €1.6 million respectively);
- recognition of expenses relating to the renewal of the Memorandum of Understanding for the promotion and optimisation of contemporary Italian art signed with the Ministry for Cultural Assets and Heritage (€1.5 million);
- lesser tax, duties and local taxation for the financial year (€0.5 million).

## Financial income and expense

### 8. Net financial income/(expense) - Negative €128.4 million

This caption is analysed below:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| **Financial income** | | | |
| Interest income and other financial income | 30.4 | 9.0 | 21.4 |
| Debt adjustment (bonds) and related hedges | 0.0 | 2.2 | (2.2) |
| Exchange gains | 1.2 | 0.0 | 1.2 |
| Other financial income | 5.4 | 0.0 | 5.4 |
| **Total income** | **37** | **11.2** | **25.8** |
| **Financial expense** | | | |
| Financial expenses from the Parent | (9.8) | (1.3) | (8.5) |
| Interest expense on medium/long-term loans and related hedges | (172.7) | (121.2) | (51.5) |
| Debt adjustment (bonds) and related hedges | (0.2) | 0.0 | (0.2) |
| Discounting of post-employment benefits and other personnel-related provisions | (4.5) | (4.9) | 0.4 |
| Exchange losses | 0.0 | (5.6) | 5.6 |
| Other financial expense | (4.1) | (0.7) | (3.4) |
| Capitalised borrowing costs | 25.9 | 17.4 | 8.5 |
| **Total expense** | **(165.4)** | **(116.3)** | **(49.2)** |
| **Total** | **(128.4)** | **(105.1)** | **(23.4)** |

Net financial expense amounted to €128.4 million, entirely attributable to the Parent Company, comprising €165.4 million in financial expense and €37.0 million in financial income. The increase of €23.4 million with respect to the previous financial year is the net result of the following main factors:

- increased financial proceeds (€21.4 million) which were primarily attributable to the joint effect of:
  - greater liquidity invested at higher interest rates (€21.2 million);
  - lower late payment interest for the late payment of receivables in respect of dispatching activities (a negative €0.4 million);
  - recording of higher income for uplift fees (€0.7 million);
- greater net financial income (€2.0 million) mainly referring to the companies transferred (€1.4 million);
- adjustment to the currency exchange of the provision for probable expenses relating to the sale of the equity interest held in the Brazilian subsidiaries (€6.8 million);
- recognition of greater financial expense to the parent company CDP (a negative €8.5 million) deriving from the use of the loan of €500 million on 8 April 2011;
- greater financial expense deriving from medium and long-term debt and the related hedges (a negative €51.5 million) due to the increased gross debt and the rise in market interest rates in 2011;
- the net economic loss deriving from the fair value adjustment of bonds and the related hedges (a negative €2.4 million);
- lower financial expense deriving from the discounting of employee benefits (€0.4 million);
- greater capitalised financial expense (€8.5 million) as a result of greater capital expenditure during 2011 compared with the previous financial year.

### 9. Share of profit/(losses) from equity method-accounted investees - €7.4 million

This item includes the economic effects of the recognition and measurement as of 31 December 2011 of the equity interest in the Montenegro company CGES (€1.8 million), of the adjustment to the share of shareholders' equity held as of 31 December 2011 in the associates CESI S.p.A. (amounting to €5.5 million, up by €2.3 million on 2010) and CORESO (€0.1 million). The difference in the item (€4.8 million) with respect to the previous financial year's figure also suffers the 2010 impairment of the equity interest in the Tunisian joint venture Elmed Études (a negative €0.6 million) following the changed political situation in Tunisia, which, at present, makes it difficult to recover the investment.

## 10. Income taxes - €387.3 million

Income taxes for the financial year amount to €387.3 million, up by €140.5 million on the previous financial year, substantially by virtue of the "corrective manoeuvre-*bis*" (the "Robin Hood Tax"), which, against a pre-tax result basically in line with 2010, entailed greater taxes of 153.8 million during the financial year, determined by the recognition of greater net deferred tax liabilities for €65.4 million and greater current taxes for €88.4 million.
The following table reports changes in taxes with respect to 2010:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| **Income taxes of the year** | | | |
| Current taxes: | | | |
| - IRES | 334.4 | 238.7 | 95.7 |
| - IRAP | 66.1 | 59.2 | 6.9 |
| **Total current taxes** | **400.5** | **297.9** | **102.6** |
| New temporary differences: | | | |
| - deferred tax assets | (56.3) | (13.9) | (42.4) |
| - deferred tax liabilities | 0.0 | 0.0 | 0.0 |
| Reversal of temporary differences: | | | |
| - deferred tax assets | 17.8 | 11.5 | 6.3 |
| - deferred tax liabilities | (56.6) | (43.7) | (12.9) |
| Adjustment - tax restatement of IRES pursuant to Italian Law Decree no. 138 of 13.08.2011 (Robin Hood Tax) | 77.6 | 0.0 | 77.6 |
| Adjustment - restatement of IRAP (pursuant to paragraph 5 of Art. 23 of Italian Law Decree no. 98 of 06.07.2011) | 5.3 | 0.0 | 5.3 |
| **Total change in deferred tax assets and liabilities** | **(12.2)** | **(46.1)** | **33.9** |
| Adjustment of prior-year taxes | (1.0) | (5.0) | 4.0 |
| **Total** | **387.3** | **246.8** | **140.5** |

### Current taxes

Current taxes include an increase of €102.6 million with respect to the balance of the previous financial year, due, as described above, to the increase in the IRES rate, from 27.5% to 38% as a result of the above manoeuvre (€88.4 million) and to the adjustment of the IRAP rate relating to the effects of the economic manoeuvre for concession holders (pursuant to Art. 23, paragraph 5 of Italian Law Decree no. 98 of 6 July 2011, which determined greater current taxes for €4.2 million. The item also reflects recognises the value of substitute tax paid by the Parent Company during the financial year (€16.3 million) for the release of goodwill, recognised on the consolidated financial statements with the 2009 acquisition of the subsidiary Terna Rete Italia (pursuant to Italian Law Decree no. 98 of 6 July 2011).

### Deferred tax assets and liabilities

Deferred tax assets and liabilities, totalling a negative €12.2 million, showed a net change of €33.9 million with respect to 2010. The change is mainly attributable to:

- application of greater tax rates that has, in fact, entailed the overall recalculation of deferred tax liabilities of the start of the financial year (€82.9 million, equal to €77.6 million as a result of the Robin Hood Tax and €5.3 million for additional IRAP);
- recognition of deferred tax assets (€39.8 million) for the release of the goodwill recorded on the consolidated financial statements following the acquisition of the company Terna Rete Italia;
- release of the share attributable to the year (€3.8 million) of the advances allocated for the release of the goodwill recorded on the financial statements of the Parent Company following the merger of RTL (pursuant to Italian Legislative Decree no. 185/2008);
- greater utilisation of prior period accruals covering the additional depreciation and amortisation recorded by the Parent Company Terna and the subsidiary Terna Rete Italia (€10 million), including the amount released in relation to the depreciation charge for the year associated with merger differences allocated to property, plant and equipment at the time of the mergers carried out in prior years (€1.6 million).

### Adjustment of prior-year taxes

Adjustment of prior-year taxes, amounting to a negative €1.0 million, referring to greater current taxes paid in previous years, record a change for €4.0 million with respect to the 2010 figure (amounting to a negative €5.0 million).

The effective rate of income tax (which totalled €387.3 million) on profit before taxes came to 54.2% (amounting to 54.3%, without taking into account adjustments from previous years), with respect to 34.7% in 2010 (amounting to 35.4%, without taking into account adjustments from previous years).
The greater taxes recognised for the adjustment of the balance at the start of the financial year of the deferred tax liabilities have affected profit before taxes by 11.6 percentage points; the tax rate for the financial year, without considering this adjustment, of the corrections made in relation to previous years and net of the comprehensive tax effect of the release of goodwill relating to Terna Rete Italia stands at 46%, up 10.6% with respect to the figure of the previous financial year, basically as a result of the greater tax rates described above (10.7% for the Robin Hood Tax and 0.5% for additional IRAP).

For a clearer presentation of the differences between the theoretical and actual tax rates, the table below reconciles the profit before taxes with taxable income for IRES (corporate income tax) purposes:

| € million | 2011 | 2010 |
|---|---|---|
| Profit before taxes | 714.6 | 711.9 |
| **Theoretical tax (38%)** | **271.5** | **195.8** |
| IRAP | 66.1 | 59.2 |
| Permanent differences | 50.7 | (3.2) |
| *of which adjustment - restatement pursuant to Italian Law Decree no. 138 of 13.08.2011 (the "Robin Hood Tax")* | *77.6* | |
| *of which adjustment - restatement for IRAP (pursuant to paragraph 5 of Art. 23 of Italian Law Decree no. 98 of 06.07.2011)* | *5.3* | |
| **Actual tax charge** | **388.3** | **251.8** |
| **Actual tax rate** | **54.3%** | **35.4%** |
| Adjustment of prior-year taxes | (1.0) | (5.0) |
| **Actual tax net of prior year adjustments** | **387.3** | **246.8** |

## 11. Profit for the year from discontinued operations and assets held for sale - €112.7 million

Pursuant to accounting standard IFRS 5 – Non-current assets held for sale and discontinued operations, the item, amounting to €112.7 million, includes:

- the related income, amounting to €50.6 million (net of expenses for contractual guarantees amounting to €11.9 million and discounting the tax effect) recorded upon conclusion of the sale of the equity investment held in Rete Rinnovabile S.r.l. in the first quarter of 2011; in particular, as extensively described in the consolidated financial statements at 31 December 2010, as a consequence of the sale agreement, this income essentially derives from the optimisation of the 2011 margin on the construction of the related photovoltaic plants concerned by the sale. It is pointed out that this sale generated total net proceeds of around €196 million (of which €146.8 million recognised in 2010, as contract margin with respect to the total costs sustained during the year, on the basis of the work progress);
- the partial release of the provision allocated in 2009 for €33.8 million, inclusive of the related exchange gains or losses, with reference to contractual obligations, which expired during the financial year, deriving from the sale of the majority share package in Terna Participações;
- the net income originating from the sale of the company Nuova Rete Solare, formalised on 24 October 2011, amounting to €28.3 million, as the difference between the price of the sale and the book value of the assets and liabilities sold (€70.7 million), net of expenses for contractual guarantees and other accessory sales expenses (€31.7 million) and taxes relating to the operation (€10.7 million).

As specified previously, the 2010 comparative figure (of €146.9 million) substantially included the net margin for 2010 realised with the photovoltaic plants sold with the companies Rete Rinnovabile S.r.l. and Valmontone Energia (€146.8 million).

With reference to the sale of the equity interest in Rete Rinnovabile S.r.l. (and in its subsidiary Valmontone Energia S.r.l.), below are details of the economic items that determined the net income for the financial year under the scope of discontinued operations and assets held for sale:

| € million | 2011 |
|---|---|
| Total revenue | 122.5 |
| Total operating expenses | (76.5) |
| **Period gross contract result** | **46.0** |
| Capital gains on net other assets sold | 13.8 |
| Expenses for contractual guarantees | (11.9) |
| Income taxes | (2.7) |
| **RTR Group net profit for the year from discontinued operations** | **50.6** |

With reference to the sale of the equity interest in Nuova Rete Solare S.r.l., please note that the net income realised includes the contribution to the consolidation of the company's financial year result accrued at the date of the sale for €1.8 million. The economic items that determined the net profit of the discontinued operations and assets held for sale (€28.3 million) deriving from the sale of NRTS are as follows:

| € million | 2011 |
|---|---|
| Capital gain net of expenses for contractual guarantees and other accessory expenses | 37.2 |
| Capital gain tax | 10.7 |
| **Net capital gain** | **26.5** |
| **Profit from discontinued operations and assets held for sale pertaining to the Group** | **1.8** |
| **Profit from discontinued operations and assets held for sale - NRTS** | **28.3** |

Basic earnings per share in 2011, which corresponds to diluted earnings per share, from discontinued operations and assets held for sale amounts to €0.056 (with a numerator of €112.7 million and a denominator of 2,099,992.0 thousand). Below is a breakdown of the income obtained by NRTS during the financial year until the date of its sale:

| € million | 2011 |
|---|---|
| Total revenue | 2.2 |
| Total operating expenses | (1.0) |
| **EBIT** | **1.2** |
| Financial income/(expense) | 0.5 |
| **Profit before taxes** | **1.7** |
| **Income taxes** | **(0.1)** |
| **Profit 08.03 - 24.10.2011 from discontinued operations and assets held for sale pertaining to the Group** | **1.8** |

## 12. Earnings per share

The basic and diluted earnings per share from continuing and discontinued operations and assets held for sale is €0.219 (numerator of €440.0 million being the sum of the profit from continuing operations, €327.3 million, and that from discontinued operations and assets held for sale for €112.7 million and denominator of 2,009,992.0 thousand).
Basic earnings per share, which corresponds to diluted earnings per share, from continuing operations amounts to €0.163 (with a numerator of €327.3 million and a denominator of 2,009,992.0 thousand).

# D. Notes to the consolidated statement of financial position

## Assets

### 13. Property, plant and equipment - €8,618.2 million

Property, plant and equipment amounts to €8,618.2 million (€7,802.6 million at 31 December 2010). The amount and changes for each category are reported in the following table:

| € million | Land | Buildings | Plant and machinery | Industrial and commercial equipment | Other assets | Assets under construction and payments on account | Total |
|---|---|---|---|---|---|---|---|
| **Cost at 01.01.2011** | **81.7** | **958.0** | **11,090.7** | **62.7** | **93.1** | **930.1** | **13,216.3** |
| Investments | 0.4 | 17.8 | 11.5 | 3.4 | 18.5 | 1,126.5 | 1,178.1 |
| Entry into use | 11.5 | 142.2 | 723.3 | 1.8 | 5.0 | (883.8) | 0.0 |
| Intra-group sales/acquisitions | | (0.6) | (1.0) | | | 1.6 | 0.0 |
| Disposals and impairment | | (0.6) | (45.5) | (0.2) | (10.8) | (3.3) | (60.4) |
| Other changes (grants) | | | (8.6) | | | (3.5) | (12.1) |
| Reclassifications | 0.1 | (0.1) | | (0.40) | 0.40 | | 0.0 |
| **Cost at 31.12.2011** | **93.7** | **1,116.7** | **11,770.4** | **67.3** | **106.2** | **1,167.6** | **14,321.9** |
| **Accumulated depreciation and impairment at 01.01.2011** | **0.0** | **(286.1)** | **(5,030.8)** | **(41.4)** | **(55.4)** | **0.0** | **(5,413.7)** |
| Depreciation charge for the year | | (25.1) | (302.5) | (3.6) | (12.1) | | (343.3) |
| Disposals | | 0.6 | 42.4 | 0.2 | 10.1 | | 53.3 |
| Reclassifications | | 0.1 | | | (0.1) | | 0.0 |
| **Accumulated depreciation and impairment at 31.12.2011** | **0.0** | **(310.5)** | **(5,290.9)** | **(44.8)** | **(57.5)** | **0.0** | **(5,703.7)** |
| **Carrying amount** | | | | | | | |
| At 31.12.2011 | 93.7 | 806.2 | 6,479.5 | 22.5 | 48.7 | 1,167.6 | 8,618.2 |
| At 31.12.2010 | 81.7 | 671.9 | 6,059.9 | 21.3 | 37.7 | 930.1 | 7,802.6 |

"Plant and equipment", at 31 December 2011, includes the energy transportation network as well as the transformation stations in Italy.

The item shows an increase on the previous financial year amounting to €815.6 million, as a result of ordinary transactions made during the financial year, relating to:

- investments for the financial year for €1,178.1 million, of which €1,168.7 million made under the scope of the Group's core business (and relating to the Parent Company Terna for €1,122.7 million, to the subsidiaries Terna Rete Italia and Terna Cnra Gora respectively for €44.5 million and €1.5 million); under the scope of diversified activities, the subsidiary SunTergrid contributes with investments for €9.4 million;
- depreciation for the year (a negative €343.3 million);
- divestments (a negative €7.1 million) and contributions directly reducing the value of the operating plants and plants under construction (a negative 12.1 million).

A summary of changes in property, plant and equipment during the year is provided in the table below:

| € million | |
|---|---|
| Investments | |
| - Transmission lines | 476.3 |
| - Transformation stations | 569.4 |
| - Other | 123.0 |
| **Total investments in property, plant and equipment - core business** | **1,168.7** |
| Investments in property, plant and equipment - non-core business (SunTergrid) | 9.4 |
| **Total investments in property, plant and equipment** | **1,178.1** |
| Depreciation | (343.3) |
| Divestments and other changes | (19.2) |
| **Total** | **815.6** |

With reference to investments made during the financial year in core business (€1,170.3 million), please note, in particular, those of the Parent Company, mainly in relation to the progress of works in relation to Sorgente-Rizziconi (€117.5 million), with the development of civil works of the stations of Scilla (Calabria) and Sorgente (Sicily) and the laying of the first out of six submarine cables between Villafranca and Favazzina for the development of the 380 kV double three-phase power line connection, the conclusion of preliminary works for the development of the tunnel in Favazzina and the development of the 380 kV long-distance power lines (overhead part) on the Calabria side; development of two new 380 kV power stations in the municipalities of Chignolo Po and Maleo and the new double three-phase power line between the stations along the La Casella-Caorso line (€69.0 million); the purchase of the armouring in the station of Piossasco with a view to developing the HVDC interconnection Italy-France (€39.7 million); works on 380 kV stations suited to reducing congestion and connection to new renewable fuel generating plants located in the areas of Maida, Bisaccia, Deliceto, Troia, South Brindisi, Castellaneta, Tuscania and Rotello; the installation of a PST (System Phase Shifter) in the Foggia power station (€27.7 million); progress of works for the development of the Avellino North station aimed at connecting Montecorvino-Benevento (€25.1 million); completion of the civil works and start of electromechanical assemblies in the Aliano station for the restructuring of the north Calabria grid (€21.6 million); development of foundations prior to starting assembly of the supports to the Trino-Lacchiarella long-distance power line (€17.9 million).
In terms of assets under construction at the end of the year, the main Parent Company grid development and upgrading projects worth more than €5 million are listed below.

| **Transmission lines** | euros |
|---|---|
| Sorgente-Rizziconi 380 kV Power Line | 83,346,291 |
| Rationalis. 380 kV in the Province of Lodi | 42,791,833 |
| Valcamonica (Phase A1) | 23,415,387 |
| Trino-Lacchiarella 380 kV Power Line | 17,767,292 |
| SA.PE.I. | 17,284,706 |
| Restructuring of the 220 kV Line in Naples | 14,960,900 |
| Restructuring of Metropolitan Area of Rome | 10,473,773 |
| Paternò-Pantano-Priolo | 10,398,598 |
| Pot.150 kV Collect. Wind Pwr Prod. Campania | 7,798,939 |
| Alta Valtellina (Phase A2) | 7,712,546 |
| Restructuring of Carpi Fossoli (Mo) Grid | 7,603,343 |
| **Transformation stations** | |
| Piossasco 380/220/132 kV station | 36,928,055 |
| Foggia 380 kV station | 27,712,675 |
| Avellino North 380 kV station | 17,119,347 |
| Maleo 380 kV station | 16,691,204 |
| Camporosso 220 kV station | 15,201,380 |
| Aliano 380 kV station | 14,408,214 |
| Rotello 380/150 kV station | 13,753,293 |
| Castellaneta 380/150 kV station | 12,378,073 |
| Villanova station | 11,828,989 |
| Chignolo Po 380 kV station | 9,510,754 |
| Troia 380/150 kV station | 9,172,910 |
| Scilla 380/150 kV station | 8,945,146 |
| Tuscania 380 kV station | 8,852,128 |
| Villafranca 380/150 kV station | 8,743,511 |
| Turin North 220 kV station | 7,962,087 |
| Sorgente 380/150 kV station | 6,811,194 |
| Sorgente 380/150 kV station | 6,768,097 |
| Meduno station | 6,660,380 |
| Cardano station | 6,369,747 |
| Fiumesanto station | 6,067,783 |
| Marianopoli 150 kV station | 6,016,355 |

## 14. Goodwill - €190.2 million

Goodwill amounted to €190.2 million and it is unchanged as compared to the balance of the previous year.

### Impairment testing

#### Cash Generating Unit - Terna Group

The recoverable amount of the goodwill arising from the acquisition of Terna Rete Italia, (recognised in the consolidated accounts in the amount of €101.6 million) was estimated on the basis of the value of use criteria, applying the unlevered version of the discounted cash flow method to Terna Group Cash Generating Unit.
The forecast of cash flows was prepared over the time frame 2012-2021; in particular cash flows were determined up to 2016 on the basis of the business plan, while for subsequent years the cash flow projection was made assuming business development operations in line with the last year of the business plan and, for investment only, considering the information of the ten-year NTG development plan. The business plan has been developed considering the latest estimates of the electricity sector and the latest macroeconomic forecasting in addition to the news introduced by the latest review of the tariffs (IV regulatory period) and by Italian Law Decree no. 138/11 (introduction of the Robin Hood Tax with additional IRES of +10.5% in 2011-2013 and +6.5% from 2014). The final value was assumed to be equal to the RAB (Regulatory Asset Base) at the end of 2021 and the adopted discount rate was equal to 4.95%. The value in use of the CGU determined as indicated above was €3,767 million higher than the carrying amount. The excess value in use of the CGU comes to zero if WACC increases up to 9.48%.

#### Cash Generating Unit - Terna

The recoverable amount of the goodwill arising from the acquisition of RTL (merged into the Parent Terna in 2008), recognised in the financial statements in the amount of €88.6 million on the basis of the value in use was estimated by applying the unlevered version of the discounted cash flow method to the Cash Generating Unit (CGU) - Terna.
Forecast cash flows have been estimated in line with the approach followed by the Group solely with regard to the relevant scope. The discount rate adopted was 4.85%.
The value in use of the CGU, determined as indicated above, was €3,263 million higher than the carrying amount. The excess value in use of the CGU comes to zero if WACC increases up to 9.04%.

## 15. Intangible assets - €280.7 million

Changes during the year in intangible assets are detailed below:

| € million | Infrastructure rights | Concessions | Other assets | Assets under development and payments on account | Total |
|---|---|---|---|---|---|
| **Balance at 31.12.2010** | **106.4** | **106.5** | **37.8** | **29.7** | **280.4** |
| Investments | | | 0.2 | 50.9 | 51.1 |
| Entry into use | 36.5 | | 17.0 | (53.5) | 0.0 |
| Amortisation | (25.1) | (5.6) | (20.1) | | (50.8) |
| Other changes (grants) | | | | | 0.0 |
| Reclassifications | | | | | 0.0 |
| **Balance at 31.12.2011** | **117.8** | **100.9** | **34.9** | **27.1** | **280.7** |
| Cost | 276.1 | 135.4 | 128.9 | 27.1 | 567.5 |
| Accumulated amortisation | (158.3) | (34.5) | (94.0) | - | (286.8) |
| **Balance at 31.12.2011** | **117.8** | **100.9** | **34.9** | **27.1** | **280.7** |

Intangible assets amount to €280.7 million (€280.4 million at 31 December 2010). This item, in particular, includes:

- the infrastructure used for the dispatching service, as from 1 January 2010, booked in accordance with the provisions of IFRIC 12 – Service concession arrangements, with a net carrying amount at 31 December 2011, of €117.8 million for infrastructure already in use and €23.1 million for the infrastructure under construction classified in the "Assets under construction and payments on account" caption, and a net carrying amount at 31 December 2010, of €106.4 million for infrastructure already in use and €25.1 million for the infrastructure under construction classified in the "Assets under construction and payments on account" caption;
- the licensing for the provision of electricity transmission and dispatching services in Italy (with net carrying amount of €100.9 million at 31 December 2011), recognised initially during 2005 at fair value and subsequently measured at cost.

Other intangible assets comprise application software developed internally or purchased when implementing systems development projects. Related investments (€16.7 million) are made essentially through internal development.
The difference, which is not significant with respect to the previous financial year (€0.3 million) is due to the combined effect of routine movements during the period, regarding mainly to investments (€51.1 million, including €34.4 million in infrastructure rights) - mainly in application software - and amortisation (€50.8 million, of which €25.1 million in relation to dispatching infrastructures and €5.6 million relative to licensing).
Investments for the year in intangible assets (€51.1 million, of which €49.7 million refer to the Parent Company and €1.4 million to the subsidiary Terna Rete Italia) included expenditure on the development and evolution of software for the remote management system for dispatching (€13.0 million), for the Power Exchange (€11.0 million) and for the protection of the electrical system (€0.8 million), as well as software applications and licenses (€14.3 million).

## 16. Equity accounted investee - €66.8 million

This item amounts to €66.8 million and relate to the shareholdings of the Parent Company Terna S.p.A.:
- in the associate CESI S.p.A. (€30.4 million), representing a stake of 42.406%;
- in the associate CORESO S.A. (€0.4 million), which was acquired in November 2010, representing a stake of 22.485%;
- in the associate CGES - CrnoGorski Elektroprenosni Sistem AD (€36.0 million), which was acquired in January 2011, representing a stake of 22.0889%.

CESI S.p.A. operates in the construction and management of laboratories and plants for tests, inspections, studies and experimental research relating to the electro-technical field in general and technical and scientific developments in that area.
The value of the equity interest increased by €7.1 million on previous year as a result of the recognition of the cost incurred for the acquisition (completed by the Parent Company during the financial year) of additional interests in Tirreno Power S.p.A. for 1.5% and by SO.GI.N - Società di Gestione Impianti Nucleari S.p.A. for 1% of the share capital (€1.6 million) and the adjustment of the equity investment in the shareholders' equity held by the Group at the end of the year (€5.5 million).
As is permitted by current legislation, CESI opted not to not to apply IFRSs to prepare its financial statements as at 31 December 2011. The financial statements at 31 December 2011 of the associate CESI were therefore prepared in accordance with the Italian GAAPs.
The company CORESO S.A. is the first technical centre owned by various electrical energy transmission companies which implements joint TSO technical coordination activities in order to improve and strengthen security and coordination of the electrical system in central/western Europe; it prepares daily forecasts and analyses in real time of energy flows in the region, identifying potentially critical areas and promptly notifying the TSOs which are affected.
CGES is the electricity dispatch and transmission operator in Montenegro. The financial investment of Terna in CGES, which was made following an industrial cooperation and country system and included as part of inter-governmental understandings reached by Italy and Montenegro, sanctions the institutional commitment to the development of a new submarine electrical interconnection and the implementation of the partnership between national transmission operators.
The value of the shareholding in the Tunisian joint venture ELMED Études Sarl (equal to 50% of share capital) was brought to zero as early as 31 December 2010 due to the write-down of the investment itself (€0.7 million). The write-down was required by the changed political situation in Tunisia in the previous financial year which currently makes the investment difficult to recover.

The main figures of the above associates, restated in accordance with the presentation and measurement criteria applied by Terna Group, are as follows:

| Company | Assets | | Liabilities | | Equity | Revenue | Profit for the year |
|---|---|---|---|---|---|---|---|
| € million | Current | Non-current | Current | Non-current | | | |
| CESI | 91.8 | 51.8 | 41.8 | 28.6 | 73.2 | 104.4 | 14.4 |
| CORESO | 1.0 | 1.7 | 1.4 | - | 1.3 | 4.8 | 0.1 |
| CGES | 57.6 | 136.8 | 9.4 | 21.9 | 163.1 | 26.5 | 4.7 |
| ELMED Études | 1.1 | - | 0.1 | - | 1.0 | - | (0.3) |

## 17. Financial assets

The following table details financial assets recognised in the consolidated financial statements:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| FVH derivatives | 521.8 | 200.3 | 321.5 |
| Other investments: | 0.6 | 0.5 | 0.1 |
| **Non-current financial assets** | **522.4** | **200.8** | **321.6** |
| Other current financial assets | 155.5 | 0.5 | 155.0 |
| **Current financial assets** | **155.5** | **0.5** | **155.0** |

At 31 December 2011, "Non-current financial assets", amounting to €522.4 million, reported the value of fair value hedge derivatives hedging against of bonds as well as the value of other equity interests held by the Parent Company.
The increase in the fair value of derivatives (€321.5 million) as compared with 31 December 2010 is due to the rate curve declining in the long-term part, which has impacted both the fair value of new fair value hedge derivatives subscribed to hedge the bond issued in March 2011 (€140.0 million) and the fair value of derivatives existing as at 31 December 2010 (€181.5 million).
"Other investments" (€0.6 million) refers to:

- the interest held of 5.6% in the share capital of Desertec Industrial Initiative ("DII") (€0.1 million) acquired in September 2010;
- the interest held of 8.3% in the share capital of CASC CWE S.A. (€0.3 million) acquired in November 2010;
- the 5% interest held in the share capital of Medgrid SAS (€0.2 million, which has increased by €0.1 million following the subscription of the capital increase of the subsidiary).

"Current financial assets" of €155.5 million (€0.5 million at 31 December 2010) rose from the previous year by €155.0 million mainly due to the subscription of deposit certificates maturing on 14 June 2013 and with the faculty to request early redemption every three months (€150 million) and to interest accrued and not yet collected at the reporting date concerning deposit certificates and short-term liquidity investments (€4.9 million).

## 18. Other assets

"Other assets" are analysed below:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| Receivables due from others: | | | |
| - loans and advances to employees | 6.1 | 5.9 | 0.2 |
| - deposits with third parties | 0.5 | 0.4 | 0.1 |
| **Other non-current assets** | **6.6** | **6.3** | **0.3** |
| Other tax receivables | 11.1 | 4.6 | 6.5 |
| Receivables due from others: | | | |
| - advances to employees | 0.2 | 0.2 | 0.0 |
| - others | 9.2 | 15.5 | (6.3) |
| **Other current assets** | **20.5** | **20.3** | **0.2** |

**"Other non-current assets"** (€6.6 million) - which are reported in the table above – are essentially unchanged since the end of last year (€6.3 million) and mainly comprise loans and advances paid to employees of the Parent Company (€6.1 million).

**"Other current assets"**, amounting to €20.5 million, which are reported in the table above, show an insignificant change (€0.2 million) with respect to the balance at 31 December 2010, mainly as a result of the combined effect of the following:

- greater tax receivables (€6.5 million) mainly for the withholdings and tax receivables from the tax office on interest income accrued on financial assets (€4.5 million) and the greater net VAT receivable of the Group from the tax office (€1.8 million);

- lower receivables from others (€6.3 million), mainly regarding:
  - decreased quotas of previously paid costs which accrue in subsequent years (a negative €4.9 million) and which are ascribable to insurance premiums;
  - collection by the Parent Company of the receivable for an insurance reimbursement, ascertained at end of financial year 2010 (approximately a negative €1.9 million);
  - the booking of revenue which accrued during the year and which was not yet collected at the reporting date (€1.2 million) and relating to the rentals for the use by Enel Distribuzione of the Company's infrastructures, aiming to ensure power line communication.

## 19. Inventories - €16.3 million

Current inventories amounting to €16.3 million (€11.4 million at 31 December 2010) consist of materials and equipment intended for the operation, maintenance and construction of plants; the increase of €4.9 million is mainly attributable to the purchase value of the photovoltaic modules acquired during the financial year by the subsidiary SunTergrid and to be realised through sale (in compliance with the provisions of Italian Legislative Decree no. 93 of 1 June 2011).

## 20. Trade receivables - €1,690.2 million

Trade receivables are analysed as follows:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| Energy-related receivables | 1,258.0 | 1,117.0 | 141.0 |
| Grid transmission fees receivables | 356.7 | 304.8 | 51.9 |
| Other trade receivables | 75.5 | 74.0 | 1.5 |
| **Trade receivables** | **1,690.2** | **1,495.8** | **194.4** |

Trade receivables amount to €1,690.2 million. The increase (€194.4 million) with respect to the previous year mainly comprises pass-through amounts deriving from the electricity dispatching activities carried out by the Parent Company.
Receivables are measured net of impairment losses on items considered non-collectable that are covered by allowances for doubtful accounts (€16.9 million for energy items and €6.7 million for other items in 2011), which is basically in line with the previous financial year.

### Energy-related receivables - €1,258.0 million

They mainly include receivables in relation to the "pass-through" energy items arising in respect of dispatching activities. This item also includes receivables for fees payable by market operators for dispatching activities (DIS fee as per AEEG Resolution no. 237/04 and its subsequent amendments and supplements).
The increase in this caption by €141.0 million vis-à-vis the end of last year was mainly due to:

- additional receivables for the accrued incentives associated with the reduction in volumes procured from the Market for Dispatching Service, made available under AEEG Resolution 213/09 (€66.0 million), partially offset by the collection of the receivable connected with the premium recognised on the basis of said incentive accrued in 2009, in accordance with AEEG Resolution 206/08 includes also the receivable related to the quality of the transmission service (€7.7 million);
- increased receivables for the sale of electricity within the Power Exchange (€77.0 million), mainly deriving from the net effect of increased receivables for the uplift component (€131.5 million), from the recognition of receivables booked on the market coupling mechanism for the management of congestion on the inter-connection with Slovenia (€14.3 million), for the greater receivables generated by the increased quantities and prices of the measurement of the imbalance (€32.0 million); partly offset, as described under "Trade payables", by the reduction in the volumes of resources attained from energy market (€50.7 million), by the reduction in credit items relating to the price to cover the costs of the modulation of wind power production pursuant to Article 44-*bis* of AEEG Resolution 111/06 (€17.5 million), by the reduction in receivables relating to the dispatch of electricity produced by non-programmable renewable sources envisaged by Resolution ARG/elt 5/10 (€11.3 million) and by lower payables deriving from virtual inter-connection activities (€22.7 million);
- greater receivables for the sale of electricity outside the Power Exchange (€16.5 million), mainly as a result of the recognition (€16 million) of the price for the transitory safeguarding service envisaged by Art. 25-*bis*, Resolution ARG/elt 107/09.

### Grid transmission fees receivable - €356.7 million

The grid transmission fees receivable, €356.7 million, reflect the remuneration paid to the Parent Company and other owners for the use of the National Transmission Grid by distributors of electricity. Said receivable recognises a positive change amounting to €51.9 million with respect to the previous financial year, mainly as a net result of the recognition of the receivable due from CCSE for the optional adhesion to the "mitigation" mechanism established by Resolution ARG/elt 188/08 to cover the risk connected with a drop in consumption (€71.1 million) and by the receivable recognised to the Parent Company for the grid transmission fee adjustment in previous years; partially offset (a negative €16.8 million) by the collection of the receivable due from CCSE for the incentive on the remuneration of investments in strategic transmission infrastructures recognised the previous financial year (Resolution ARG/2011/elt 87/10).

### Other trade receivables - €75.5 million

Other trade receivables mainly regard receivables due from clients of the diversified businesses; they reported an increase of €1.5 million with respect to the previous year and primarily due to the net effect of:

- increased receivables due from third party customers of the Parent Company (€8.3 million) and which are primarily derived from orders underway in relation to stations and connections;
- greater receivables of the Parent Company for diversified business mainly relating to rentals and optical fibre housing (€7.2 million);
- lesser receivables (a negative €14.2 million) for invoices to be issued to customers of the Parent Company mainly following completion of the sale of photovoltaic panels on the basis of specific contractual agreements, to contracting companies appointed to build photovoltaic plants owned by Group companies sold during the financial year.

This item also includes receivables for contract work in progress (€1.7 million) relative to works of multi-year duration, shown in the table below, which the Parent Company has been implementing with third party customers and which increased with respect to the previous year by €0.6 million:

| € million | Payments on account | Contract value | Balance at 31.12.2011 | Payments on account | Contract value | Balance at 31.12.2010 |
|---|---|---|---|---|---|---|
| Others | (13.5) | 15.2 | 1.7 | (11.1) | 12.2 | 1.1 |

The amount of the guarantees issued to third parties by the Parent Company Terna at 31 December 2011 comes to €42.2 million and refers for €22.2 million to sureties issued to secure the contractual obligations arising under the scope of operations and for €20.0 million to a guarantee issued on Terna credit lines but in the interest of the subsidiary SunTergrid S.p.A. for commitments made under the scope of the sale of Nuova Rete Solare S.r.l..

## 21. Cash and cash equivalents - €1,114.9 million

Cash and cash equivalents at 31 December 2011 amount to €1,114.9 million of which €765.0 million are liquid funds invested in term deposits, €349.8 million as net liquidity on bank current accounts and €0.1 million as cash on hand held by the Territorial Operational Units of the Parent Company.

## 22. Income tax assets - €4.4 million

Income tax assets amount to €4.4 million and mainly refer to the receivable due from the tax office, recognised in 2010, in accordance with Art. 6 of Italian Law of 28 January 2009, for the greater income tax paid in previous years, as a result of the failure to deduct IRAP in the amount permitted by the legislation in question.
The increase in this item (€0.2 million) with respect to the previous financial year is due to payment of the IRES advance by the subsidiary SunTergrid S.p.A..

# Liabilities

## 23. Equity attributable to the owners of the parent - €2,751.0 million

### Share capital - €442.2 million

The share capital of the Parent Company is represented by 2,009,992,000 ordinary shares, par value €0.22 each. The increase of €1.2 million with respect to the previous year reflects the issue of 5,596,300 shares, during 2011, in relation to the Stock Option Plan described later in this report.

### Legal reserve - €88.2 million

The legal reserve amounts to 20% of the share capital of the Parent Company at 31 December 2010. The increase of €0.2 million from last year, which restores this ratio of legal reserve and share capital, was resolved by the Shareholders' Meeting on 13 May 2011, as they met to approve the separate financial statements of Terna and to allocate the net profit for financial year 2010.

### Other reserves - €678.7 million

Other reserves have reduced by a net amount of €40.3 million as a result of:

- "Other comprehensive income" (€50.7 million): adjustment to fair value of derivatives hedging floating-rate loans of the Parent Company (€64.1 million) and RTR, sold (€22.1 million) - cash flow hedges net of the related tax effect (€29.4 million and €6.1 million, respectively);
- transactions with shareholders (a negative €10.4 million): increase in the share price premium reserve (a negative €11.4 million) and decrease in the stock option reserve (a negative €1.0 million) to reflect the stock options exercised during the year.

### Retained earnings and losses carried forward - €1,262.7 million

The increase of the year of the item "Retained Earnings/Losses carried forward" of €190.6 million essentially refers to the allocation of the residual profit of the Group in 2010 compared to the distribution of the 2010 dividend on the part of the Parent Company (€421.6 million). The opening balance incorporates the change to comparative data at 31 December 2010 (for €14.2 million) as a consequence to the change in the accounting policies relative to the booking of the release in financial year 2009 of goodwill deriving from the merger into Terna of RTL, in compliance with Art. 15 of Italian Legislative Decree no. 185/2008.

### Interim dividend

After receiving the report of the independent auditors PricewaterhouseCoopers required by Art. 2433-*bis* of the Italian Civil Code, on 9 November 2011 the Parent Company's Board of Directors approved the distribution of an interim dividend amounting to €160.8 million, equal to €0.08 per share, which is payable on 24 November 2011, with an ex dividend date (coupon 15) of 21 November 2011.

### Terna S.p.A. Stock Option Plans

On 21 December 2005, based on proposals presented by the Remuneration Committee, the Company's Board of Directors approved a Stock Option Plan for 2006 applicable to those senior managers of Terna who hold key roles in terms of achieving the Company's strategic objectives.

This plan is aimed at giving Terna - in line with international best practice and that of the leading Italian companies listed on the Stock Exchange - a management incentive and loyalty tool that imbues key employees with a sense of belonging to the corporate team, while ensuring they are constantly focused on creating value, with a view to melding the interests of shareholders and management.

The 2006 Stock Option Plan entailed the granting, on 21 December 2005, of 9,992,000 options with a strike price of €2.072 to 17 managers of the Company. The Board of Directors verified that the conditions to exercise were met when it approved the financial statements of 31 December 2006.

Options in circulation at the start of 2011, amounting to 5,596,300, were all exercised.

The weighted-average prices of the shares at their exercise dates were:

- €3.318 (*) at 21 February 2011;
- €3.292 (*) at 22 February 2011;
- €3.282 (*) at 23 February 2011;
- €3.298 (*) at 24 February 2011;
- €3.323 (*) at 25 February 2011;
- €3.338 (*) at 28 February 2011;
- €3.382 (*) at 27 April 2011.

(*) Source: Bloomberg.

Fair value at the grant date was determined using the Cox-Rubinstein pricing method, which takes account of Terna's stock price at the grant date, the volatility of the security, and the rate curve at the grant date considering the term of the plan. The following pricing parameters were used:
- closing price (underlying or spot price) for the stock on the grant date (source Bloomberg) of €2.058;
- strike price amounting to €2.072;
- rate curve for calculating the discount factors at the grant date (source Reuters);
- historical volatility of the stock identified at the grant date (source Bloomberg) of 14.860%.

## 24. Loans and financial liabilities

The following table details loans and financial liabilities recognised in the consolidated financial statements at 31 December 2011:

| | Carrying amount | | |
|---|---|---|---|
| € million | 31.12.2011 | 31.12.2010 | Change |
| Bonds | 4,303.9 | 2,728.2 | 1,575.7 |
| Bank loans | 2,434.8 | 2,419.3 | 15.5 |
| **Long-term loans** | **6,738.7** | **5,147.5** | **1,591.2** |
| CFH derivatives | 111.4 | 47.1 | 64.3 |
| **Non-current financial liabilities** | **111.4** | **47.1** | **64.3** |
| Short-term loans | 0.0 | 73.1 | (73.1) |
| Current portion of long-term loans | 59.7 | 59.7 | 0.0 |
| Short-term loans and current portion of medium/long-term loans | 59.7 | 132.8 | (73.1) |
| **Total** | **6,909.8** | **5,327.4** | **1,582.4** |

Gross debt for the year increased with respect to the previous year by €1,582.4 million to €6,909.8 million.
The increase in the value in bonds (€1,575.7 million) is due for €1,234.8 million to the new bond issue in 2011 net of the costs and issue discounts for €321.8 million to the change in the fair value of the risk hedged and for €2.0 million to the amortised cost and for €17.1 million to the capitalisation of year inflation.
The change linked to the hedging of the interest rate risk comprises €48.1 million in relation to the inflation-linked bond issue, €91.8 million associated to the bonds 2014-2024, €41.7 million for the private placement and €140.2 million relating to the bonds issued in 2011.
The latest official prices for the bond listed on the Luxembourg Stock Exchange are detailed below:
- bond maturing 2024, 2011 price: 93.85; 2010 price: 104.23;
- bond maturing 2014, 2011 price: 102.42; 2010 price: 105.70;
- bond maturing 2023, 2011 price (*): 82.00; 2010 price: 96.57;
- bond maturing 2019, 2011 price: 96.86; 2010 price: 105.00;
- bond maturing 2021, price at 2011: 92.35

(*) Source: bank; for lack of up-to-date listings source: Reuters and Bloomberg.

The decrease of €57.6 million in the debt originally arranged at a floating rate was mainly due to:
- use on 8 April 2011 of the credit line of €500 million signed with Cassa Depositi e Prestiti (CDP) on 2 February 2009;
- repayment on 8 April 2011 of the syndicate bank loan (revolving credit facility) originally contracted on 13 December 2004 and subsequently renegotiated on 10 April 2006 for a total amount of €750 million;
- obtaining in August of an EIB loan totalling €325 million;
- a €59.7 million reduction in EIB (European Investment Bank) loans and other financing following repayments made on outstanding loans;
- repayment of a short-term loan for €50 million and the availability of credit facilities used during last year for €23.1 million.

## Long-term loans

The following table reports the book values of long-term debt and the repayment plan as of 31 December 2011, broken down by loan type, including amounts falling due within one year and average interest rate at year-end:

| € million | Maturity | 31.12.2010 | 31.12.2011 | Due within one year | Due beyond one year | 2013 | 2014 | 2015 | 2016 | After | Average interest rate as of 31.12.2011 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Bonds 10y and 20y Bond | 2014-2024 | 1,518.8 | 1,611.0 | 0.0 | 1,611.0 | 0.0 | 640.5 | 0.0 | 0.0 | 970.5 | 4.62% |
| Inflation linked | 2023 | 589.7 | 654.8 | 0.0 | 654.8 | 0.0 | 0.0 | 0.0 | 0.0 | 654.8 | 2.75% |
| Bond Private placement | 2019 | 619.7 | 662.0 | 0.0 | 662.0 | 0.0 | 0.0 | 0.0 | 0.0 | 662.0 | 4.87% |
| Bond 10y (2011) | 2021 | 0.0 | 1,376.1 | 0.0 | 1,376.1 | 0.0 | 0.0 | 0.0 | 0.0 | 1,376.1 | 4.75% |
| **Total fixed rate** | | **2,728.2** | **4,303.9** | **0.0** | **4,303.9** | **0.0** | **640.5** | **0.0** | **0.0** | **3,663.4** | |
| EIB | 2014-2030 | 1,080.1 | 1,345.4 | 59.7 | 1,285.7 | 69.4 | 79.0 | 76.9 | 84.9 | 975.4 | 1.65% |
| Club Deal | 2015 | 648.9 | 649.1 | 0.0 | 649.1 | 0.0 | 0.0 | 649.1 | 0.0 | 0.0 | 1.89% |
| RCF 2006 | 2013 | 750.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| CDP | 2019 | 0.0 | 500.0 | 0.0 | 500.0 | 0.0 | 0.0 | 0.0 | 0.0 | 500.0 | 2.58% |
| **Total floating rate** | | **2,479.0** | **2,494.5** | **59.7** | **2,434.8** | **69.4** | **79.0** | **726.0** | **84.9** | **1,475.4** | |
| **Total** | | **5,207.2** | **6,798.4** | **59.7** | **6,738.7** | **69.4** | **719.5** | **726.0** | **84.9** | **5,138.8** | |

To repay the nominal value of the bonds, amounting to €3,250.0 million, €600.0 million will be repaid on 28 October 2014, €600 million on 3 October 2019, €1,250 million on 15 March 2021 and €800.0 million on 28 October 2024; whilst the inflation-linked bond will be repaid at maturity on 15 September 2023 with the nominal amount adjusted to reflect inflation. For all other financial debt items the table above shows the related repayment plan.

The total amount of Terna borrowing at 31 December 2011, is equal to €6,798.4 million, of which €5,138.8 million is due after more than five years.

The previous table shows the average interest rate for each type of financial liability. Below we also comment on the Group's hedging operations against interest rate fluctuations.

As regards the 2014-2024 bonds, with an average coupon of 4.62%, if fair value hedging operations are taken into account, the average interest rate is equal to 1.95%.

For the inflation-linked bonds – and taking hedges into account – and assuming a 3.22% inflation rate, the average interest rate paid in the year was 3.04%.

The fixed-rate private placement was synthetically transformed to a floating rate security by means of derivative contracts with the same maturity. Consequently, the average interest rate paid in the year was 2.69%.

The average coupon of the 2021 bond is 4.75%; if we consider FVH operations, the average interest rate amounts to 2.70%. With regard to floating rate loans covered by fluctuations in interest rates – and taking into account the effect of derivative financial instruments booked as cash flow hedges – an average rate of 3.81% is reported for EIB financing while for the Club Deal financing totalling €650 million the average rate was 4.75% and for the CDP financing the average rate was 3.98%. The following table reports changes in long-term debt for the year:

| Type of loan<br>€ million | Nominal debt at 31.12.2010 | Carrying amount at 31.12.2010 | Repayment and capitalisation | New issues | Delta fair value 31.12.2010 31.12.2011 | Change in carrying amount | Nominal debt at 31.12.2011 | Carrying amount at 31.12.2011 |
|---|---|---|---|---|---|---|---|---|
| Fixed-rate 10y and 20y bonds (2004) | 1,400.0 | 1,518.8 | 0.0 | 0.0 | 92.2 | 92.2 | 1,400.0 | 1,611.0 |
| Listed IL bond | 529.8 | 589.7 | 17.1 | 0.0 | 48.1 | 65.2 | 546.9 | 654.8 |
| Private placement | 600.0 | 619.7 | 0.0 | 0.0 | 42.2 | 42.2 | 600.0 | 662.0 |
| Fixed rate 10 y bond (2011) | - | - | 0.0 | 1,234.8 | 141.3 | 1,376.1 | 1,250.0 | 1,376.1 |
| **Total bonds** | **2,529.8** | **2,728.2** | **17.1** | **1,234.8** | **323.8** | **1,575.7** | **3,796.9** | **4,303.9** |
| Bank loans | 2,480.1 | 2,479.0 | (809.7) | 825.0 | 0.2 | 15.5 | 2,495.4 | 2,494.5 |
| **Total bank loans** | **2,480.1** | **2,479.0** | **(809.7)** | **825.0** | **0.2** | **15.5** | **2,495.4** | **2,494.5** |
| **Total financial debt** | **5,009.9** | **5,207.2** | **(792.7)** | **2,059.8** | **324.0** | **1,591.2** | **6,292.3** | **6,798.4** |

As compared with 31 December 2010, long-term debt shows an overall increase of €1,591.2 million, due for €1,234.8 million to the issue of a new bond maturing in 2021, net of expenses and issue discount, for €500 million to the disbursement of the CDP loan maturing in 2019, €325 million to the disbursement of the EIB loan maturing in 2030, €17.1 million to the capitalisation of period inflation linked to the IL bond, €323.8 million to the increase in the fair value of bonds, also considering the amortised cost, €750 million to the repayment of the revolving credit facility and for €59.7 million to the repayment in instalments on the EIB loans.
At 31 December 2011, Terna had unused credit lines exceeding €1,203.8 million, of which more than €703.8 million in short-term credit lines and €500.0 million in a medium-term credit line.

### Non-current financial liabilities

The table below reports the amount and changes in non-current financial liabilities with respect to value at the end of 2010:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| CFH derivatives | 111.4 | 47.1 | 64.3 |
| **Total** | **111.4** | **47.1** | **64.3** |

“Non-current financial liabilities” includes the fair value of cash flow hedges.
Fair value was measured by discounting the expected cash flows using the market yield curve at the reporting date. The change in the interest rate curve since 31 December 2010 resulted in a change amounting to €64.3 million.

### Current financial liabilities

Current financial liabilities, due to the net interest expense accrued on financial instruments but not yet settled, have increased by €15.9 million since the end of last year.
The following table details deferred liabilities on the basis of the financial liabilities to which they relate:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| **Deferred liabilities on:** | | | |
| Derivatives | | | |
| *- hedging* | *(43.2)* | *(6.5)* | *(36.7)* |
| Bond | | | |
| *- IL* | *4.4* | *4.3* | *0.1* |
| *- private placement* | *7.2* | *7.2* | *0.0* |
| *- ten-year* | *4.5* | *4.5* | *0.0* |
| *- twenty-year* | *7.0* | *7.0* | *0.0* |
| *- ten-year (2011)* | *47.4* | *0.0* | *47.4* |
| **Total** | **70.5** | **23.0** | **47.5** |
| Loans | 12.8 | 7.7 | 5.1 |
| **Total** | **40.1** | **24.2** | **15.9** |

### Net financial position

Pursuant to CONSOB Communication of 28 July 2006 and in compliance with Recommendation ESMA/2011/81 of 23 March 2011, the net financial position of the Group is as follows:

| € million | 31.12.2011 |
|---|---|
| A. Cash | 349.9 |
| B. Short-term deposits | 765.0 |
| C. Deposit certificates | 150.0 |
| **D. Liquidity (A) + (B) + (C)** | **1,264.9** |
| E. Current portion of long-term debt | 59.7 |
| **F. Current financial debt (E)** | **59.7** |
| **G. Net current financial debt (F) - (D)** | **(1,205.2)** |
| H. Non-current bank payables | 2,434.8 |
| I. Bonds issued | 4,303.9 |
| L. Derivative financial instruments in portfolio | (410.4) |
| **M. Net non-current financial debt (H) + (I) + (L)** | **6,328.3** |
| **N. Net financial debt (G) + (M)** | **5,123.1** |

The debt/equity ratio of the Group stoods at 1.86 in 2011. For more details on the composition of the items in this table, please see Notes 17 and 21, as well as the information presented here in Note 24.
For more information on the contractual provisions of outstanding loans at 31 December 2011, please see the Notes to the financial statements of Terna S.p.A..

## 25. Employee benefits - €119.2 million

The Group provides benefits to its employees during their period of employment (loyalty bonus), at the termination of their employment (termination benefits, additional month's pay and indemnity for lack of notice), and in the period after the termination of employment (electricity discount and the ASEM health plan). The loyalty bonus is awarded to employees and managers of the Group when they reach certain seniority levels (25 and 35 years of service).
The benefits granted at the termination of employment are recognised for all employees (termination indemnities), managers hired or appointed before 28 February 1999 (indemnity for lack of notice), and employees (production workers, office staff and junior managers) hired before 24 July 2001 (additional month's pay indemnity).
Post-employment benefits consist of the following:

- discount on electrical energy consumed for domestic use. This benefit is offered to all employees hired before 30 June 1996 (electricity discount);
- a healthcare plan complementing the national health service, as agreed under the terms of the national contract for industrial managers (the ASEM health plan).

The composition of termination benefits and other employee-related provisions at 31 December 2011, pertaining entirely to the Parent Company, is detailed below along with changes in the year:

| € million | 31.12.2010 | Provision | Interest cost | Utilisations and other changes | 31.12.2011 |
|---|---|---|---|---|---|
| **Benefits payable to employees** | | | | | |
| Loyalty bonus | 4.2 | 0.0 | 0.2 | (0.6) | 3.8 |
| **Total** | **4.2** | **0.0** | **0.2** | **(0.6)** | **3.8** |
| **Benefits payable upon termination of employment** | | | | | |
| Termination benefits | 67.9 | 0.0 | 2.4 | (5.9) | 64.4 |
| Additional months' pay | 6.7 | 0.4 | 0.4 | (1.0) | 6.5 |
| Indemnities for lack of notice and similar | 3.0 | 0.0 | 0.0 | (0.3) | 2.7 |
| **Total** | **77.6** | **0.4** | **2.8** | **(7.2)** | **73.6** |
| **Post-employment benefits** | | | | | |
| Energy discount | 29.3 | 0.8 | 1.3 | (0.5) | 30.9 |
| ASEM | 11.2 | 0.0 | 0.2 | (0.5) | 10.9 |
| **Total** | **40.5** | **0.8** | **1.5** | **(1.0)** | **41.8** |
| **Total** | **122.3** | **1.2** | **4.5** | **(8.8)** | **119.2** |

The item, equal to €119.2 million at 31 December 2011 (€122.3 million at 31 December 2010), decreased by €3.1 million on the previous year, due to the utilisations of the year (€8.8 million), partially offset by the allocations and the recognition of the discounting charge for the year (€5.7 million in total).

Below is the reconciliation of the current value of the obligation for employee benefits with respect to the assets and liabilities recognised on the financial statements:

| € million | Termination benefits | Indemnities for lack notice and similar | Additional months' pay | Loyalty bonus | ASEM | Energy discount | Total |
|---|---|---|---|---|---|---|---|
| Current value of obligation | 58.3 | 0.9 | 8.3 | 3.8 | 5.7 | 28.9 | 105.9 |
| Net actuarial gains/losses not recognised | 6.1 | 1.8 | (1.8) | 0.0 | 5.2 | 2.0 | 13.3 |
| **Net liabilities recognised** | **64.4** | **2.7** | **6.5** | **3.8** | **10.9** | **30.9** | **119.2** |

Costs for liabilities in respect of employee benefits recognised in the income statement break down as follows:

| € million | Termination benefits | Indemnities for lack notice and similar | Additional months' pay | Loyalty bonus | ASEM | Energy discount | Total |
|---|---|---|---|---|---|---|---|
| Service cost | 0.0 | 0.1 | 0.3 | 0.2 | 0.2 | 0.8 | 1.6 |
| Financial expense | 2.4 | 0.0 | 0.4 | 0.2 | 0.2 | 1.3 | 4.5 |
| Amortisation of actuarial gains/losses | (0.1) | (0.4) | 0.1 | (0.2) | (0.5) | 0.0 | (1.1) |
| **Total** | **2.3** | **(0.3)** | **0.8** | **0.2** | **(0.1)** | **2.1** | **5.0** |

The main assumptions made in the actuarial estimate of employee benefit obligations are as follows:

| Percentage figures | 2011 | 2010 |
|---|---|---|
| Discount rate | 4.1% | 4.1% |
| Salary increase rate | 2.0% - 4.0% | 2.0% - 4.0% |
| Rate of increase in healthcare costs | 3.0% | 3.0% |

## 26. Provisions for risks and charges - €193.8 million

The breakdown of the Provisions for risks and charges at 31 December 2011 is detailed below together with the changes in the period:

| € million | Provision for disputes and litigation | Provisions for other risks and charges | Provision for early retirement incentives | Total |
|---|---|---|---|---|
| **Balance at 31.12.2010** | **16.7** | **141.9** | **13.0** | **171.6** |
| Provision | 0.5 | 73.1 | 7.9 | 81.5 |
| Utilisations and other changes | (0.4) | (58.1) | (0.8) | (59.3) |
| **Balance at 31.12.2011** | **16.8** | **156.9** | **20.1** | **193.8** |

### Provision for disputes and litigation - €16.8 million

The provision is accrued to cover the liabilities at year end that may arise from lawsuits and out-of-court disputes relating to Group activities. The amount accrued takes into account the opinions both of internal and external legal counsel. The caption is substantially in line with the previous year.
Litigation for which no potential charge can reasonably be calculated are described under "Off-balance sheet commitments and risks".

### Provision for other risks and charges - €156.9 million

The provision reported a net increase of €15.0 million with respect to the previous year, ascribable to accruals of €73.1 million and utilisations of a negative €58.1 million in the course of the year. More specifically:

- partial release of the fund accrued by the Parent Company in 2009 for probable charges relating to the sale of the majority share package of Terna Participações (a negative €33.8 million inclusive of the exchange rate effect), for the part of the contractual bonds that matured during the financial year;

- exchange rate adjustment (a negative €1.2 million) of the provision for probable expenses relating to tax obligations deriving from the sale of Terna Participações by the Parent Company;
- accrual by SunTergrid S.p.A. for probable expenses connected with the sale of Nuova Rete Solare S.r.l. and Rete Rinnovabile (€30.7 million and €11.9 million respectively);
- a net accrual of €2.2 million relating to "Projects for urban and environmental renewal" of the Parent Company, the aim of which is to offset the environmental impact of the construction of long-distance power lines;
- net accrual by the Parent Company and Terna Rete Italia (€1.1 million and €2.5 million respectively) for expenses to be paid to distributors for power failures of transformation plants connected to the NTG (*ex* Resolution 341/07) and the sharing of indemnities due to final users (€1.1 million) by the Parent Company.

**Provision for early retirement incentives - €20.1 million**

This provision reflects the estimated extraordinary charges related to the voluntary early termination of the working relationship of employees of the Parent Company who are eligible for retirement. The item reflects an increase of €7.1 million for net accruals made during the financial year.

## 27. Deferred tax liabilities - €251.8 million

The changes in this provision are analysed below:

| € million | 31.12.2010 | Impact recognised in profit or loss | | Impact recognised in equity (*) | 31.12.2011 |
|---|---|---|---|---|---|
| | | Provisions | Utilisations | | |
| **Deferred tax liabilities** | | | | | |
| Property, plant and equipment | 382.1 | 101.4 | (56.6) | | 426.9 |
| Employee benefits and financial instruments | 3.5 | 0.8 | | | 4.3 |
| **Total deferred tax liabilities** | **385.6** | **102.20** | **(56.6)** | **0.0** | **431.2** |
| **Deferred tax assets** | | | | | |
| Provisions for risks and charges | 16.4 | 26.1 | (3.5) | | 39.0 |
| Allowance for impairment accounts | 3.1 | 0.5 | | | 3.6 |
| Employee benefits | 22.9 | 14.6 | (10.5) | | 27.0 |
| FVH - CHF derivatives | 12.9 | | | 29.4 | 42.3 |
| Release of goodwill | 25.2 | 46.1 | (3.8) | | 67.5 |
| **Total deferred tax assets** | **80.5** | **87.3** | **(17.8)** | **29.4** | **179.4** |
| **Net deferred tax liabilities** | **305.1** | **14.9** | **(38.8)** | **(29.4)** | **251.8** |

(*) In the "Other comprehensive income".

This balance, equal to €251.8 million, reflects the net movements in the Group's deferred tax assets and liabilities.
Deferred tax liabilities totalled €431.2 million, up €45.6 million, essentially due to:

- allocation of deferred taxes as a consequence of the adjustment of the IRES rate to the higher rate established by the so called "corrective manoeuvre-*bis*" approved by Italian Law Decree no. 138 of 13 August 2011, enacted by Parliamentary Law on 14 September (amending regulations of the Robin Hood Tax) for a total of €96.7 million, of which €76.3 million relating to Terna S.p.A. and €20.4 million relating to the Parent Company Terna S.p.A. (including €14.8 million to adjust deferred taxes calculated on the excess cost paid for the purchase of the subsidiary Terna Rete Italia and allocated to the transmission plants and intangible assets);
- adjustment of initial deferred taxes to the higher IRAP rate of concession holding companies established by Italian Law Decree no. 98 of 6 July 2011, Art. 23, paragraph 5 for €5.5 million in total, inclusive of the adjustment of deferred taxes calculated on the excess cost paid for the acquisition of Terna Rete Italia (€2.6 million);
- utilisation of prior period allocations covering the accelerated depreciation recorded by the Parent Company Terna and the subsidiary Terna Rete Italia in excess of the tax-allowable amounts (€39.1 million and €3.3 million, respectively), including the amount released in relation to the depreciation charge for the period associated with merger differences allocated to property, plant and equipment at the time of the mergers carried out in prior years (€3.3 million);
- release of the charge for year (€9.1 million) of the provision for deferred IRAP liabilities governed by Law no. 244 dated 24 December 2007 (the 2008 Finance Law), recorded in prior years in relation to economic/technical rates;

- release of the amount for the year of the deferred taxes calculated on the excess cost paid for the acquisition of Terna Rete Italia following its allocation to the transmission plant and other intangible assets (totalling €5.0 million, after considering the effect of the plant transfers to the Parent Company).

Deferred tax assets (€179.4 million) include the change to the opening balance in order to consider the change in the accounting principle relative to the booking of the release in financial year 2009 of goodwill deriving from the merger of RTL into the Company in financial year 2009, in compliance with Art. 15 of Italian Legislative Decree no. 185/2008, for an amount of €25.2 million. An increase is also seen of €98.2 million, mainly referring to the following changes:
- allocation of deferred tax assets as a consequence of the above-mentioned adjustment of the IRES rate to that established by the "corrective manoeuvre-*bis*" for €24.1 million;
- accrual of €39.8 million in relation to the tax recognition of the goodwill recorded following the acquisition of the subsidiary Terna Rete Italia S.r.l. established by Italian Law Decree no. 98 of 6 July 2011;
- accrual of €24.4 million, attributable to the tax effect, which has no impact on the income statement, in respect of changes in cash flow hedge instruments of the Parent Company;
- net use, amounting to €3.8 million, of the share for the year of deferred tax assets allocated for the release of goodwill recorded following the merger of RTL;
- net use of €2.6 million relative to movements in provisions for employee benefits of the Parent Company;
- net accrual for €17.1 million in relation to uses during the year of the provisions for risks and charges. Specifically, they reflect the tax effects of the accruals for risks of the Parent Company (€4.3 million), of Terna Rete Italia (€1.1 million) and SunTergrid (€11.7 million).

## 28. Other non-current liabilities - €137.1 million

This item, amounting to €137.1 million at 31 December 2011 encompasses the deferred positions of set-up grants of the Parent Company (€129.1 million) and of Terna Rete Italia (€8.0 million).
The decrease of €4.7 million in the item with respect to the previous year regards:
- the release, in the amount of €2.5 million, of the portions of grants in connection with depreciation of the plants to which they refer;
- the release of the share of the year for the remuneration of costs incurred during the financial year for the NTG Security Plan (€2.3 million).

## 29. Current liabilities

Current liabilities at 31 December 2011 break down as follows:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| Short-term loans (*) | 0.0 | 73.1 | (73.1) |
| Current portion of long-term loans (*) | 59.7 | 59.7 | 0.0 |
| Trade payables | 2,029.8 | 1,542.20 | 487.6 |
| Tax liabilities | 116.5 | 69.6 | 46.9 |
| Current financial liabilities (*) | 40.1 | 24.2 | 15.9 |
| Other current liabilities | 137.6 | 135.7 | 1.9 |
| **Total** | **2,383.7** | **1,904.5** | **479.2** |

(*) See the comments in Note 24. Loans and financial liabilities.

### Trade payables - €2,029.8 million

Trade payables at 31 December 2011 break down as follows:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| Suppliers: | | | |
| - Energy-related payables | 1,334.8 | 1,068.5 | 266.3 |
| - Non energy-related payables | 684.8 | 466.7 | 218.1 |
| Payables due to associates | 7.1 | 5.0 | 2.1 |
| Payables for contract work in progress | 3.1 | 2.0 | 1.1 |
| **Total trade payables** | **2,029.8** | **1,542.2** | **487.6** |

## Suppliers

### Energy-related payables

This item reports the effects on the balance sheet of payables for "pass-through" costs not ascribable to the Parent Company, and refers mainly to purchase of energy relative to dispatching activities and the transport fee due to the owners of other sections of the NTG.

The increase of €266.3 million compared with the previous year is essentially attributed to:

- increased payables (€263.1 million) relative to "pass-through items" which are mainly ascribable to the joint effect of:
  - the increase in payables for the acquisition of electrical energy outside of the Power Exchange (€234.1 million) which is essentially due to the greater balance of net payables for capacity payment (€110.8 million), the increase in debt items awaiting definition on the part of the AEEG - in particular the availability of productive capacity (PC), totalling €34.9 million - as well as the rise in payables for the essential units for the safety of the electrical system (EUSES), totalling €84.7 million;
  - increased debt for the purchase of electricity within the Power Exchange (€29.0 million), mainly deriving from the net effect of the greater payables generated by the increased quantities and prices of the measurement of the imbalance (€97.2 million) and from the recognition of payables relating to the market coupling mechanism for the management of congestion on the inter-connection with Slovenia (€7.7 million); partly offset, as already described in the "Trade receivables" sections, by the reduction in volumes of resources attained on the energy market (€19.6 million), by the reduction of the debt items relative to the dispatching of electricity produced by non-programmable renewable sources envisaged by the Resolution ARG/elt 5/10 (€14.3 million) and the lower payables deriving from the virtual interconnection activities (€44.3 million);
- greater payables not ascribable to the Parent Company (€3.2 million) to the Compensation Fund for the Electrical Sector, deriving from the increased charges payable to the Exceptional Events Fund for power failures which occurred during financial year 2011 and as adjustment for the previous year (€1.6 million), in accordance with Resolution 341/07 and its subsequent amendments as well as the reimbursement of the grid transmission fees balance for previous years (€1.6 million) which was partially offset by the receivable booked by the Parent Company for the same amount, as described in the paragraph relative to "Receivables for grid transmission fees" under trade receivables.

### Non energy-related payables

Amounts due to suppliers refer to invoices both already received and yet to be received for tenders, services and the purchase of materials and equipment.
The increase on previous year (€218.1 million) is essentially due to purchases and services in respect of increased capital expenditure in the last quarter of 2011 compared with the same period of 2010 and also as a result of payments made during the first few days of the next financial year.

### Payables due to associates

This item amounts to €7.1 million and includes payables to the associate CESI for services provided to the Parent Company in the construction and management of laboratories and plants for tests, inspections, studies and experimental research in the general field of electricity technology and scientific and technical progress. The increase (€2.1 million) compared with 31 December 2010 is the result of an increase in services delivered in the final part of the year.

Group commitments with suppliers amounted to about €2,294.5 million and refer to purchase commitments relating to normal "operating activities" for the period 2012-2017.

### Payables for contract work in progress

Payables for contract work in progress concerning advances from customers amounted to €3.1 million at 31 December 2011 and was substantially in line with the balance at 31 December 2010 (+€1.1 million). It is composed as follows:

| € million | Payments on account | Contract value | Balance at 31.12.2011 | Payments on account | Contract value | Balance at 31.12.2010 |
|---|---|---|---|---|---|---|
| Other | (15.5) | 12.4 | (3.1) | (23.2) | 21.2 | (2.0) |

### Tax liabilities - €116.5 million

The caption refers to the Group's tax liabilities for the financial year and refers to:

- the Parent Company Terna in the amount of €88.2 million;
- the subsidiary SunTergrid in the amount of €22.0 million;
- the subsidiary Terna Rete Italia in the amount of €6.3 million.

It reflects an increase of €46.9 million on last year, mainly due to the subsidiary SunTergrid (€21.8 million) for the higher tax burden arising mostly from extraordinary transactions carried out during the year and the Parent Company (€19.1 million), substantially as a result the adjustment to the new IRES tax regulations introduced by Italian Law Decree no. 138 of 13 August 2011 (Robin Hood Tax).

### Other current liabilities - €137.6 million

Other current liabilities break down as follows:

| € million | 31.12.2011 | Due within one year | Due beyond one year | 31.12.2010 | Change |
|---|---|---|---|---|---|
| Payments on account | 38.8 | 21.9 | 16.9 | 30.7 | 8.1 |
| Other tax liabilities | 20.5 | 20.5 | | 7.5 | 13.0 |
| Payables to social security institutions | 22.3 | 22.3 | | 22.4 | (0.1) |
| Payables to employees | 31.2 | 31.2 | | 38.9 | (7.7) |
| Other payables to third parties | 24.8 | 4.9 | 19.9 | 36.2 | (11.4) |
| **Total** | **137.6** | **100.8** | **36.8** | **135.7** | **1.9** |

### Payments on account

The item (€38.8 million) reports set-up grants related to plants received by the Group (€37.1 million for the Parent Company and €1.7 million for the subsidiary Terna Rete Italia) for assets under construction at 31 December 2011.

Compared to 2010 (€30.7 million), there is an increase of €8.1 million, mainly due to the net effect of new payments on account received from third parties for €20.2 million and a decrease of €12.1 million in the grants reducing the book values of assets entered into operation during the financial year; in particular there are payments on account received in accordance with the mandate contract for the design of interconnection networks "Interconnector" with abroad (€18.6 million, in accordance with Resolution ARG/elt 179/09 and its subsequent amendments).

### Other tax liabilities

Other tax liabilities, amounting to €20.5 million, show an increase of €13.0 million with respect to the previous financial year, mainly as a result of the recognition of the VAT payable for the year of the Parent Company.

### Payables to social security institutions

Payables to social security institutions, mainly relating to payables due to INPS by the Parent Company, amount to €22.3 million (€22.4 million at 31 December 2010), basically in line with the previous financial year. The item also includes the payable (€4.8 million) due to Fondo Previdenza Elettrici – F.P.E. (security fund for electricians).

### Payables to employees

Amounts payable to employees, which came to €31.2 million (€38.9 million at 31 December 2010), pertain to the Parent Company and mainly regard:

- accruals made for staff incentives to be paid the following year (€16.5 million);
- payments due to employees for unused holiday time and abolished public holidays (€8.8 million);
- termination indemnities due to employees whose employment was terminated before 31 December 2011 (€2.0 million).

### Other payables to third parties

Other payables, equal to € 24.8 million (€36.2 million at 31 December 2010), mainly regard security deposits (€19.9 million) received from electricity market operators securing their obligations in respect of dispatching contracts. This item reports a decrease of €11.4 million which is essentially attributable to above-described caution money (a negative €12.7 million).

# E. Commitments and risks

## Risk management

### Market and financial risks

During the financial year, in going about its business, the Terna Group is exposed to various different financial risks: market risk (namely exchange rate risk, interest rate risk and inflation risk), liquidity risk and credit risk.
This section provides information regarding the Terna Group's exposure to all the above risks, along with a presentation of the objectives, policies and processes for managing those risks and the methods used to measure them, with further quantitative disclosures concerning the 2011 financial statements.
The Group's risk management policies seek to identify and analyse the risks the Company is exposed to, establishing appropriate limits and controls and monitoring risks and compliance with such limits. These policies and the related systems are reviewed on a regular basis in order to take account of any changes in market conditions or in the operations of the companies.
The exposure of the Terna Group to the aforementioned risks is substantially represented by the exposure of the Parent Company. As a part of the financial risk management policies approved by the Board of Directors, Terna has established the responsibilities and operating procedures for financial risk management, specifically as concerns the instruments to be used and the precise operating limits in managing them.

| | 2011 | | | | | 2010 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| € million | Receivables | Receivables at fair value | Hedging derivatives | Assets available for sale | Total | Receivables | Receivables at fair value | Hedging derivatives | Assets available for sale | Total |
| **Assets** | | | | | | | | | | |
| Derivative financial instruments | - | - | 521.8 | - | 521.8 | - | - | 200.3 | - | 200.3 |
| Short-term cash, deposits, deposit certificates | 1,264.9 | - | - | - | 1,264.9 | 150.1 | - | - | - | 150.1 |
| **Total** | **1,264.9** | **-** | **521.8** | **-** | **1,786.7** | **150.1** | **-** | **200.3** | **-** | **350.4** |

| | 2011 | | | | | 2010 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| € million | Payables | Loans at fair value | Hedging derivatives | Other liabilities at amortised cost | Total | Payables | Loans at fair value | Hedging derivatives | Other liabilities at amortised cost | Total |
| **Liabilities** | | | | | | | | | | |
| Long-term debt | 2,494.5 | 4,303.9 | - | - | 6,798.4 | 2,552.1 | 2,728.2 | - | - | 5,280.3 |
| Derivative financial instruments | - | - | 111.4 | - | 111.4 | - | - | 47.1 | - | 47.1 |
| **Total** | **2,494.5** | **4,303.9** | **111.4** | **-** | **6,909.8** | **2,552.1** | **2,728.2** | **47.1** | **-** | **5,327.4** |

### Market risks

Market risk is the risk that the fair value or future cash flows of a financial instrument may fluctuate as a result of changes in financial market conditions. Market risks includes three types of risks: exchange rate risk, interest rate risk and inflation risk. Risk management must be performed with the objective of maximising financial income and minimising the related risks by selecting counterparties and instruments compatible with the corporate risk management policy. Speculative activity is not envisaged in the corporate mission.
Terna Group seeks to adopt a dynamic approach to financial risk management. This approach is characterised by risk aversion, aiming at minimising risk through continuous monitoring of financial markets in order to plan hedging transactions in favourable market conditions. The dynamic approach makes it possible to take action to improve existing hedges where changes in market conditions or in the hedged item make the latter unsuitable or excessively expensive. The concept of hedging transaction is not restricted to those hedges that qualify for hedge accounting, but rather encompasses the objective of total or partial hedging of the income statement or statement of financial position item from interest rate risk.
All derivative contracts have a notional amount and maturity date less than or equal to that of the underlying financial liability, so that any change in the fair value and/or estimated cash flows of the contracts is offset by a corresponding change in the fair value and/or estimated cash flows of the underlying position. The fair value of financial derivatives reflects the estimated amount that Terna S.p.A. would pay or receive in order to extinguish contracts at the closing date.

The fair value of instruments is determined in accordance with the fair value hierarchy envisaged under IFRS 7 (Level 2) by means of appropriate valuation techniques for each category of financial instrument, using market data as at the closing date (such as interest rates, exchange rates, volatility) and discounting projected cash flows on the basis of the market yield curve and inflation at the reporting date.
The financial assets and liabilities in respect of derivative instruments in place during the year can be classified as:
- cash flow hedge derivatives, essentially related to hedging the risk of changes in the cash flows associated with long-term floating-rate loans;
- fair value hedge derivatives, essentially related to hedging the exposure to changes in the fair value of a financial asset or liability associated with fluctuations in interest rates (fixed-rate bonds).

Below are the notional amounts and fair values of the derivative financial instruments subscribed by the Terna Group:

| | 2011 | | 2010 | | Change | |
|---|---|---|---|---|---|---|
| € million | Notional amount | Fair value | Notional amount | Fair value | Notional amount | Fair value |
| FVH derivatives | 3,750.0 | 521.8 | 2,500.0 | 200.3 | 1,250.0 | 321.5 |
| CFH derivatives | 3,418.4 | (111.4) | 1,830.1 | (47.1) | 1,588.3 | (64.3) |

## Interest rate risk

Interest rate risk is represented by the uncertainty associated with interest rate fluctuations. This is the risk that a change in market rates may produce effects on the fair value or future cash flows of financial instruments.
In conducting its operations, Terna is exposed to the risk of fluctuations in interest rates. Its main source of interest rate risk is associated with items of net financial debt and the related hedging positions in derivative instruments that generate financial expense. Terna's borrowing strategy focuses on long-term loans whose term reflects the useful life of company assets. It pursues an interest rate risk hedging policy that aims to reconcile this approach with the regulatory framework, which every four years establishes the cost of debt as part of the formula to set the return on the Regulatory Asset Base (RAB).
Accordingly, the hedging instruments used, at various maturity dates, include both derivatives that transform fixed rates into floating rates and derivatives that transform floating rates into fixed rates.
In order to reduce the amount of financial debt exposed to the risk of fluctuations in interest rates and to optimise the temporal correlation between average cost of debt and regulatory rate used in the WACC formula, various types of plain vanilla derivatives are used, such as interest rate swaps.
Interest rate swaps are used in order to reduce the volume of debt exposed to fluctuations in interest rates and to reduce the volatility of borrowing costs. With an interest rate swap, Terna agrees with a counterparty to exchange, at specific intervals, the floating-rate cash flows on a specified notional amount against the fixed-rate (agreed between the parties) cash flows, or vice versa.

The following table shows the financial instruments entered into by Terna, classified according to the type of interest rate (fixed or floating):

| | Carrying amount | | |
|---|---|---|---|
| € million | 31.12.2011 | 31.12.2010 | Change |
| Fixed-rate financial instruments: | | | |
| - assets | 0.0 | 0.0 | 0.0 |
| - liabilitie | 4,415.3 | 2,775.3 | 1,640.0 |
| Floating-rate financial instruments: | | | |
| - assets | 1,786.7 | 350.4 | 1,436.3 |
| - liabilities | 2,494.5 | 2,552.1 | (57.6) |
| **Total** | **5,123.1** | **4,977.0** | **146.1** |

## Sensitivity to interest-rate risk

As regards the management of interest rate risk, Terna has, on the one hand, entered into fixed-to-floating interest rate swaps (FVH) to hedge the fair value of the fixed-rate risk bonds and, on the other, floating-to-fixed interest rate swaps (CFH) to hedge the expected cash flows in respect of all other floating-rate debt.
Since the hedging relationship between the derivative and the hedged item is formally documented and the effectiveness of the hedge, as verified initially and periodically over its life, is high (between 80% and 125%), the Company has elected to use hedge accounting to ensure the perfect temporal matching of the hedge and the hedged item. The aim of hedge

accounting is to recognise the effects of the hedges and the hedged items in the income statement at the same time. Accordingly, for FVH derivatives, any changes in the fair value of the hedged item attributable to the risk being hedged must be booked in the income statement, thereby offsetting the changes in the fair value of the derivative booked in the income statement. For CFH derivatives, the changes in the fair value of the derivative must be booked in "Other comprehensive income" equity (recognising any ineffective portion of the hedge directly in the income statement) and then reversed through the income statement in the same period in which the cash flows of the hedged instrument materialise. The characteristics of the CFH derivatives mirror those of the underlying hedged asset so the related cash flows will materialise at the same maturities as the interest on the debt, with no impact of the changes in fair value on the income statement.

The following table reports the amounts booked in the income statement and "Other comprehensive income" for positions that are sensitive to changes in interest rates, the theoretical value of the positions following a positive or negative shift in the yield curve and the differential impact booked in the income statement and shareholders' equity of such changes. A hypothetical 10% variation in interest rates with respect to market interest rates at the reporting date was assumed:

| | Profit or loss | | | Equity | | |
|---|---|---|---|---|---|---|
| € million | Current rates +10% | Current rates | Current rates -10% | Current rates +10% | Current rates | Current rates -10% |
| **31 December 2011** | | | | | | |
| Positions sensitive to interest rate variations (FVH, bonds, CFH) | 1.0 | (0.2) | (1.4) | (100.0) | (111.4) | (122.9) |
| *Hypothetical change* | 1.2 | | 1.2 | 11.4 | | (11.5) |
| **31 December 2010** | | | | | | |
| Positions sensitive to interest rate variations (FVH, bonds, CFH) | 2.9 | 2.2 | 1.7 | (44.5) | (47.1) | (49.9) |
| *Hypothetical change* | 0.7 | - | (0.5) | 2.6 | - | (2.8) |

### Inflation risk

As regards inflation rate risk, the rates established by Regulators to remunerate Terna S.p.A.'s activities are determined so as to allow coverage of the sector's recognised costs. Such cost components are updated on an annual basis to consider the accrued impact of inflation. In 2007, the Company used an inflation-linked bond issue to obtain an effective hedge of profit for the year; any decrease in expected revenue due to a decrease in the inflation rate would be offset by lower financial expense.

### Exchange rate risk

Generally Terna hedges exchange rate risk through the forward sale or purchase of currencies (forward contracts) or the use of options. Currency options give Terna the right or the obligation to buy or sell predetermined amounts of a currency at a specific exchange rate at the end of a specific period of time. Normally, both forward contracts and options have maturities of no more than 12 months.

Such contracts have a notional amount and maturity date less than or equal to that of the underlying financial liability, or the expected cash flows, so that any change in the fair value and/or estimated cash flows deriving from an appreciation or depreciation of the euro against other currencies is fully offset by a corresponding change in the fair value and/or estimated cash flows of the underlying position.

At 31 December 2011 (as at 31 December 2010), no financial instruments exposed to exchange rate risk were present.

### Liquidity risk

The liquidity risk is the risk Terna might encounter difficulty in discharging its obligations in respect of its financial liabilities and operational cycle. Liquidity risk management seeks to ensure adequate coverage of financial needs by obtaining adequate lines of credit and appropriate management of any surplus liquidity. As of 31 December 2011 Terna had €500 million in medium-term credit lines and €703.8 million in short-term credit lines. The table below shows the repayment plan at 31 December 2011 of the nominal long-term debt:

| € million | Maturity | Notional amount of debt 31.12.2011 | Maturity within 12 months | Maturity beyond 12 months | 2013 | 2014 | 2015 | 2016 | After |
|---|---|---|---|---|---|---|---|---|---|
| Bonds 10y and 20y | 2014-2024 | 1,400.0 | 0.0 | 1,400.0 | 0.0 | 600.0 | 0.0 | 0.0 | 800.0 |
| Bond Inflation linked | 2023 | 546.9 | 0.0 | 546.9 | 0.0 | 0.0 | 0.0 | 0.0 | 546.9 |
| Bond Private placement | 2019 | 600.0 | 0.0 | 600.0 | 0.0 | 0.0 | 0.0 | 0.0 | 600.0 |
| Bond 10y | 2021 | 1,250.0 | 0.0 | 1,250.0 | 0.0 | 0.0 | 0.0 | 0.0 | 1,250.0 |
| **Total fixed rate** | | **3,796.9** | **0.0** | **3,796.9** | **0.0** | **600.0** | **0.0** | **0.0** | **3,196.9** |
| EIB | 2014-2030 | 1,345.4 | 59.7 | 1,285.7 | 69.4 | 79.0 | 76.9 | 84.9 | 975.4 |
| Club Deal | 2015 | 650.0 | 0.0 | 650.0 | 0.0 | 0.0 | 650.0 | 0.0 | 0.0 |
| CDP | 2019 | 500.0 | 0.0 | 500.0 | 0.0 | 0.0 | 0.0 | 0.0 | 500.0 |
| **Total floating rate** | | **2,495.4** | **59.7** | **2,435.7** | **69.4** | **79.0** | **726.9** | **84.9** | **1,475.4** |
| **Total** | | **6,292.2** | **59.7** | **6,232.5** | **69.4** | **679.0** | **726.9** | **84.9** | **4,672.3** |

## Credit risk

Credit risk is the risk a customer or one of the counterparties to a transaction in financial instruments could cause a financial loss by failing to discharge an obligation. It is mainly generated by trade receivables and the financial investments of the Company.
The credit risk originated by open positions on transactions in financial derivatives is considered to be marginal since the counterparties, in compliance with financial risk management policies, are leading international credit institutions with high ratings and such transactions are diversified in compliance with specific concentration limits.
Terna provides its services to counterparties considered solvent by the market, who therefore have a high credit standing, and does not have highly concentrated credit risk.
Credit risk management is guided by the provisions of AEEG Resolution no. 111/06, which, in Art. 49, introduced instruments for the limitation of risks related to the insolvency of dispatching customers, both on a preventive basis and in the event of actual insolvency. In particular, the Resolution establishes three instruments to safeguard the electricity market: a guarantee system (bank guarantees provided by individual dispatching customers, based on their sales revenue), the option of terminating dispatching contracts (in the event of insolvency or failure to replace enforced guarantees) and, finally, the possibility of recovering uncollected receivables, after having taken all other possible collection actions, through a specific fee defined by the Authority.

The following table summarises the exposure to such risk as at the reporting date:

| € million | Carrying amount 31.12.2011 | Carrying amount 31.12.2010 | Change |
|---|---|---|---|
| FVH derivatives | 521.8 | 200.3 | 321.5 |
| Deposit certificates | 150.0 | - | 150.0 |
| Cash and cash equivalents | 1,114.9 | 150.1 | 964.8 |
| Trade receivables (*) | 1,684.0 | 1,495.6 | 188.4 |
| **Total** | **3,470.7** | **1,846.0** | **1,624.7** |

(*) The balance of trade receivables of the Parent Company Terna S.p.A. is stated, as this is most representative of exposure to the credit risk.

The total value of the exposure to credit rate risk at 31 December 2011 is represented by the carrying amount of financial assets (current and non current), trade receivables and cash and cash equivalents.

The following tables provide qualitative information on customer receivables that are not past due and have no impairment:

GEOGRAPHICAL DISTRIBUTION

| € million | Carrying amount 2011 | 2010 |
|---|---|---|
| Italy | 1,654.2 | 1,482.6 |
| Euro-area countries | 27.2 | 8.9 |
| Other countries | 2.6 | 4.1 |
| **Total** | **1,684.0** | **1,495.6** |

CUSTOMER TYPOLOGY

| € million | Carrying amount 2011 | 2010 |
|---|---|---|
| Distributors (*) | 243.4 | 243.9 |
| Electricity Equalisation Fund (**) | 131.3 | 71.7 |
| Input dispatching contractors | 229.4 | 310.2 |
| Withdrawal dispatching contractors (non distributors) | 1,000.2 | 765.3 |
| Parties which have undersigned virtual import contracts and virtual import services (interconnectors and shippers) | 12.5 | 35.2 |
| Receivables from unregulated activities | 67.2 | 69.3 |
| **Total** | **1,684.0** | **1,495.6** |

(*) Includes receivable accrued in respect of Terna Rete Italia grid transmission fees.
(**) Of which € 116.2 million from volume effect on grid transmission fees.

The following table breaks down customer receivables by age, reporting any potential impairment:

| € million | 2011 Allowance for impairment accounts | 2011 Gross | 2010 Allowance for impairment accounts | 2010 Gross |
|---|---|---|---|---|
| Not yet past due | - | 1,560.0 | - | 1,430.9 |
| 0-30 days past due | - | 50.0 | - | 38.5 |
| 31-120 days past due | - | 37.9 | - | 3.5 |
| More than 120 days past due | (23.6) | 59.7 | (23.5) | 46.2 |
| **Total** | **(23.6)** | **1,707.6** | **(23.5)** | **1,519.1** |

Changes in the provision for bad debts in the course of the year were as follows:

| € million | 2011 | 2010 |
|---|---|---|
| Balance at 1 January | (23.5) | (27.0) |
| Reversal of provision | - | 3.5 |
| Impairment for the year | (0.1) | - |
| **Balance at 31 December** | **(23.6)** | **(23.5)** |

The value of guarantees received from eligible electricity market customers is illustrated below:

| € million | 2011 | 2010 |
|---|---|---|
| Input dispatching activity | 254.6 | 220.5 |
| Withdrawal dispatching activity | 763.0 | 831.3 |
| Grid transmission fees - distributors | 174.8 | 173.7 |
| Virtual importing | 280.2 | 338.0 |
| **Balance at 31 December** | **1,472.6** | **1,563.5** |

### Default risk and debt covenants

This risk is associated with the possibility that the loan contracts or bond rules to which the Company is party may contain provisions authorising counterparties to call in such loans immediately upon the occurrence of certain events, thereby generating liquidity risk. For more information on the contractual provisions of outstanding loans at 31 December 2011, please see the section “Loans and financial liabilities” in the Notes to the separate financial statements of Terna S.p.A..

## Legal disputes

The main unrecognised commitments and risks of the Parent Company Terna and the subsidiary Terna Rete Italia at 31 December 2011 are discussed below. The other subsidiaries had no unrecognised commitments and contingencies at that date.

### Environmental and urban planning litigation

Environmental litigation originates from the installation and operation of electrical plants and primarily involves damages which could be derived from exposure to electrical and magnetic fields that are generated by long-distance power lines. The Parent Company and the subsidiary Terna Rete Italia are involved in various civil and administrative suits requesting the transfer or change in operations of allegedly-harmful power lines, even though they were installed in full compliance with applicable legislation (Italian Law no. 36 of 22 February 2001 and Prime Minister’s Decree 8 July 2003). Only a very small number of cases include claims for damages for harm to health caused by electromagnetic fields.

In sporadic cases, adverse judgements have been issued against the Parent Company. These have been appealed and the appeals are still pending; adverse decisions are considered unlikely.

In addition, a number of cases relating to urban planning and environmental issues are pending in respect of the construction and operation of certain transmission lines. The possible effects of any unfavourable outcome to these cases are unpredictable and, accordingly, have not been considered when determining the “Provision for disputes and other risks”.

In a limited number of cases, the possibility of an adverse outcome cannot be entirely ruled out. The possible consequences could, in addition to the award of damages, include, *inter alia*, the costs of modifying lines and the temporary suspension of their use. In any case, any unfavourable outcome would not jeopardise line operations.

The above litigation has been examined, also considering the opinion of independent legal counsel, and any negative outcome is considered remote.

### Litigation concerning concession activities

Given that it has been the licensee for transmission and dispatching activities since 1 November 2005, the Parent Company has been involved in a number of cases appealing AEEG, MAP and/or Terna measures relating to activities operated under the license. Only in those cases in which the plaintiffs not only claim defects in the measures, but also allege that Terna violated the rules established by such authorities has the Company appeared in court. Within the scope of this litigation, although a number of cases have seen the AEEG Resolutions struck down in the first and/or second-level court, together with the consequent measures adopted by Terna, it is felt that there is little risk of adverse outcomes for Terna, since the matters generally regard pass-through items. This position is supported by the information provided by the external legal counsel representing the Company in the cases involved. As the licensee for transmission and dispatching activities, the measures taken by the Parent Company Terna when applying the Resolutions adopted by the Authority are sometimes the subject of challenges. In appropriate circumstances, the economic costs of such challenges may be borne by the Authority.

# F. Business combinations

There were no business combinations during 2011.

# G. Related-party transactions

The Terna Group's transactions with related parties during the year, taking account of the *de facto* control exercised by Cassa Depositi e Prestiti S.p.A. ascertained in 2007, regarded the associate company CESI S.p.A., the employee pension funds (Fondenel and Fopen), Cassa Depositi e Prestiti, as well as companies belonging to:

- the GSE Group;
- the Enel Group;
- the Eni Group;
- the Ferrovie dello Stato Group;

and those with ANAS S.p.A..

Related party transactions in 2011 are mainly services that are part of core business and regulated by market conditions. More specifically, with respect to the previous financial year, please note the use on 8 April 2011 of the credit line of €500 million granted by Cassa Depositi e Prestiti (CDP) on 2 February 2009.
Below is an explanation of the nature of the transactions implemented by the Terna Group with related parties and the respective income and expense totalled during the year, in addition to the respective receivables and payables in place as of 31 December 2011:

| Related party | Revenue transactions | Cost transactions |
|---|---|---|
| **Cassa Depositi e Prestiti S.p.A.** | | **Non energy-related items**<br>Credit line |
| **CESI S.p.A.** | **Non energy-related items**<br>Lease of laboratories and similar structures for specific purposes | **Non energy-related items**<br>Technical consultancy, studies and research, projects and experimentation |
| **Gruppo GSE** | **Energy-related items**<br>MIS component, energy sale, rights of withdrawal, rights to use transport capacity for interconnections, dispatching prices<br><br>**Non energy-related items**<br>Specialist services, leases, IT services | **Energy-related items**<br>Purchase of energy, rights to use transport capacity for interconnections, prices for lost wind-powered generation |
| **Gruppo Enel** | **Energy-related items**<br>Remuneration of the NTG and measurement aggregation, energy sale, rights of withdrawal, rights to use transport capacity for interconnections, dispatching prices<br><br>**Non energy-related items**<br>Lease and rent, line maintenance, works to move/vary lines | **Energy-related items**<br>Aggregation of measurements, purchase of energy, rights to use transport capacity for interconnections, EUSES remuneration<br><br>**Non energy-related items**<br>Return of electricity discount, staff administration, building services, supply of MV power to new stations, specialised services for connection to Terna control and protection systems |
| **Gruppo ENI** | **Energy-related items**<br>Sale of energy, rights to use transport capacity for interconnections, dispatching prices<br><br>**Non energy-related items**<br>Line maintenance | **Energy-related items**<br>Energy purchase, coverage of joint management costs, interruptibility service |
| **Gruppo Ferrovie** | **Energy-related items**<br>Dispatching prices, energy sale<br><br>**Non energy-related items**<br>Line moving | **Energy-related items**<br>NTG remuneration, energy purchase<br><br>**Non energy-related items**<br>Right-of-way fees |
| **ANAS S.p.A.** | **Non energy-related items**<br>Line moving/variants | **Non energy-related items**<br>Right-of-way fees |
| **Fondenel e Fopen** | | **Non energy-related items**<br>Pension contributions borne by the Terna Group |

| Company<br>€ million | Income statement | | | | | | |
|---|---|---|---|---|---|---|---|
| | Income items | | | | Expenses | | |
| | Grid transmission fees and other energy-related items | Grid transmission fees for other owners and pass-through energy items | Non energy-related items | Dividends | Grid transmission fees and other energy-related items | Grid transmission fees for other owners and pass-through energy items | Non energy-related items |
| De facto parent company | | | | | | | |
| Cassa Depositi e Prestiti S.p.A. | - | - | - | - | - | - | 9.8 |
| **Total de facto parent company** | **-** | **-** | **-** | **-** | **-** | **-** | **9.8** |
| Associates: | | | | | | | |
| CESI S.p.A. | - | - | 0.1 | - | - | - | 2.3 |
| **Total associates** | **-** | **-** | **0.1** | **-** | **-** | **-** | **2.3** |
| **Other related companies:** | | | | | | | |
| GSE Group | 25.9 | 1,132.9 | 0.5 | - | - | 769.4 | - |
| Enel Group | 1,187.8 | 685.2 | 1.6 | - | - | 810.1 | 2.6 |
| Eni Group | 4.3 | 266.3 | 0.4 | - | - | 127.8 | 0.1 |
| Ferrovie Group | 1.5 | 39.4 | 0.1 | - | 6.8 | 194.5 | 0.1 |
| ANAS S.p.A. | - | - | - | - | - | - | - |
| **Total other related companies** | **1,219.5** | **2,123.8** | **2.6** | **-** | **6.8** | **1,901.8** | **2.8** |
| **Pension funds:** | | | | | | | |
| Fondenel | | | | | | | 0.4 |
| Fopen | - | - | - | - | - | - | 1.8 |
| **Total pension funds** | **-** | **-** | **-** | **-** | **-** | **-** | **2.2** |
| **Total** | **1,219.5** | **2,123.8** | **2.7** | **0.0** | **6.8** | **1,901.8** | **17.1** |

| Company<br>€ million | Statement of financial position<br>Property plant and equipment<br>Capitalised costs | Receivables and other assets<br>Other | Receivables and other assets<br>Financial | Payables and other liabilities<br>Other | Payables and other liabilities<br>Financial | Guarantees (*) |
|---|---|---|---|---|---|---|
| De facto parent company | | | | | | |
| Cassa Depositi e Prestiti S.p.A. | - | - | 0.4 | - | 502.4 | - |
| **Total de facto parent company** | **-** | **-** | **0.4** | **-** | **502.4** | **-** |
| **Associates:** | | | | | | |
| CESI S.p.A. | 16.0 | - | - | 7.1 | - | 3.2 |
| **Total associates** | **16.0** | **-** | **-** | **7.1** | **-** | **3.2** |
| **Other related companies:** | | | | | | |
| GSE Group | - | 0.1 | - | 0.1 | - | - |
| Enel Group | 8.1 | 121.4 | - | 39.5 | - | 390.9 |
| Eni Group | - | 0.4 | - | 2.8 | - | 15.9 |
| Ferrovie Group | 0.1 | 0.1 | - | 0.5 | - | 22.0 |
| ANAS S.p.A. | - | 0.5 | - | 0.8 | - | - |
| **Total other related companies** | **8.2** | **122.5** | **-** | **43.7** | **-** | **428.8** |
| **Pension funds:** | | | | | | |
| Fondenel | | | | | | |
| Fopen | - | - | - | 1.4 | - | - |
| **Total pension funds** | **-** | **-** | **-** | **1.4** | **-** | **-** |
| **Total** | **24.2** | **122.5** | **0.4** | **52.2** | **502.4** | **432.0** |

(*) The guarantees refer to the bank guarantees received on contracts.

# H. Significant non-recurring events and transactions, and atypical or unusual transactions

No significant, non-recurring, atypical or unusual transactions – with the exception of those described above – were carried out during 2011, either with third parties or with related parties.

# I. Notes to the statement of cash flows

The cash flow generated from **continuing operations** in the year amounted to around €849.1 million, which reflects around €1,433.9 million in cash from operating activities (self-financing) and around €584.8 million in financial resources generated by the management of net working capital.
With regard to *discontinued operations and assets held for sale*, the finalisation of the sale of the equity interest in Rete Rinnovabile generated total liquidity of more than €200 million, including the realised profit (€50.6 million), the deconsolidation of the photovoltaic plants and the related commercial relations of the sold companies, as well as the net financial position of €254.6 million; the contribution arising from the disposal of NRTS to the Group self-financing amounted, instead, to €28.3 million.

In respect of continuing operations, **investing activities** used net financial resources of around €1,251.8 million, and included €1,166.0 million of investment in property, plant and machinery (€1,178.1 million net of plant grants totalling €12.1 million) and €51.1 million of investment in intangible assets. In this context, the value is also recognised of financial investments made for the purchase of 22.09% of the share capital in the Montenegro associate CGES (€36 million) and for the additional interest in CESI S.p.A. (€7.1 million).
The net change in **loan flows** mainly derives from the net increase in financial debt (€1,622.7 million), net of the disbursement of the 2010 dividend balance (€261.3 million) and the 2011 interim dividend (€160.8 million). More specifically, with reference to actual financial debt, please note the increase in medium/long-term debt (€1,845.8 million, including the short-term portion and net of FVH derivatives) – which, *inter alia*, reflects the March 2011 issue of a bond for a nominal value of €1,250.0 million – the repayment of a short-term loan taken out late 2010 (€50 million) and the subscription in 2011 of deposit certificates with maturity of less than 12 months, for a total of €150 million.
Other changes in the equity attributable to the owner of the Parent relate to the effects deriving from the exercise of stock options during the year (+€11.6 million in total) and the impact of the acquisition of addition interest shares in the associate CESI S.p.A. (a negative €1.0 million).
Therefore, considering the extraordinary transactions carried out during the year, the financial resources used in for investing activities and the remuneration of equity, total financial requirements came to €1,258.6 million in the year, part of which (€849.1 million) was covered by the cash flows generated by operating activities, and remainder through new borrowings.

# L. Subsequent events

## Resolutions published by the AEEG for the new tariffs in regulatory period 2012-2015

On **2 January 2012**, the Authority for Electricity and Gas (AEEG) published Resolutions nos. 199/11, 204/11 and 197/11 thereby establishing, for the new regulatory period 2012-2015, the remuneration for the supply of electricity transmission, distribution, measurement and dispatching services and the regulation of the quality of the transmission service. The new features introduced by AEEG Resolution 199/11 include taking the weighted average cost of capital (WACC) from the previous 6.9% to 7.4% and establishing a review by November 2013, to apply from the second two-year period of the regulatory period (2014-2015). There will also be a new incentive category (category I4) for an extra remuneration of accumulation systems amounting to 2% for a period of 12 years subsequent to the coming into service of the investments. As from 2012, the AEEG has recognised a further 1% on the WACC, aimed at compensating for the effect of the “regulatory lag”, i.e. the delay with which the tariff remunerates investments made. Resolution 204/11 updates for 2012 the price for the electricity dispatching service, amounting to €0.0526 c/kWh. Resolution 197/11 on the regulation of the quality of service confirms the framework of the previous regulatory period, based on a premium/penalty mechanism. Quality of service will only be monitored by the Energy not supplied index. With this mechanism, the potential maximum impact is estimated for the Terna Group as ranging between a negative €12 and a positive €30 million per year.

## Terna alone in the Gold Class of the Sam Sustainability Yearbook 2012

On **30 January 2012** Terna, the only Italian electrical company and amongst the world's best, joined the Gold Class of the Sam - Sustainability Yearbook 2012, the yearbook of the international ratings agency that screens companies, assessing the possibility of their accessing, remaining in or being excluded from the prestigious Dow Jones indexes. If we compare this result with those of previous years (Silver Class in 2011, Bronze Class in 2010), we can see that Terna is reinforcing, indeed improving its position in a global top position, coming before some of the best international operators.

## 5-year bond issue for €1.25 billion

On **13 February 2012** the Parent Company Terna launched a bond issue on the market in euros, at a fixed rate, with expiry in 5 years, for a total of €1.25 billion under the scope of its Euro Medium Term Notes (EMTN) programme. This has been assigned an A- Credit Watch Negative rating by Standard and Poor's, A3 Outlook Negative by Moody's and A by Fitch. The bond expiring on 17 February 2017 has an annual coupon of 4.125% and issue price of 99.809%. The bond has thus been priced with a spread of 257 basis points as compared with the midswap. The securities, which will pay one coupon per year, will be listed on the Luxembourg Stock Exchange.
This transaction is intended for Institutional Investors and is placed by a pool of banks comprising BNP Paribas, Credit Suisse, Deutsche Bank, J.P. Morgan, Mediobanca, MPS Capital Services, Natixis and Unicredit Bank AG as joint-lead managers and joint-bookrunners; it closed successfully that same day and was 4.5 times over-subscribed compared to the offer. The bond is intended to finance the grid development investments envisaged in the Company's business plan.

## Renewed Supervisory Body 231/2001

On **31 January 2012**, the Board of Directors of the Parent Company appointed the members of the Supervisory Body pursuant to Italian Legislative Decree no. 231/2001 which had expired in financial year 2011. Prof. Bruno Assumma was confirmed Chairman while Mr. Ernesto Calaprice and Mr. Massimo di Noia, Mr. Alberto Bianchi and Ms. Filomena Passeggio were appointed members. The Board also resolved that Mr. Fulvio De Luca will act as secretary of the Supervisory Body together with the audit function.

## Terna Cnra Gora share capital increase

On **10 February 2012**, the Parent Company subscribed a share capital increase of the subsidiary Terna Cnra Gora for €5 million, in order to provide the company with the resources necessary to develop the business.

## Terna rating

On **30 January 2012** Fitch Ratings revised the rating for the senior unsecured debt of Terna S.p.A. from A+ to A following the downgrading of the Italian Republic from A+ to A- with negative outlook. At the same time, Fitch confirmed both the long-term rating of the issuer as A with negative outlook and the short-term rating at F1.
On **8 March 2012** S&P confirmed the long and short-term rating of Terna S.p.A. at A- and A-2, respectively, and the senior unsecured debt rating at A-. In line with the Agency method for government related entities, these levels had been assigned to the Company on 20 January 2012, following the downgrading from A to BBB+ of the Italian Republic. At the same time, the Agency removed the "CreditWatch" status with negative implications, the long-term rating of the Company and the rating of the senior unsecured debt, a status assigned by the agency in December 2011. The outlook is negative.

## The Business plan

On **20 March 2012**, Terna approved the Terna Group Business Plan for the period 2012-2016; guidelines are set out below:

- **core business:** over the next 5 years, €4.1 billion will be invested in the safety and modernisation of the electricity grid, of which 82% will be for the National Transmission Grid development with investments focused on maximizing the use of system capacity and reducing congestion, fostering the development of generation capacity from renewable sources;
- **non-core business:** up to approximately €1 billion will be used for the development of battery accumulation systems for 240 MW, at present awaiting authorisation and in any case as long as suitable remuneration is obtained. Additionally, both in Italy and abroad, investments of up to 900 million are planned in projects for private customers, with a forecast return that exceeds that of regulated business. In thus doing, the objective expenditure in non-core business is doubled (up to €1.9 billion), with respect to the previous plan;
- **improved margins (EBITDA margin):** it is expected that the increased revenue and the control of costs will allow to achieve an accumulated EBITDA over the period 2012-16, up approximately 19% with respect to the previous five-year plan. Average annual growth in EBITDA goes from 5% to 7.5%, showing a consistent improvement in operative cash flow. At the end of the period, the EBITDA margin will exceed 80% increasing with respect to the previous target of 78%;
- **a sound capital structure:** the commitment to strengthen equity coefficients continues. During the course of the plan, net debt is estimated as growing by approximately €1.6 billion to €6.7 billion, with a significant reduction of €1 billion with respect to the previous plan. The capital structure remains solid: during the plan, the ratio of net debt and RAB remains below 55% in all years of the plan and the ratio of net debt and EBITDA with respect to the 4.2 times of end 2011, remaining below the 4 times;
- **new dividends policy:** as from 2012, a basic dividend is envisaged from core business amounting to 19 euro cents per share, in addition to the contribution of non-core business (payout of 60% on results and/or gains).

## Disclosure pursuant to art. 149-*duodecies* of the CONSOB Issuers Regulation

The following table, prepared in accordance with Art. 149-*duodecies* of the CONSOB Issuers Regulations, reports the fees for 2011 for the audit and non-audit services provided to the Terna Group by the same auditing company.

| In euros | Entity providing service | | Prices due for the year |
|---|---|---|---|
| | KPMG S.p.A. | PWC S.p.A.(*) | |
| Statutory audit | 178,300.00 | 247,414.90 | 425,714.90 |
| Attestation services | 109,793.61 | 52,800.00 | 162,593.61 |
| **Total** | **288,093.61** | **300,214.90** | **588,308.51** |

(*) Appointment made by the Ordinary Shareholders' Meeting on 13 May 2011 for the nine years 1 January 2011-31 December 2019.

The CEO

***Certification of the consolidated financial statements pursuant to Art. 81-ter of CONSOB Regulation no. 11971 dated 14 May 1999 and subsequent amendments and additions***

1. The undersigned Flavio Cattaneo, as CEO, and Luciano Di Bacco, as Executive in Charge of the preparation of accounting documents for TERNA S.p.A., also considering that established by art. 154-*bis*, paragraphs 3 and 4 of Italian Legislative Decree no. 58 of 24 February 1998, certify:

- the suitability in relation to the business characteristics; and
- the effective application of the administrative and accounting procedures for the preparation of the consolidated financial statements during financial year 2011.

2. On this regard, no significant aspects emerged.

3. It is also specified that:

3.1 the consolidated financial statements at 31 December 2011:

a) are prepared in compliance with the applicable international accounting standards recognised in the European Community in accordance with Regulation (EC) no. 1606/2002 of the European Parliament and Council of 19 July 2002 and the provisions issued in implementation of art. 9 of Italian Legislative Decree no. 38/2005;

b) comply with the results of the accounts and accounting entries;

c) are suitable to providing a truthful, correct representation of the equity, economic and financial position of the issuer and all companies included in the consolidation;

3.2 the report on operations includes a reliable analysis of the trend and operating result, in addition to the position of the issuer and all businesses included in the scope of consolidation and a description of the main risks and uncertainties to which they are exposed.

Rome, 20 March 2012


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# Report

Auditors' Report in accordance
with articles 14 and 16 of Legislative Decree no. 39 of 27 January 2010
Consolidated Financial Statements as of 31 December 2011

## AUDITORS' REPORT IN ACCORDANCE WITH ARTICLES 14 AND 16 OF LEGISLATIVE DECREE NO. 39 OF 27 JANUARY 2010

To the Shareholders of
Terna SpA

1 We have audited the consolidated financial statements of Terna SpA and its subsidiaries ("Terna Group") as of 31 December 2011 which comprise the statement of financial position, the income statement, the statement of comprehensive income, the statement of changes in equity, the statement of cash flows and the related notes. The directors of Terna SpA are responsible for the preparation of these financial statements in accordance with the International Financial Reporting Standards, as adopted by the European Union, and with the regulations issued to implement article 9 of Legislative Decree No. 38/2005. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

2 We conducted our audit in accordance with the auditing standards recommended by Consob, the Italian Commission for listed Companies and Stock Exchange. Those standards require that we plan and perform the audit to obtain the necessary assurance about whether the consolidated financial statements are free of material misstatement and, taken as a whole, are presented fairly. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the directors. We believe that our audit provides a reasonable basis for our opinion.

The consolidated financial statements of the prior year are presented for comparative purposes. As disclosed in the notes to the consolidated financial statements, the directors have reclassified certain comparative information related to prior year, compared to information previously presented and reviewed by other auditors, which issued their report dated 18 April 2011. We have examined the methods adopted to reclassify the comparative information of the prior year and related disclosure included in the notes to the consolidated financial statements for the purpose of issuing the audit opinion on the consolidated financial statements as of 31 December 2011.

3 In our opinion, the consolidated financial statements of Terna Group as of 31 December 2011 comply with the International Financial Reporting Standards, as adopted by the European Union, and with the regulations issued to implement article 9 of Legislative Decree No. 38/2005; accordingly, they have been prepared clearly and give a true and fair view of the financial position, result of operations and cash flows of Terna Group for the year then ended.

***PricewaterhouseCoopers SpA***

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4 The directors of Terna SpA are responsible for the preparation of the report on operations and the report on corporate governance and ownership structure in accordance with the applicable laws and regulations. Our responsibility is to express an opinion on the consistency of the report on operations and of the information referred to in paragraph 1, letters c), d), f), l), m), and paragraph 2, letter b), of article 123-bis of Legislative Decree No. 58/98 presented in the report on corporate governance and ownership structure, with the financial statements, as required by law. For this purpose, we have performed the procedures required under Italian Auditing Standard 1 issued by the Italian Accounting Profession (Consiglio Nazionale dei Dottori Commercialisti e degli Esperti Contabili) and recommended by Consob. In our opinion, the report on operations and the information referred to in paragraph 1, letters c), d), f), l), m) and paragraph 2, letter b), of article 123-bis of Legislative Decree No. 58/98 presented in the report on corporate governance and ownership structure are consistent with the consolidated financial statements of Terna Group as of 31 December 2011.

Rome, 18 April 2012

PricewaterhouseCoopers SpA

Signed by

Paolo Caccini
(Partner)

*This report is an English translation of the original audit report, which was issued in Italian. This report has been prepared solely for the convenience of international readers.*

# Separate financial statements

at 31 December 2011

Terna

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# Separate financial statements

# Income statement

| In euros | Note | 2011 | 2010 |
|---|---|---|---|
| **A. Revenue** | | | |
| 1. Revenue from sales and services | 1 | 1,515,963,890 | 1,459,126,551 |
| *of which: related parties* | | *1,505,504,944* | *1,420,000,250* |
| 2. Other revenue and income | 2 | 37,957,250 | 45,943,205 |
| *of which: related parties* | | *1,138,348* | *4,073,007* |
| **Total revenue** | | **1,553,921,140** | **1,505,069,756** |
| **B. Operating expenses** | | | |
| 1. Raw materials and consumables | 3 | 34,095,767 | 36,666,582 |
| *of which: related parties* | | *2,713* | *80,650* |
| 2. Services | 4 | 165,829,664 | 166,471,383 |
| *of which: related parties* | | *4,156,148* | *7,479,433* |
| 3. Personnel expenses | 5 | 214,240,270 | 214,836,298 |
| *- gross personnel expenses* | | *278,496,018* | *276,400,504* |
| *- personnel expenses, capitalised* | | *(64,255,748)* | *(61,564,206)* |
| *of which: related parties* | | *2,754,498* | *3,554,549* |
| 4. Amortisation, depreciation and impairment | 6 | 348,882,118 | 318,768,336 |
| 5. Other operating expenses | 7 | 18,078,990 | 17,808,652 |
| *of which: related parties* | | *329,064* | *246,904* |
| **Total operating expenses** | | **781,126,809** | **754,551,251** |
| **A-B Operating profit (EBIT)** | | **772,794,331** | **750,518,505** |
| **C. Financial income/expense** | | | |
| 1. Financial income | 8 | 157,668,834 | 29,180,259 |
| *of which: related parties* | | *20,693,596* | *17,960,646* |
| 2. Financial expense | 8 | (166,480,603) | (116,919,577) |
| *of which: related parties* | | *(10,898,440)* | *(1,353,972)* |
| **D. Profit before taxes** | | **763,982,562** | **662,779,187** |
| **E. Income taxes** | 9 | **344,213,830** | **232,100,228** |
| **F. Profit for the year from continuing operations** | | **419,768,732** | **430,678,959** |
| **G. Profit for the year from discontinued operations and assets held for sale** | 10 | **33,818,822** | **1,433,700** |
| **H. Profit for the year** | | **453,587,554** | **432,112,659** |

# Statement of comprehensive income

| In euros | Note | 2011 | 2010 |
|---|---|---|---|
| **Profit for the year** | | **453,587,554** | **432,112,659** |
| Other comprehensive income items for the year | | | |
| - Cash flow hedges net of tax effect | 20 | (34,685,551) | 25,917,385 |
| **Comprehensive income for the year** | | **418,902,003** | **458,030,044** |

# Statement of financial position
## Assets

| In euros | Note | 31.12.2011 | 31.12.2010 | 01.01.2010 |
|---|---|---|---|---|
| **A. Non-current assets** | | | | |
| 1. Property, plant and equipment | 11 | 7,514,015,690 | 6,687,666,965 | 5,890,992,393 |
| *of which: related parties* | | *37,215,423* | *48,665,342* | *15,340,771* |
| 2. Goodwill | 12 | 88,577,142 | 88,577,142 | 88,577,142 |
| 3. Intangible assets | 13 | 273,976,474 | 274,008,599 | 261,548,444 |
| 4. Non-current financial assets | 14 | 1,644,659,308 | 1,284,012,471 | 1,198,860,941 |
| *of which: related parties* | | *500,000,000* | *500,000,000* | *500,000,000* |
| 5. Other non-current assets | 15 | 6,556,985 | 6,295,263 | 5,539,468 |
| **Total non-current assets** | | **9,527,785,599** | **8,340,560,440** | **7,445,518,388** |
| **B. Current assets** | | | | |
| 1. Inventories | 16 | 12,385,102 | 11,353,045 | 11,707,939 |
| 2. Trade receivables | 17 | 1,684,024,162 | 1,495,632,378 | 1,177,146,436 |
| *of which: related parties* | | *125,827,102* | *157,663,489* | *130,665,643* |
| 3. Current financial assets | 14 | 158,185,137 | 2,921,817 | 503,278,695 |
| *of which: related parties* | | *3,028,213* | *2,816,880* | *2,684,770* |
| 4. Cash and cash equivalents | 18 | 933,043,878 | 168,718,782 | 81,468 |
| *of which: related parties* | | *(181,311,199)* | *18,604,996* | *0* |
| 5. Income tax assets | 19 | 4,200,000 | 4,200,000 | 4,200,000 |
| 6. Other current assets | 15 | 17,039,991 | 18,643,499 | 26,521,078 |
| *of which: related parties* | | *3,894* | *761,928* | *1,088,319* |
| **Total current assets** | | **2,808,878,270** | **1,701,469,521** | **1,722,935,616** |
| **C. Discontinued operations held for sale** | | **0** | **504,591,056** | **57,367** |
| **Total assets** | | **12,336,663,869** | **10,546,621,017** | **9,168,511,371** |

# Statement of financial position
## Liabilities

| In euros | Note | 31.12.2011 | 31.12.2010 | 01.01.2010 |
|---|---|---|---|---|
| **D. Equity** | | | | |
| 1. Share capital | | 442,198,240 | 440,967,054 | 440,199,936 |
| 2. Other reserves | | 766,874,399 | 791,002,191 | 758,627,068 |
| 3. Retained earnings | | 1,053,482,789 | 1,043,214,157 | 619,512,997 |
| 4. Interim dividend | | (160,799,360) | (160,351,656) | (140,063,616) |
| 5. Profit for the year | | 453,587,554 | 432,112,659 | 804,224,735 |
| **Total Equity** | 20 | **2,555,343,622** | **2,546,944,405** | **2,482,501,120** |
| **E. Non-current liabilities** | | | | |
| 1. Long-term loans | 21 | 6,738,696,429 | 5,147,465,361 | 4,199,231,857 |
| *of which: related parties* | | *500,000,000* | *0* | *0* |
| 2. Employee benefits | 22 | 119,228,211 | 122,338,330 | 125,067,204 |
| 3. Provisions for risks and charges | 23 | 142,222,950 | 165,009,275 | 147,861,138 |
| 4. Deferred tax liabilities | 24 | 169,082,674 | 223,705,836 | 248,001,763 |
| 5. Non-current financial liabilities | 21 | 111,425,992 | 47,126,002 | 82,553,826 |
| 6. Other non-current liabilities | 25 | 129,109,886 | 136,604,167 | 151,567,857 |
| **Total non-current liabilities** | | **7,409,766,142** | **5,842,248,971** | **4,954,283,645** |
| **F. Current liabilities** | | | | |
| 1. Short-term loans | 21 | 0 | 73,118,084 | 42,632,206 |
| *of which: related parties* | | *0* | *0* | *2,640,220* |
| 2. Current portion of long-term loans | 21 | 59,689,067 | 59,689,067 | 59,689,067 |
| 3. Trade payables | 26 | 2,047,720,626 | 1,522,764,668 | 1,487,642,509 |
| *of which: related parties* | | *65,596,362* | *67,626,377* | *45,910,293* |
| 4. Tax liabilities | 26 | 88,143,944 | 69,094,800 | 20,825,680 |
| 5. Current financial liabilities | 21 | 40,114,622 | 24,240,177 | 25,524,303 |
| *of which: related parties* | | *2,406,806* | *2,423,611* | *1,156,250* |
| 6. Other current liabilities | 26 | 135,885,846 | 133,146,671 | 95,412,841 |
| *of which: related parties* | | *3,962,547* | *3,143,863* | *5,517,902* |
| **Total current liabilities** | | **2,371,554,105** | **1,912,053,467** | **1,731,726,606** |
| **G. Liabilities of discontinued operations and assets held for sale** | | **0** | **245,374,174** | **0** |
| **Total liabilities and equity** | | **12,336,663,869** | **10,546,621,017** | **9,168,511,371** |

# Statement of changes in equity

31 DECEMBER 2010 - 31 DECEMBER 2011 — SHARE CAPITAL AND RESERVES TERNA S.P.A.

| € millions | Share/quota capital | Legal reserve | Share premium reserve | Hedging reserve | Other reserves | Retained earnings | Interim dividend | Profit for the year | Equity |
|---|---|---|---|---|---|---|---|---|---|
| **At 31 December 2010** | **441.0** | **88.0** | **8.6** | **(35.3)** | **729.7** | **1,043.2** | **(160.4)** | **432.1** | **2,546.9** |
| **Equity at 31 December 2010** | **441.0** | **88.0** | **8.6** | **(35.3)** | **729.7** | **1,043.2** | **(160.4)** | **432.1** | **2,546.9** |
| **Profit for the year** | | | | | | | | **453.6** | **453.6** |
| **Other comprehensive income:** | | | | | | | | | |
| Change in fair value of derivatives and cash flow hedges, net of tax effect | | | | (34.7) | | | | | (34.7) |
| **Total other comprehensive income** | **0.0** | **0.0** | **0.0** | **(34.7)** | **0.0** | **0.0** | **0.0** | **0.0** | **(34.7)** |
| **Comprehensive income** | **0.0** | **0.0** | **0.0** | **(34.7)** | **0.0** | **0.0** | **0.0** | **453.6** | **418.9** |
| **Transactions with equity owners:** | | | | | | | | | |
| Allocation of 2010 profit | | | | | | | | | |
| *- 2010 dividend* | | | | | | | *160.4* | *(421.7)* | *(261.3)* |
| *- 2010 retained earnings* | | *0.2* | | | | *10.2* | | *(10.4)* | *0.0* |
| Exercise of stock options | 1.2 | | 11.4 | | (1.0) | | | | 11.6 |
| 2011 interim dividend | | | | | | | (160.8) | | (160.8) |
| **Total transactions with equity owners** | **1.2** | **0.2** | **11.4** | **0.0** | **(1.0)** | **10.2** | **(0.4)** | **(432.1)** | **(410.5)** |
| **Equity at 31 December 2011** | **442.2** | **88.2** | **20.0** | **(70.0)** | **728.7** | **1,053.4** | **(160.8)** | **453.6** | **2,555.3** |

31 DECEMBER 2009 - 31 DECEMBER 2010 — SHARE CAPITAL AND RESERVES TERNA S.P.A.

| € millions | Share/quota capital | Legal reserve | Share premium reserve | Hedging reserve | Other reserves | Retained earnings | Interim dividend | Profit for the year | Equity |
|---|---|---|---|---|---|---|---|---|---|
| **At 31 December 2009** | **440.2** | **88.0** | **1.8** | **(61.2)** | **730.1** | **619.5** | **(140.1)** | **790.0** | **2,468.3** |
| Adjustment of opening balances | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 14.2 | 14.2 |
| **Equity at 31 December 2009** | **440.2** | **88.0** | **1.8** | **(61.2)** | **730.1** | **619.5** | **(140.1)** | **804.2** | **2,482.5** |
| **Profit for the year** | | | | | | | | **432.1** | **432.1** |
| **Other comprehensive income:** | | | | | | | | | |
| Change in fair value of derivatives and cash flow hedges, net of tax effect | | | | 25.9 | | | | | 25.9 |
| **Total other comprehensive income** | **0.0** | **0.0** | **0.0** | **25.9** | **0.0** | **0.0** | **0.0** | **0.0** | **25.9** |
| **Comprehensive income** | **0.0** | **0.0** | **0.0** | **25.9** | **0.0** | **0.0** | **0.0** | **432.1** | **458.0** |
| **Transactions with equity owners:** | | | | | | | | | |
| Allocation of profit 2009 | | | | | | | | | |
| *- 2009 dividend* | | | | | | | *140.1* | *(380.5)* | *(240.4)* |
| *- 2009 retained earnings* | | | | | | *423.7* | | *(423.7)* | *0.0* |
| Exercise of stock options | 0.8 | | 6.8 | | (0.4) | | | | 7.2 |
| 2010 interim dividend | | | | | | | (160.4) | | (160.4) |
| **Total transactions with equity owners** | **0.8** | **0.0** | **6.8** | **0.0** | **(0.4)** | **423.7** | **(20.3)** | **(804.2)** | **(393.6)** |
| **Equity at 31 December 2010** | **441.0** | **88.0** | **8.6** | **(35.3)** | **729.7** | **1,043.2** | **(160.4)** | **432.1** | **2,546.9** |

(*) The retrospective application of IFRIC 12 - Service Concession Arrangements had no effect on opening equity at 31 December 2009.

# Statement of cash flows (*)

| € million | 2011 | 2010 |
|---|---|---|
| **Profit for the year** | **453.6** | **432.1** |
| **Adjustments for:** | | |
| Amortisation, depreciation, impairment losses/(reversals of impairment losses) on property, plant and equipment and intangible assets (**) | 340.2 | 310.2 |
| Provisions (including employee-related provisions) and impairment losses | 49.2 | 58.0 |
| (Gains)/Losses on disposals of property, plant and equipment | (3.9) | (3.1) |
| Financial (income)/expense | 10.0 | 81.4 |
| Income taxes | 345.3 | 235.5 |
| **Cash flows generated by operating activities, before changes in net working capital** | **1,194.4** | **1,114.1** |
| Increase/(Decrease) in provisions (including employee-related and tax provisions) | (79.4) | (45.4) |
| (Increase)/Decrease in inventories | (1.0) | 0.3 |
| (Increase)/Decrease in trade receivables and other current assets | (36.4) | (288.5) |
| Increase/(Decrease) in other non-current liabilities | 1.1 | (6.4) |
| Increase/(Decrease) in other non-current assets | (533.8) | (205.2) |
| Increase/(Decrease) in trade payables and other current liabilities | 572.2 | 199.7 |
| Interest income and other financial income received | 111.9 | 127.4 |
| Dividend received | 100.0 | 0 |
| Interest expense and other financial expense paid | (219.6) | (215.9) |
| Income taxes paid | (347.1) | (209.1) |
| **Cash flows generated by operating activities [a]** | **762.3** | **471.0** |
| Investments in property, plant and equipment, net of recognised grants | (1,110.9) | (1,051.3) |
| Revenue from sale of property, plant and equipment and intangible assets | 7.4 | 4.4 |
| Investments in intangible assets, net of grants received | (49.7) | (56.8) |
| Intra-group transactions | (18.0) | (21.2) |
| Increase in investments | (39.0) | (8.0) |
| **Cash flows used in investing activities [b]** | **(1,210.2)** | **(1,132.9)** |
| Changes in share capital | 1.2 | 0.8 |
| Changes in reserves | 10.4 | 6.4 |
| Dividends paid | (422.1) | (400.8) |
| Changes in short- and medium/long-term financial payables and loans (including short-term portions) (***) | 1,518.1 | 978.7 |
| Change in short-term financial investments | (150.0) | 500.0 |
| Assets held for sale | 254.6 | (254.6) |
| **Cash flows generated by financing activities [c]** | **1,212.2** | **830.5** |
| **Increase/(Decrease) in cash and cash equivalents [a+b+c]** | **764.3** | **168.6** |
| Opening cash and cash equivalents | 168.7 | 0.1 |
| Closing cash and cash equivalents | 933.0 | 168.7 |

(*) For comments on the statement of cash flows, please see the section "Notes to the statement of cash flows" in the Notes to the financial statements.
(**) Net of set-up grants taken to income statement for the year.
(***) Net of FVH derivatives.

# Notes to the separate financial statements

# A. Accounting policies and measurement criteria

## Introduction

Terna S.p.A., which operates in the electrical energy transmission and dispatching sector, is a public limited company headquartered in Via Egidio Galbani 70, Rome, Italy. These separate financial statements have been authorized for publication by the Directors on 20 March 2012.
The separate financial statements as at and for the year ended 31 December 2011 are available upon request within the registered office of the company Terna S.p.A., Viale Egidio Galbani, 70 Rome or at the website www.terna.it.

## Compliance with IAS/IFRS

The separate financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS), International Accounting Standards (IAS) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and the Standing Interpretations Committee (SIC), endorsed by the European Commission (IFRS-EU) at that date.
This document has also been prepared by taking into account the provisions of Legislative Decree no. 38 of 28 February 2005, the Italian Civil Code and CONSOB Resolutions nos. 15519 (*"Provisions governing financial statements in implementation of Art. 9, paragraph 3, of Legislative Decree no. 38/2005"*) and 15520 (*"Amendments to the implementing rules for Legislative Decree no. 58/1998"*), both of 27 July 2006, as well as CONSOB Communication no. DEM/6064293 of 28 July 2006 (*"Disclosure requirements for listed issuers and issuers of financial instruments that are widely held among the public and pursuant to Art. 116 of the Consolidated Financial Act"*).
The separate financial statements have been prepared on a historic cost basis, modified where necessary for certain financial instruments, as well as on a going concern basis. The Company has determined that, despite the challenging economic and financial environment, it does not face material uncertainties (as defined in paragraph 25 of IAS 1) that might cast doubt on its ability to continue as a going concern.

## Basis of presentation

The separate financial statements consist of the statement of financial position, the income statement, the statement of comprehensive income, the statement of cash flows, the statement of changes in equity and the notes thereto.
In the statement of financial position, assets and liabilities are classified on a "current/non-current" basis, with separate reporting of assets and liabilities held for sale. Current assets, which include cash and cash equivalents, are those held for realisation, sale or consumption in the Company's normal operating cycle. Current liabilities are those expected to be settled in the Company's normal operating cycle or within one year from the reporting date.
The income statement is classified on the basis of the nature of costs. The income statement is presented as two statements, the first of which (income statement) presents the components of profit or loss for the year; while the second (statement of comprehensive income) starts with the result for the year and then presents the revenue and expense items (including reclassification adjustments) that are recognised in equity rather than profit or loss for the year.
The statement of cash flows has been prepared using the indirect method.
The financial statements are accompanied by the Directors' Report for Terna S.p.A. and the Terna Group, which as from the 2008 financial year has been prepared as a single document, exercising the option granted under Legislative Decree no. 32 of 2 February 2007, which amended Art. 40 (Directors' Report on Operations) of Legislative Decree no. 127 of 9 April 1991.
The financial statements have been prepared in euros, while the figures in the notes are given in millions of euros, unless otherwise specified.
The financial statements have been prepared using the historic cost method, with the exception of captions that are recognised at fair value in accordance with IFRS-EU, as indicated in the accounting policies for each caption.
It is specified that some comparative balances of the financial statements as of 31 December 2010 have been adjusted to consider the change in the accounting model of the effects arising from the decision taken in financial year 2009, to adhere to the release of the goodwill established by Italian Law Decree no. 185 of 29 November 2008, enacted by Italian Law no. 2 of 28 January 2009. The change from the substitute tax model recorded as an advance on current taxes to the substitute tax model recorded by recognising deferred tax assets has, therefore, entailed the recording as of 31 December 2010 of greater deferred tax assets (classified amongst net deferred tax liabilities) for an amount of €25.2 million and lower tax assets for €12.6 million, with an impact of €14.2 million recorded as retained earnings and €1.6 million as lower result (greater current taxes) under the shareholders' equity as of 31 December 2010.

## Use of estimates

The preparation of the statement of financial position and income statement in accordance with the IFRS-EU requires the use of estimates and assumptions that affect the carrying amounts of assets and liabilities and related disclosures, in addition to contingent assets and liabilities at the reporting date. The estimates and associated assumptions are based on previous experience and various factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed periodically and the effects of any changes are recognised in the income statement for the year, if they relate solely to that period. If changes affect both that year and future years, the change is recorded in the year in which the estimate is reviewed as well as in the relative future years.
The critical areas for key estimates and assumptions used by management in applying the IFRS endorsed by the European Commission that could have significant effects on the separate financial statements or that could give rise to risks that would entail significant adjustments to the carrying amounts of assets and liabilities in subsequent years are summarised below.

### Employee benefits

The liability for employee benefits paid upon or following termination of employment in relation to defined benefit plans or other long-term benefits is recognised net of any plan assets and is measured on the basis of actuarial assumptions, estimating the amount of future benefits that employees have vested at the reporting date.

### Provisions for risks and charges

Accruals to the provisions for risks and charges are recognised when, at the reporting date, there is a legal or constructive obligation as a result of a past event, and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the financial effect of the passage of time is material, accruals are measured by discounting the estimated outflow at a pre-tax discount rate that reflects current market assessments of the time value of money and, if applicable, the risks specific to the liability. Any increase in provisions associated with the passage of time is taken to the income statement under “Financial expenses”.

### Allowance for impairment accounts

Trade receivables are initially recognised at fair value net of any impairment losses relating to sums considered non recoverable, which are taken to the specific allowance for impairment accounts. Impairment losses are measured on the basis of the present value of estimated future cash flows, discounted at the original effective interest rate.

### Recoverable amount of non-current assets

Property, plant and equipment and intangible assets are analysed at least once a year to check for indications of impairment. If there is an indication that an asset may be impaired, its recoverable amount is estimated.
Recoverable amount is the higher of an asset’s fair value, net of costs to sell and its value in use, measured by discounting estimated future cash flows considering available information at the time of estimate and on the basis of subjective assessments of the performance of future variables – such as prices, costs, demand growth rates, production profiles – and discounted at a rate that reflects current market assessments of the time value of money with respect to the investment period and the risks specific to the asset.

## Investments in subsidiaries and associates

Investments in subsidiaries are those in entities over which Terna has the power to directly or indirectly govern financial and operating policies so as to obtain benefits from their activities. Investments in associates are those in entities over which Terna has significant influence.
In assessing whether or not the Company has control or significant influence, potential voting rights that are presently exercisable or convertible are considered.
Investments in subsidiaries and associates are measured at cost, reduced to reflect impairment losses. If the reasons for the impairment losses no longer exist, the carrying amount of the investment is reinstated within the limits of the impairment losses, and the reversal is taken to profit or loss.
In the event that an investee’s losses attributable to the shareholders of the Parent Company exceed that investments’ carrying amount, any excess is recognised in a specific provision, where the Parent Company is required to meet the legal or construction obligations of the investee or, in any case, to cover its losses.

## Translation of foreign currency items

Terna S.p.A. prepares its financial statements in euros, which is also the functional currency. In these financial statements, all transactions in currencies other than the functional currency are recognised at the exchange rate prevailing on the date of the transaction. Monetary assets and liabilities in currencies other than the functional currency are subsequently adjusted at the exchange rate prevailing at year end. Any exchange rate differences are taken to profit or loss.
Non-monetary assets and liabilities in foreign currency stated at historic cost are converted at the exchange rate prevailing when the transaction was initially recognised. Non-monetary assets and liabilities in foreign currency stated at fair value are converted at the exchange rate prevailing when fair value was measured.

## Business combinations

The Company books business combinations in compliance with the updated version of IFRS 3 – Business combinations, approved on 3 June 2009 by the European Commission with Regulation no. 495/2009 and which came into force on 1 January 2010. The change in the accounting standard has been applied prospectively and has had no significant effect on earnings per share.
Business combinations are booked using the purchase method, on the date of purchase or rather on the date on which control is effectively obtained, defined as the power to determine the financial and managerial policies of an entity in order to obtain benefits from its operations. In assessing the existence of such control, the Company must consider the voting rights that can potentially be exercised.
The new provisions of IFRS 3 require, among other matters, the expensing of costs associated with business combinations, inclusive of settlement costs, and the recognition through profit or loss of any changes in contingent consideration; they also allow full recognition of the goodwill arising from the transaction, including the portion attributable to non-controlling interests (full goodwill method). The standard establishes that the potential price shall be booked at fair value on the date of purchase. If this price is classified as shareholders' equity, it needs not be recalculated and its subsequent repayment must be booked to shareholders' equity. If not, subsequent changes to the fair value of the potential price are booked to the year profit or loss.
The new provisions also change the current criterion for the recognition of step acquisitions, envisaging the recognition through profit or loss of the difference, at the time of acquiring control, between the fair value of the net assets previously held and their carrying amount.
For acquisitions made subsequent to 1 January 2010, the Company measures goodwill on the date of purchase at fair value, increased by any non-controlling interest in the company acquired, including, where the combination takes place in several stages, the fair value of the interest held previously, all deducted from the net amount booked for identifiable assets purchased and identifiable liabilities assumed. When the excess, calculated in this way, is negative, in the year profit or loss is immediately recognised income deriving from a purchase made at favourable prices.
On 3 June 2009, with Regulation 494/2009 issued by the European Commission, the updated version of IAS 27 – Statutory and separate financial statements was also approved. In compliance with the new standard, acquisitions of non-controlling interests are booked as transactions implemented with shareholders, as shareholders and as such these transactions shall not give rise to the recording of goodwill. Adjustments made to non-controlling interests are based on a proportional amount of the net assets of the subsidiary. The revised version of IAS 27 requires, among other matters, that the effects deriving from the acquisition (disposal) of equity investments subsequent to the acquisition of control (without loss of control) be recognised in equity. Furthermore, the new regulations establish that in the event of disposal of part of the shares in investments held with subsequent loss of control, joint control or association, the shareholding maintained must be adjusted to its fair value and the revaluation contributes to the gain (loss) deriving from the disposal.
The new standard does not apply retrospectively, but only in relation to any business combinations that take place subsequent to the date on which it comes into force.

## Property, plant and equipment

Property, plant and equipment are recognised at historic cost, including costs directly attributable to putting the asset in the condition necessary for it to be capable of operating in the manner for which it was acquired. In the event of legal or constructive obligations, cost also includes the present value of the estimated cost of disposal or removal of the asset. The corresponding liability is recognised in the provisions for contingencies and charges. Borrowing costs directly attributable to the acquisition, construction or production of an asset that qualify for capitalisation pursuant to IAS 23R are capitalised as part of the cost of the asset. For more information, please see the section “Financial income and expense” below. Costs incurred after purchase are recognised as an increase in the carrying amount of the asset to which they relate if it is probable that the future benefits of that cost will flow to the Company and if the cost can be reliably measured. All other costs are recognised in profit or loss when incurred.
Each element of an item of property, plant and equipment of material value, with respect to the total value of the item to which it belongs, is recognised and depreciated separately.
Certain assets that were revalued at 1 January 2005 (transition date) or previously are recognised at the revalued amount, which is considered deemed cost at the date of the revaluation.
Certain assets that were revalued at 1 January 2005 (transition date) or previously are recognised at the revalued amount, which is considered deemed cost at the date of the revaluation.
Property, plant and equipment are shown net of accumulated depreciation and any impairment losses, which are measured as described below. Depreciation is calculated on a straight-line basis over the estimated useful economic life of the asset, which is reviewed annually, with revisions applied on a prospective basis. The depreciation of assets begins when the assets become available for use.
Liabilities associated with items of property, plant and equipment are taken to a specific provision as a balancing entry to the related asset. The amount is taken to profit or loss through the depreciation of the asset.

The main depreciation rates calculated on the basis of the related asset’s useful life are as follows:

DEPRECIATION RATES

| | |
|---|---|
| Civil and industrial buildings | 2.50% |
| Transmission lines | 2.50% |
| | |
| Transformer stations: | |
| - Electrical machinery | 2.38% |
| - Electrical devices and equipment | 3.13% |
| - Automation and control systems | 6.70% |
| | |
| Central systems for remote management and control: | |
| - Devices, electrical equipment and ancillary plants | 5.00% |
| - Electronic calculation equipment | 10.00% |

Land, regardless of whether it is free of construction or related to civil and industrial buildings, is not depreciated, since it has an indefinite useful life.
Property, plant and equipment acquired under finance leases, through which the Company has acquired substantially all the risks and rewards of ownership, are recognised as Company assets at the lower of fair value and the present value of minimum lease payments due, including any amounts to be paid to purchase the asset at the end of the lease. The corresponding liability to the lessor is recognised under financial payables. Assets are depreciated using the criteria and rates described above. If the company is not reasonably certain that it will acquire ownership at the end of the lease, the asset is depreciated over the shorter of the term of the lease and the asset’s useful life.
Leases in which the lessor maintains substantially all the risks and rewards of ownership are classified as operating leases. Costs related to operating leases are taken in full to profits or losses over the term of the lease.

## Intangible assets

Intangible assets, which all have finite useful lives, are recognised at cost, having obtained, if necessary, the approval of the Board of Statutory Auditors, and shown net of accumulated amortisation and any impairment losses, measured as described below.

Amortisation begins when the asset becomes available for use and is calculated on a straight-line basis over the estimated useful life of the related asset, which is reviewed annually. Any revisions to estimated figures are applied on a prospective basis.

Intangible assets essentially regard the exclusive license to carry out electricity transmission and dispatching activities and other intangible assets. In particular, Terna S.p.A. obtained the license for electricity transmission and dispatching activities in Italy on 1 November 2005 when it acquired the TSO business unit. As established in the Decree issued by the Ministry of Productive Activities on 20 April 2005, this license runs for twenty-five years, renewable for another twenty-five years, from the date of effective transfer of the activities, functions, assets and legal arrangements of the concession from GSE (formerly GRTN) to Terna S.p.A.. This intangible asset was initially recognised at cost, which reflected fair value.

Other intangible assets mainly relate to the following:

- the development and innovation of application software to manage the electricity invoicing process;
- the development and innovation of application software to protect the electrical system;
- software applications related to the development of the Power Exchange, particularly relating to the registration of operators, consumption units and the development of foreign procedures.

Development costs are capitalised by the Company only if all following conditions are met: costs can be reliably estimated and there are technical possibilities and intent to complete the intangible asset so as for it to be available after use; the asset can be used and it is possible to demonstrate that it will generate probable future economic benefits.

Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset pursuant to IAS 23R are capitalised as part of the cost of the asset. For more information, please see the section “Financial income and expense” below. These intangible assets are amortised over their estimated residual useful life, which is normally three years, given their rapid obsolescence.

### Rights on the infrastructure

IFRIC 12 – Service Concession Arrangements (also “Interpretation”) came into force on 1 January 2010. IFRIC 12 specifies the accounting treatment of service concession arrangements, not expressly governed by any specific accounting standard, in order to ensure the consistency and comparability of the financial statements of companies that hold concessions for the delivery of public services. More specifically, the interpretation sets out rules for accounting for the infrastructure used to provide the services under concession, for the costs associated with developing and maintaining such infrastructure, and for the revenue generated by the overall provision of the services. IFRIC 12 does not apply to all arrangements. Its scope is limited to service concession arrangements between public bodies and private operators in which the granter: (1) controls the use of the infrastructure and governs which services are to be provided, the manner in which they are to be provided and the prices of such services and (2) controls any residual interest in the infrastructure at the end of the concession period. The interpretation also applies to infrastructure constructed by or obtained from third parties for the provision of services under the concession, and to existing infrastructure that the granter makes available to the operator in order to provide such services. It does not apply to infrastructure owned and accounted for as property, plant and equipment by the operator prior to entering into the service concession arrangement.

Assisted by external consultants, Terna has performed a detailed study of the applicability of IFRIC 12 and the effects of its adoption on the financial statements, identifying that this interpretation does not apply to the transmission activities aspect of Terna’s concession. In particular, neither the concession nor related legislation envisage the NTG’s return to public ownership, either via the payment of an indemnity or otherwise. Accordingly, the public sector does not control, whether as owner or as holder of beneficial interests or other rights, any significant residual interest in the NTG’s infrastructure at the end of the concession period.

By contrast, the Ministry is entitled to reclaim the operating assets employed directly in dispatching activities at the end of the concession. As such, the Group considers that IFRIC 12 does apply to its dispatching infrastructure since the relevant criteria apply: the services provided are regulated and control exists over the residual interest. More specifically, in view of the rate system for dispatching activities, the intangible asset model has been applied. Consequently, the property, plant and equipment and intangible assets employed in the dispatching activities, carried out under concession, are classified as “Intangible assets”, in the “Infrastructure rights” caption, with application of the original amortisation schedule.

The revenue and costs relating to the investment in dispatching activities are recognised with reference to the contracts concerned on a stage-of-completion basis; revenue recognised during the construction phase is limited to the amount of the internal and external construction costs incurred, considering that the fair value of the construction services is equivalent to the construction cost recognised to third-party contractors plus the internal cost of the technical personnel employed on such construction activities.

By contrast, tariff revenue continues to be recognised in accordance with IAS 18 and borrowing costs continue to be capitalised pursuant to IAS 23R.

## Impairment losses

Property, plant and equipment and intangible assets with finite useful lives are tested at least once a year to check for evidence of impairment. If there is an indication that an asset may be impaired, its recoverable amount is estimated.
The recoverable amount of goodwill and intangible assets with indefinite useful lives, where present, as well as intangible assets not yet available for use, is estimated at least annually.
Recoverable amount is equal to the greater of fair value less costs to sell and value in use. Value in use is measured by discounting estimated future cash flows considering available information at the time of estimate and on the basis of subjective assessments of the performance of future variables, such as prices, costs, demand growth rates, production profiles, and discounted at a pre-tax rate that reflects current market assessment of the time value of money for the investment period and risks specific to the asset. If the intangible asset does not generate cash inflows that are largely independent, the asset's recoverable amount is calculated as part of the CGU to which it belongs.
An impairment loss is recognised in the income statement when the asset's book value, or the net invested capital of the CGU to which it belongs, is greater than its recoverable amount.
Impairment losses of CGUs are first taken as a reduction in the carrying amount of any allocated goodwill and then as a reduction in other assets of the CGU on a pro rata basis. Except for goodwill, impairment losses may be reversed up to the recoverable amount if there is an indication that the impairment loss no longer exists or when there is a change in the methods used to measure recoverable amount.

## Inventories

Inventories are recognised and measured at the lower of purchase cost and net estimated realisable value. Cost is calculated as the weighted average cost, including related charges. Net estimated realisable value stands for the estimated price of sale under normal conditions net of completion costs and the estimated costs to sell.

## Contract work in progress

When the profit or loss on a contract can be reliably estimated, the related contract costs and revenue are recognised separately in the income statement on a percentage of completion basis. Progress is measured based on the work carried out and measured proportionally to the ratio of costs for the works carried out up to reporting date and total cost of the contract (cost-to-cost). Differences between the value of completed contracts and payments on account received are recognised under statement of financial position assets or liabilities, considering any impairment losses on the work carried out so as to take into account the risks of customers' refusal to recognise the work performed. Expected contract losses are immediately taken to profit or loss.
Contract costs include all those costs that relate directly to the specific contract, as well as fixed and variable costs incurred by the Company as part of normal operations.

## Financial instruments

### Financial assets

Any financial assets other than financial derivatives that the Company has the positive intention and ability to hold to maturity are recognised at cost at the settlement date, which is the fair value of the initial consideration given in exchange, including transaction costs. They are subsequently measured at amortised cost, using the effective interest method, net of any impairment losses, which are determined as the lower of the asset's carrying amount and the present value of estimated future cash flows, discounted using the original interest rate. Financial assets are derecognised when, following their transfer or settlement, the Company is no longer involved in their management and no longer holds the risks and rewards of the transferred or settled instruments.

### Trade receivables

Trade receivables are initially recognised at fair value and subsequently measured at amortised cost, using the effective interest method, and net of any impairment losses due to sums considered non-recoverable, which are taken to the specific allowance for impairment. Impairment losses are measured on the basis of the present value of estimated future cash flows, discounted at the original effective interest rate.
Receivables with due dates that fall under normal commercial terms are not discounted.

### Cash and cash equivalents

Cash and cash equivalents are stated at nominal value. They include monetary items, i.e. amounts that are available on demand or with a very short maturity, subject to an insignificant risk and without collection costs.

### Trade payables

Trade payables are initially recognised at fair value and subsequently stated at amortised cost. If their due date falls under normal commercial terms, they are not discounted.

### Financial liabilities

Financial liabilities other than financial derivatives are recognised at the settlement date and measured at fair value, net of directly related transaction costs.
Subsequently, financial liabilities are measured at amortised cost, using the original effective interest method. If the liabilities are covered by fair value hedges, they are adjusted to reflect changes in fair value with respect to the hedged risk.

### Derivative financial instruments

Derivatives are recognised at fair value at the trade date and classified as hedges if the relationship between the derivative and the hedged item is formally documented and the hedge is highly effective within a range of 80% to 125%, as initially verified and periodically checked. When derivatives cover the risk of changes in the cash flows of the hedged instruments (cash flow hedges), the part of changes in the fair value qualifying as effective is initially taken to "Other comprehensive income" and subsequently to profit or loss, in line with the effects of the hedged transaction. The portion of the fair value of the hedging instrument that does not qualify as effective is taken to profit or loss.
When hedging derivatives cover the risk of changes in the fair value of hedged instruments (fair value hedges), they are recognised at fair value in the income statement. Accordingly, the hedged items are adjusted to reflect changes in the fair value associated with the hedged risk.
Changes in the fair value of derivatives that do not meet hedge accounting requirements in accordance with the IFRS-EU are recognised in profit or loss.
Fair value is measured on the basis of official quotations for instruments traded in regulated markets. The fair value of instruments not traded in regulated markets is measured by discounting projected cash flows along a yield curve of interest rates at the reporting date, and by converting amounts in currency other than the euro at the year-end exchange rate.
Financial and non-financial contracts (which are not already measured at fair value) are also analysed to identify any embedded derivatives, which must be separated and measured at fair value. This analysis is conducted at the time the entity becomes party to the contract or when the contract is renegotiated in a manner that produces a material change in the original associated cash flows.
The measurement techniques used for derivatives existing at year end did not change with respect to the previous year. Accordingly, the effects in profit or loss and "Other comprehensive income" of these measurements are essentially attributable to normal market developments, as well as new derivative contracts signed during the year.

## Employee benefits

The liability in respect of employee benefits payable upon or after termination of employment relates to defined benefit plans (termination benefits, additional month's pay, indemnity for lack of notice, energy discount, ASEM health benefits and other benefits) or other long-term employee benefits (loyalty bonus) and is recognised net of any plan assets. It is measured separately for each plan on the basis of actuarial calculations that estimate the amount of future benefits that employees have accrued at the reporting date. The liability is recognised on an accruals basis over the vesting period. It is measured by independent actuaries.
Actuarial gains and losses at 1 January 2005 (date of transition to IFRS-EU) were recognised in equity. After that date, unrecognised actuarial gains and losses in excess of 10% of the greater of the present value of the defined benefit plan obligation and the fair value of plan assets are taken to profit or loss for the average expected term of service of employees participating in the plan. Otherwise, actuarial gains and losses are not recognised.

## Provisions for risks and charges

Accruals to the provisions for risks and charges are recognised when, at the reporting date, the Company has a legal or constructive obligation towards others as a result of a past event and it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the effect of the time value of money is material, accruals are measured by discounting estimated future cash flows using a pre-tax discount rate that reflects current market assessment of the time value of money and those risks specific to the liability, if present. Where discounting is used, the increase in the provision due to the passage of time is recognised in the income statement as interest expense. If the liability relates to property, plant and equipment (site disposal and restoration, for example), the provision is recognised as a balancing entry to the asset to which it relates. The expense is recognised in profit or loss through depreciation of the item of property, plant and equipment to which it relates.
Changes in the estimate are recognised within the income statement for the year in which the change happens, except for those costs expected for dismantling, removal and reclamation, which come as a result of changes in the timing and use of economic resources necessary to extinguish the obligation or attributable to a material change in the discount rate, which are recognised as an increase or reduction of the related assets and recognised in profit or loss through depreciation.

## Share-based payments

The cost of employee service remunerated through Stock Option Plans is measured at the fair value of the options granted to employees at the grant date. The fair value of options granted is recognised under personnel expense over the vesting period, with a corresponding effect on "Other comprehensive income", considering the best possible estimate of the number of options that employees will be able to exercise. Such estimate is reviewed where subsequent information indicates that the expected number of instruments representative of capital that will mature differs from the estimate previously carried out, regardless of achievement of the market conditions.
The measurement method used to calculate fair value considers all the characteristics of the options (term, price and conditions, etc.), as well as the price of Terna S.p.A. shares at the grant date, the volatility of the stock and the yield curve at the grant date, in line with the term of the plan.
At the vesting date, the estimate is revised through the income statement to recognise the actual amount corresponding to the number of equity instruments that have actually vested, regardless of achievement of the market conditions.

## Grants

Grants received in relation to specific assets whose value is recognised under non-current assets are, for plants operating before 31 December 2002, recognised under other liabilities and taken to profit or loss over the depreciation period of the related assets. From 2003, grants for new plants that have entered operation are recognised as a direct reduction in the value of the related asset.
Grants for operating expenses are expensed in full when the recognition requirements are satisfied.

## Revenue

Revenue is recognised when it is probable that the economic benefits deriving from the operation will be used by the enterprise. Depending on the type of transaction, revenue is recognised on the basis of the following specific criteria:

- revenue from the sale of goods is recognised when the material risks and rewards of ownership of the goods have been transferred to the buyer and their total amount can be reliably determined and collected;
- revenue from services rendered is recognised with reference to the stage of completion of the transaction. If revenue cannot be reliably measured, it is recognised to the extent of recoverable costs;
- revenue accrued during the year in respect of contract work in progress is recognised on the basis of the payments agreed for the progress of works using the cost-to-cost method. In addition to contractual payments, project revenue includes any payments in respect of variations, price revisions and incentives, with the latter recognised where it is probable that they will actually be earned and can be reliably determined. Revenue is also adjusted for any penalties for delays attributable to the Company;
- when the recovery of an amount already recognised in revenue is uncertain, the non-recoverable value or the amount whose recovery is no longer probable is recorded as a cost, with recognition of a balancing entry in provisions for risks and charges;
- amounts collected on behalf of third parties, such as the fees paid to non-Terna grid owners, as well as revenue recognised for managing activities related to the balancing of the National Electrical System, which do not increase equity, are reported net of the related costs. This reporting method, which reflects the substance of transactions by offsetting revenue with the related costs arising from the “same transaction”, is discussed in full in a specific section of the explanatory notes.

## Financial income and expense

Borrowing costs directly attributable to the acquisition, construction or production of an asset that qualify for capitalisation are capitalised as part of the cost of the asset. The qualifying assets (property, plant and equipment and intangible assets) involved are those that require at least one year before being ready for use. The directly attributable borrowing cost is that which would not have been incurred if the expenditure for the asset had not been incurred.
Where funds are borrowed specifically, costs eligible for capitalisation are the actual costs incurred less any income earned on the temporary investment of such borrowings. Where funds are raised through general borrowing, the eligible amount is determined by applying a capitalisation rate to the expenditure on that asset. The capitalisation rate will be the weighted average of the borrowing costs applicable to the general pool, excluding any specifically borrowed funds. The amount of borrowing costs capitalised during a year shall in any case not exceed the amount of borrowing costs incurred during that year.
Capitalisation commences as from the date all the following conditions have been met: (a) expenditures have been incurred for the asset; (b) borrowing costs are being incurred; and (c) activities to prepare the asset for its intended use or sale are in progress. Capitalisation ceases when the activities necessary to prepare the asset for its intended use or sale are substantially complete. The capitalisation rate used for 2011 amounts to 3.08% and that for 2010 amounts to 2.63%.
Financial income and expense other than capitalised amounts are recognised on an accruals basis in respect of the interest on the net value of the related financial assets and liabilities using the effective interest rate.

## Dividends

The dividends of associates are booked when it is established that shareholders have the right to receive payment. This generally coincides with the date of the meeting resolution.
Dividends and interim dividends payable to third parties are shown as changes in equity at the date in which they are approved by the Shareholders’ Meeting and the Board of Directors, respectively.

## Income taxes

Current income taxes, recognised under “tax liabilities” net of prepayments, or under “tax assets” when there is a net credit balance, are recognised on the basis of estimated taxable income and in accordance with current legislation, taking account of any applicable exemptions.
Deferred tax assets and liabilities are calculated on the temporary differences between the carrying amounts of assets and liabilities recognised in the separate financial statements and the corresponding amounts recognised for tax purposes, using current tax rates or the rates expected to be in effect when the temporary differences reverse, based on current rates or those that are substantially approved at the reporting date.

Deferred tax assets are recognised when their recovery is considered probable, i.e. when future taxable income will be available against which the asset can be used. The recoverability of deferred tax assets is reviewed at each year end. Deferred tax liabilities are recognised in any case if they exist.
Taxes in respect of components recognised in “Other comprehensive income” are also recognised in the same item.

## Discontinued operations and non-current assets held for sale

Non-current assets (or disposal groups) whose carrying amount will be recovered principally through a sale rather than through continuing use are classified as held for sale and reported separated from other assets and liabilities in the statement of financial position. Non-current assets (or disposal groups) classified as held for sale are first measured in conformity with the IFRS/IAS applicable to each asset and liability and subsequently are measured at the lower of their carrying amount and fair value less costs to sell. The carrying amounts of each asset and liability that are not governed by the measurement rules set out in IFRS 5, but are held for sale, are remeasured on the basis of the applicable IFRS before the fair value less costs to sell is redetermined. The individual assets of the companies classified as held for sale are not amortised, whereas financial expense and other expenses attributable to liabilities held for sale continue to be recognised. Any subsequent impairment losses are recognised directly as an adjustment to the carrying amount of the non-current assets (or disposal groups) classified as held for sale through profit or loss. The corresponding statement of financial position values for the previous year are not reclassified. A discontinued operation is a component of an entity that either has been disposed of, or is classified as held for sale, and:
- represents a separate major line of business or geographical area of operations;
- is part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations; or
- is an operation acquired exclusively with a view to resale.

## New standards

### International Financial Reporting Standards taking effect from 1 January 2011
The following international financial reporting standards and related interpretations took effect from 1 January 2011:

#### Amendment of IAS 24 – Related Party Disclosures
Issued on 4 November 2009, this amendment simplifies the disclosure requirements for related party for government-related entities (i.e. entities subject to control, joint control or significant influence by a government body), and clarifies the definition of a related party eliminating certain application.

#### Amendment of IFRS 7 – Financial instruments: disclosures – Transfers of financial assets
With European Commission Regulation no. 1205/2011 issued on 22 November 2011, the disclosure required on financial instruments in the financial statements is extended. The amendment will allow users of financial statements to better evaluate exposure to risk connected with the transfer of financial assets and the effects of said risks on the entity’s financial position. According to that established by the new Regulation, the entity must provide a disclosure that enables users of the financial statements to understand: the ratio of the financial assets transferred and not fully eliminated and the associated liabilities; to assess the nature, and related risks, of the residual involvement of the entity in the financial assets eliminated.
This standard has not had a significant impact on the separate financial statements at 31 December 2011.

#### Improvements to the IFRS (published in 2010)
2010 version of the document that contains minor amendments to the standards already published. This group of amendments was endorsed during the first quarter of 2011 and came into force on 1 January 2011.

The following standards and interpretations have also been endorsed and come into force, and govern circumstances that are not relevant to the financial statements of the Company at the moment:
- amendment to IAS 32 – Financial instruments – Presentation: classification of rights issues (or warrants);
- amendment to IFRIC 14 – Prepayment of a minimum funding requirement;
- IFRIC 19 – Extinguishing financial liabilities – Extinguishing financial liabilities with equity instruments.

### International financial reporting standards endorsed but not yet in force
At the date on which these financial statements were prepared, no international reporting standards had been endorsed by the European Commission that had not yet come into force.

### International financial reporting standards not yet endorsed

For amendments, new standards and interpretations that have not yet been endorsed by the EU, but which address issues that affect or could affect Terna, the Company is assessing the possible impact of their application on its financial statements, taking account of the date on which they take effect. This assessment covers the standards and interpretations listed below.

### IFRS 9 – Financial Instruments

On 12 November 2009, the IASB published standard IFRS 9 – Financial instruments on the classification and measurement of financial assets applicable no longer as from 1 January 2013 but from 1 January 2015, as proposed by the IASB amendment (currently being endorsed), which postpones the coming into force. The new standard arises from a complex procedure, articulated into various different stages that aims to entirely replace IAS 39; for the stages currently published by the IASB, the new standard defines the classification criteria of financial assets and liabilities and derecognition of financial assets from the financial statements. More specifically, to determine the measurement criteria of financial assets, it introduces a unique approach that, replacing the many different methods in IAS 39, is based on the methods by which financial instruments are managed and on the characteristics of the contractual cash flow of the financial assets themselves. On the contrary, for financial liabilities, the main change concerns the representation of "Other Comprehensive Income" (OCI) of the effects of changes to the fair value assigned to the credit risk of liabilities measured at fair value, which will no longer be stated on the income statement.

Finally, we stress that the adoption process of standard IFRS 9 is currently suspended in the EU, given that the European Commission intends to proceed with the approval of the standard only upon conclusion of the definitive standard publication by IASB, when the replacement of IAS 39 has been completed.

### New accounting standards on the consolidation

On 12 May 2011, the IASB completed the draft concerning consolidation with the publication of the following 5 standards (IFRS 10, IFRS 11, IFRS 12, IAS 27 Amended, IAS 28 Amended), the first application of which is scheduled for 1 January 2013, with a probable postponement of one year as required by EFRAG. In particular:

### IFRS 10 – Consolidated Financial Statements

The standard introduces a single control model that is valid for all types of entity, superseding SIC 12 – Consolidation of SPE (Specific Purpose Entity) and removing from IAS 27 the part relating to control and consolidation. In particular, the standard introduces a new definition of control, based on the figures of the investee (a company actually or potentially controlled) and the investor (the Parent Company drawing up the separate financial statements), which has the control if it is exposed, or has variable returns with respect to its involvement in the investee and has the possibility of affecting these returns through its power over the investee. Additionally, in identifying the investor, both potential yet substantive voting rights must be considered, where the holder has the real possibility of exercising these rights, in addition to actual control, intended as the possibility of unilaterally guiding activities. The first application of the standard will be retrospective.

### IFRS 11 – Joint Arrangements

The new standard introduces important simplifications as it supersedes the 3-type classification as established by IAS 31. The new classification is based on the analysis of the rights and obligations arising from the agreement and establishes only two types: joint operations and joint ventures. The former derive from a non-structured agreement through an SPV that is separated from the parties, which determines rights over the assets and obligations of the liabilities, in accounting terms the controlling share of assets, liabilities and the corresponding costs and revenue is noted. The second, on the other hand, are classified as joint ventures where there are structured agreements through an SPV that is separated from the parties. In this case, the entity must carry out assessments based on the legal form of the "SPV", the contractual terms and the other facts and circumstances from which the rights over the net assets of the agreement derive. For joint ventures, the standard provides for the elimination of the proportional consolidation method, replaced by the equity method only. The new standard therefore replaces IAS 31 and SIC 13.

### IFRS 12 – Disclosure of interests in other entities

The standard governs the disclosure to be made in the financial statements with regard to the equity interests held in subsidiaries, associates and joint control companies in addition to structured entities, in lieu of the requirements previously included in IAS 27 and IAS 28. The objective of the new standard is to require additional information in the financial statements in relation to the basis for the control evaluation, any limits to consolidated assets and liabilities and exposure to risk deriving from the involvement with the entity.

### Amendment to IAS 27 – Separate Financial Statements

The amendment to IAS 27 has the objective of setting standards to be applied in accounting for investments held in subsidiaries, joint ventures and associates when preparing separate (non-consolidated) financial statements. The amendment therefore leaves unchanged the provisions for separate financial statements, and replaces the parts relating to the separate financial statements with the prescriptions of the new IFRS 10, to which reference should be made for further details.

### Amendment to IAS 28 – Investments in Associates and Joint Ventures

The amendment to IAS 28 (as amended in 2011) sets out the requirements for the application of the equity method when accounting for investments in associates and joint ventures.

### IFRS 13 – Fair Value Measurement

On 12 May 2011, the IASB published IFRS 13, which seeks to increase consistency and comparability in fair value measurements and related disclosures through a “fair value hierarchy”. The hierarchy categorises the inputs used in valuation techniques into three levels. The hierarchy gives the highest priority to quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs. The first application is scheduled for 1 January 2013.

### Amendment to IAS 19

On 16 June 2011, the IASB published an amendment to IAS 19 – Employee benefits, which introduces changes to the recognition and measurement of employee benefits related and severance indemnity costs and the disclosure on all employee benefits. The amendment has eliminated the option to defer the recognition of actuarial gains and losses using the corridor method and provided for the recognition of the cost connected with work rendered and net financial expenses on the income statement, the recognition of actuarial gains and losses deriving from remeasurements of assets and liabilities to be presented in “Other Comprehensive Income” (OCI). Additionally, the return on the asset included amongst net financial expenses must be calculated according to the liability discount rate and no longer on the forecast return on the asset. Finally, the amendment also introduces new additional information to be given in the notes to the financial statements. The amendment applies retrospectively from the financial year beginning on 1 January 2013.

### Amendment to IAS 1

On 16 June 2011, the IASB published an amendment to IAS 1 – Presentation of the financial statements. This established, amongst other aspects, to group together items within the "Other Comprehensive Income" (OCI), that may be reclassified to the profit or loss section of the income statement. The first application is scheduled for 1 January 2013.

### Amendment to IAS 12 – Deferred tax: recovery of underlying assets

The amendment affects all the entities that apply IAS 40 – Investment property using the fair value method and that have recognised assets under property, plant and equipment which are not depreciated and which are recorded using the revaluation model established by IAS 16. At present, therefore, the amendment does not cover situations presented in our financial statements.

### Amendment to IFRS 1 – Severe hyperinflation and removal of fixed dates for first-time adopters.

Two amendments to IFRS 1 were published: the first one replaces references to fixed transition date of 1 January 2004 with “the date of transition to IFRSs”. As a result, entities adopting IFRSs for the first time would not have to restate derecognition transactions that occurred before the date of transition to IFRSs. The second amendment provides specifications on how an entity should resume presenting financial statements in accordance with IFRSs after a period when the entity was unable to comply with the IFRSs since its functional currency was subject to severe hyperinflation.

The following standards and interpretations have also been published, governing circumstances currently not relevant to the financial statements of the Company:

- amendment to IAS 32 – Financial instruments: Offsetting Financial Assets and Financial Liabilities, provides clarifications on the application of rules by which to offset financial assets and liabilities; it will come into force on 1 January 2014;
- amendment to IFRIS 7 – Financial Instruments: Disclosures – Offsetting Financial Assets and Financial Liabilities, on the supplementary information to be supplied in relation to the actual or potential effects of the application of rules of offsetting financial assets and liabilities; the amendment will come into force on 1 January 2013;
- IFRIC 20 – Stripping costs in the Production Phase of Surface Mine – Accounting treatment of the costs of stripping a surface mine, to be recognised during production.

# B. Operating segments

Consistent with the provisions of IFRS 8 – Operating segments concerning companies that publish the consolidated financial statements of a parent company in the same document as the financial statements of that parent company, operating segment disclosures are provided for the consolidated financial statements only. Accordingly, please see the analogous section of the notes to the financial statements of the Terna Group.

# C. Notes to the income statement

## Revenue

### 1. Revenue from sales and services - €1,516.0 million

The table below details "Revenue from sales and services" for 2011 and 2010:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Grid transmission fees | 1,237.5 | 1,175.0 | 62.5 |
| Adjustments for prior year grid transmission fees | 0.1 | (2.0) | 2.1 |
| Other energy revenue | 163.4 | 169.8 | (6.4) |
| Other revenue from sales and services | 115.0 | 116.3 | (1.3) |
| **Total** | **1,516.0** | **1,459.1** | **56.9** |

**Grid transmission fees and related adjustment**

This caption reports revenue from the Company's core business, comprising fees paid to it for use of the National Transmission Grid.

The item amounted to €1,237.6 million in 2011, shows an increase of €64.6 million on the previous financial year, attributable to:

- effects of AEEG Resolution 228/10, which reviewed tariffs for 2011 (€51.2 million, including the incentive on the remuneration of strategic works pursuant to AEEG Resolution 87/10);
- increased grid transmission fees related to the Defence plan (€11.3 million);
- positive impact for the greater net negative grid transmission fees adjustments recognised in 2010 (€2.1 million).

**Other energy revenue**

This caption comprises the fees paid to the Company by electricity companies for dispatching services (DIS component, €129.3 million), together with the revenue from the construction and development of dispatching infrastructure recognised pursuant to IFRIC 12 (€34.1 million); please note that, as specified in section "A. Accounting policies and measurement criteria", such revenue corresponds to the costs incurred during the same period to purchase raw materials and consumables, services and staff which are included in operating expenses.

The decrease in the item, amounting to €6.4 million, reflects the drop in revenue deriving from the investments made during the financial year in dispatching infrastructures (€4.2 million) and the economic effects connected with the DIS component and which are due to:

- DIS tariff component for €9.9 million;
- regulating providing incentives for the quality of the transmission service (AEEG Resolution 169/08 – €3.2 million);
- adaptation of the measurement of the incentives mechanism associated with the reduction in volumes procured from the Market for Dispatching Services made available under AEEG Resolution 213/09 (€66,0 million, being a negative €11,0 million compared with €77,0 million incentives reported in 2010). More specifically, we would recall that the result achieved is recognised in terms of fair value in consideration of the three-year nature (2010/2012) of the incentive mechanism, as extensively commented in the 2010 financial report, to which we would refer;
- incentives linked to the increasing of the efficiency in the forecast for domestic energy demands and in the forecast production provided by wind power sources (down by €4.3 million).

### Other energy items - pass-through revenue/costs

This caption includes revenue and costs of a “pass-through” nature (whose balance is therefore nil). They arise in respect of daily purchases and sales with operators on the electricity market to carry out dispatching activities. To that end, the measurements at each point of input and withdrawal are taken and the differences from the energy market schedules are calculated. These differences (called imbalances) are measured using algorithms established by the regulatory framework. The net charge resulting from the measurement of these imbalances and of the buying and selling transactions executed by Terna on the Market for Dispatching Services are billed on a pro rata basis to each consumer with the uplift fee.
It also includes the remuneration paid by Terna to the other owners of the grid.

The components of these transactions are detailed below.

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| **Revenue - Power Exchange:** | | | |
| Foreign market - exports | 0.8 | 1.1 | (0.3) |
| Sale of energy on the Day Ahead Market, Adjustment Market, Market for Dispatching Service and others | 594.7 | 653.4 | (58.7) |
| Unbalancing and other minor items | 1,003.4 | 928.3 | 75.1 |
| Resources procurement for the Market for Dispatching Servces | 1,261.4 | 1,152.5 | 108.9 |
| Congestion rent - rights for use of transportation capacity (RTC), Res. no. 288/06 | 693.7 | 821.4 | (127.7) |
| Other items - Power Exchange | 65.2 | 140.4 | (75.2) |
| Interconnector/shipper | 79.0 | 125.6 | (46.6) |
| Market coupling Res.143/10 | 79.6 | 0.0 | 79.6 |
| **Total revenue - Power Exchange** | **3,777.8** | **3,822.7** | **(44.9)** |
| Revenue components under Res. nos. 168/04 - 237/04 and others | 1,048.9 | 817.3 | 231.6 |
| Other items | 182.7 | 171.4 | 11.3 |
| Revenue from grid transmission fees of other owners and GRTN share CIP/6 | 157.5 | 157.7 | (0.2) |
| **Total revenue from outside the Power Exchange** | **1,389.1** | **1,146.4** | **242.7** |
| **Total pass-through energy revenue** | **5,166.9** | **4,969.1** | **197.8** |
| **Energy purchases:** | | | |
| On Day Ahead Market and Adjustment Market | 98.5 | 160.3 | (61.8) |
| To provide the dispatching service | 1,433.8 | 1,664.8 | (231.0) |
| For unbalancing | 1,270.5 | 902.7 | 367.8 |
| On the foreign market - imports | 2.7 | 0.5 | 2.2 |
| Electricity Market Operator fees | 0.8 | 2.7 | (1,9) |
| Congestion rent - RTC, Res. no. 288/06 | 420.1 | 513.9 | (93.8) |
| Other items - Power Exchange | 60.9 | 72.7 | (11.8) |
| Interconnector/shipper | 417.0 | 505.1 | (88.1) |
| Market coupling Res.143/10 | 73.5 | 0.0 | 73.5 |
| **Total costs - Power Exchange** | **3,777.8** | **3,822.7** | **(44.9)** |
| Purchase of electricity market related services | 1,048.9 | 817.3 | 231.6 |
| Other items | 182.7 | 171.4 | 11.3 |
| Fees to be paid to NTG owners, GRTN and other | 157.5 | 157.7 | (0.2) |
| **Total services and fees** | **1,389.1** | **1,146.4** | **242.7** |
| **Total pass-through energy costs** | **5,166.9** | **4,969.1** | **197.8** |

### Other revenue from sales and services

"Other revenue from sales and services" amounted to €115.0 million and mainly relates to revenue from a variety of specialised high- and very-high-voltage services that the Company provides to third-party customers (€35.6 million) and the subsidiary Terna Rete Italia (€59.8 million). The amount reflects revenue from:

- NTG connection services of production plants and property of end users (€5.8 million);
- line design for inter-connection with abroad (€1.4 million);
- the contribution due to the Company for coverage of cost incurred for electricity discounts to its employees (€1.5 million);
- management fees services mainly for the subsidiaries Terna Rete Italia (€7.3 million) and SunTergrid (€1.5 million).

The decrease of €1.3 million is mainly due to the greater orders of 2010 connected with the development/extension of power stations and the related connections to the NTG (€11.0 million), offset by the increase in the current financial year of maintenance business and development and rationalisation works on HV plants of the subsidiary Terna Rete Italia (€8.8 million) in addition to NTG connection services of third party plants (€0.9 million).

## 2. Other revenue and income - €37.9 million

"Other revenue and income" for the years 2011 and 2010 are analysed in the following table:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Rental income | 16.2 | 17.8 | (1.6) |
| Sundry grants | 8.6 | 8.6 | 0.0 |
| Insurance settlements for losses | 2.2 | 5.8 | (3.6) |
| Gains on the disposal of plant components | 4.0 | 3.4 | 0.6 |
| Prior period income | 0.6 | 6.6 | (6.0) |
| Sales to third parties | 3.1 | 2.5 | 0.6 |
| Contractual penalties at suppliers' expense | 1.8 | 0.3 | 1.5 |
| Other revenue | 1.4 | 1.0 | 0.4 |
| **Total** | **37.9** | **46.0** | **(8.1)** |

Rental income mainly includes rent from the Wind Group for the housing of optical fibre on the grid (€11.4 million) and Enel Distribuzione's use of the Company's infrastructure for power line communication (€1.2 million).
The €8.1 million decrease in the item is mainly due to the greater contingency assets (€6.0 million) and the greater insurance reimbursements for damages to primary plants (€3.5 million) recorded during the previous financial year; these changes are partly offset by revenue from penalties charged to suppliers in 2011 for breach of contract (€1.5 million).

## Operating expenses

## 3. Raw materials and consumables - €34.1 million

This item, amounting to €34.1 million, expresses the value of the consumption of materials and miscellaneous equipment used for the core business of operation and maintaining plants in addition to costs for materials recognised in pursuance of IFRIC 12 and with reference to investing activities in dispatching infrastructures. The decrease of €2.6 million with respect to the previous financial year (€36.7 million in 2010) is mainly due to the lesser investing activities in dispatching infrastructures for optimisation on the Services Market realised in 2010 (a negative €2.4 million).

## 4. Services - €165.8 million

The table below details services for 2011 and 2010:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Tenders on plants | 52.0 | 52.0 | 0.0 |
| Maintenance and sundry services | 59.0 | 62.1 | (3.1) |
| Insurance | 5.7 | 5.8 | (0.1) |
| Remote transmission and telephone | 13.7 | 14.2 | (0.5) |
| IT services | 24.3 | 21.3 | 3.0 |
| Leases and rentals | 11.1 | 11.1 | 0.0 |
| **Total** | **165.8** | **166.5** | **(0.7)** |

The item "Services" refers to costs for tenders and services for routine maintenance operations and plant maintenance and expenditures for general services (a total of €111.0 million). It also includes costs for IT services (€24.3 million) remote transmission and telephone services (€13.7 million), leases and rentals (€11.1 million), and insurance (€5.7 million). It is specified that the costs relating to remuneration relating to the Board of Statutory Auditors amount to €0.2 million.
The item is basically in line with the previous financial year (a negative 0.7 million) as a result of the combination of lesser dispatching infrastructures development business (pursuant to IFRIC 12, €1.9 million) and the increase, during this financial year, in the routine maintenance work on NTG plants (€1.3 million).

## 5. Personnel expenses - €214.2 million

Personnel expense breaks down as follows:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Wages, salaries and other short-term employee benefits | 250.4 | 254.5 | (4.1) |
| Directors' fees | 1.9 | 1.5 | 0.4 |
| Termination indemnities, electricity discount and other post-employment benefits | 16.1 | 15.8 | 0.3 |
| Early retirement incentives | 10.1 | 4.6 | 5.5 |
| ***Personnel expenses, gross*** | ***278.5*** | ***276.4*** | ***2.1*** |
| Personnel expenses, capitalised | (64.3) | (61.6) | (2.7) |
| **Total** | **214.2** | **214.8** | **(0.6)** |

This caption includes the cost of wages and salaries, social security contributions and other costs incurred by the Company for voluntary early retirement incentives, as well as benefits paid to employees who stay with the Company and termination indemnities provided for by the current national collective employment contract for the electricity sector.
The figure for financial year 2011 is basically in line with the previous year. The increase in gross personnel expenses, amounting to €2.1 million, is more than offset by the increased capitalised personnel expenses (amounting to €2.7 million), as a result of the greater investments made during the year.
The following table shows the number of employees by category at year end and the average number for the year:

| | Average number | | Final number | |
|---|---|---|---|---|
| | 2011 | 2010 | 31.12.2011 | 31.12.2010 |
| Senior management | 60 | 64 | 60 | 59 |
| Junior management | 504 | 495 | 490 | 502 |
| Office staff | 1,949 | 1,897 | 1,966 | 1,890 |
| Production workers | 1,005 | 1,030 | 977 | 1,017 |
| **Total** | **3,518** | **3,486** | **3,493** | **3,468** |

The net change in the average number of employees at the end of 2010 was an increase of 32 units.
Reference should be made to section "22. Employee benefits" for the reconciliation of the opening and closing present value of the liability for employee benefits and the main assumptions used in the actuarial estimate.

## 6. Amortisation, depreciation and impairment - €348.9 million

These relate to accruals during the year calculated on the basis of amortisation and depreciation rates that reflect the useful lives of the Company's plant, property and equipment and intangible assets.
The composition of and changes in the item during the year are reported in the following table:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Amortisation on intangible fixed assets | 49.7 | 44.4 | 5.3 |
| *of which: infrastructure rights* | *25.1* | *23.7* | *1.4* |
| Depreciation of property, plant and equipment | 299.1 | 274.4 | 24.7 |
| Impairment of trade receivables | 0.1 | 0.0 | 0.1 |
| **Total** | **348.9** | **318.8** | **30.1** |

The increase of €30.1 million with respect to the 2010 figure is due to the greater amortisation and depreciation (totalling €30.0 million), mainly due to the entry into operation during the year of new plants and intangible assets of the Company.

## 7. Other operating expenses - €18.1 million

Other operating expenses break down as follows:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| Indirect and local taxes and duties | 5.2 | 5.6 | (0.4) |
| Accruals to provisions for risks and charges | 4.1 | 1.8 | 2.3 |
| Contingent liabilities | 1.8 | 2.4 | (0.6) |
| Power failure charges | 1.2 | 2.0 | (0.8) |
| Losses on the disposal/closure of plants | 0.1 | 0.3 | (0.2) |
| Other operating expenses | 5.7 | 5.7 | 0.0 |
| **Total** | **18.1** | **17.8** | **0.3** |

Sundry operating expenses recognised during the financial year mainly consist of taxes, duties and local taxes (€5.2 million, of which €2.7 million relating to the local property tax and €1.5 million in relation to rates for occupying public areas and spaces), accruals to the provisions for risks and charges (€4.1 million, mainly for expenses to be paid to the distributing companies for removing the transformation plants connected to the NTG and for the share in the indemnity to end users, for €2.4 million), the contribution for power failures (pursuant to Resolution 333/07 – €1.2 million) and other operating expenses.
The caption shows substantially no change on the previous year.

## Financial income and expense

### 8. Net financial income/(expense) - a negative €8.8 million

This caption is analysed below:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| **Financial income** | | | |
| Dividends from SunTergrid | 100 | 0.0 | 100.0 |
| Financial income from subsidiaries | 20.7 | 18.0 | 2.7 |
| Other financial income | 5.4 | 0.0 | 5.4 |
| Interest income and other financial income | 30.4 | 9.0 | 21.4 |
| Debt adjustment (bonds) and related hedges | 0.0 | 2.2 | (2.2) |
| Exchange gains | 1.2 | 0.0 | 1.2 |
| **Total income** | **157.7** | **29.2** | **128.5** |
| **Financial expense** | | | |
| Financial expense from the Parent | (9.8) | (1.3) | (8.5) |
| Financial expense to subsidiaries | (1.1) | 0.0 | (1.1) |
| Interest expense on medium/long-term loans and related hedges | (172.7) | (121.1) | (51.6) |
| Debt adjustment (bonds) and related hedges | (0.2) | 0.0 | (0.2) |
| Discounting of post-employment benefits and other personnel-related provisions | (4.5) | (4.9) | 0.4 |
| Exchange losses | 0.0 | (5.6) | 5.6 |
| Other financial expense | (4.1) | (0.7) | (3.4) |
| Capitalised borrowing costs | 25.9 | 17.4 | 8.5 |
| Impairment of investments in JV | 0.0 | (0.7) | 0.7 |
| **Total expense** | **(166.5)** | **(116.9)** | **(49.6)** |
| **Total** | **(8.8)** | **(87.7)** | **78.9** |

Net financial expense amounted to €8.8 million for the year, comprising €166.5 million in financial expense and €157.7 million in financial income. The decrease of €78.9 million with respect to last year is the net result of the following main factors:

- dividends for €100.0 million distributed by the subsidiary SunTergrid;
- greater financial income from subsidiaries (€2.7 million), mainly due to the impact of the increased short-term interest rate on the loan granted to the subsidiary Terna Rete Italia S.r.l.;
- greater net financial income (€2.0 million) mainly originating from the companies transferred (€1.4 million);
- increased financial proceeds (€21.4 million) which were primarily attributable to the joint effect of:
  - greater liquidity invested at higher interest rates (€21.2 million);
  - lower late payment interest for the late payment of receivables in respect of dispatching activities (a negative €0.4 million);
  - recording of greater net income for uplift (€0.7 million);
- exchange rate adjustment (€6.8 million) of the fund relating to the sale of the equity interest of the Brazilian subsidiaries;
- the net economic loss deriving from the fair value adjustment of bonds and the related hedges (a negative €2.4 million);
- recognition of greater financial expense to the parent CDP (a negative €8.5 million) deriving from the use of the loan of €500 million on 8 April 2011;
- greater financial expense with regard to subsidiaries in relation to interest accrued on correspondent accounts with the subsidiaries Terna Rete Italia S.r.l. and SunTergrid (a negative €1.1 million);
- greater financial expense deriving from medium and long-term debt and the related hedges (a negative €51.6 million) due to the increased gross debt and the rise in market interest rates in 2011;
- lower financial expense deriving from the discounting of employee benefits (€0.4 million);
- greater capitalised financial expense (€8.5 million) as a result of greater capital expenditure during 2011 compared with the previous financial year;
- lesser expenses for €0.7 million deriving from the 2010 impairment of the equity interest in Elmed Études.

## 9. Income taxes - €344.2 million

Income taxes for the financial year amount to €344.2 million, up by €112.1 million on the previous financial year, substantially by virtue of the "corrective manoeuvre-*bis*" (the "Robin Hood Tax"), which entailed greater taxes of 129.2 million during the financial year, determined by the recognition of greater net deferred tax liabilities for €47.9 million and greater current taxes for €81.3 million.
The following table reports changes in taxes with respect to 2010:

| € million | 2011 | 2010 | Change |
|---|---|---|---|
| **Income taxes of the year** | | | |
| Current taxes: | | | |
| - IRES | 308.6 | 219.0 | 89.6 |
| - IRAP | 61.9 | 55.3 | 6.6 |
| ***Total current taxes*** | ***370.5*** | ***274.3*** | ***96.2*** |
| New temporary differences: | | | |
| - deferred tax assets | (55.3) | (12.2) | (43.1) |
| - deferred tax liabilities | 0.0 | 0.0 | 0.0 |
| Reversal of temporary differences: | | | |
| - deferred tax assets | 17.8 | 11.1 | 6.7 |
| - deferred tax liabilities | (48.2) | (36.1) | (12.1) |
| Adjustment – restatement of additional IRES tax (pursuant to Italian Law Decree no. 138 of 13.08.2011 - Robin Hood Tax) | 57.8 | 0.0 | 57.8 |
| Adjustment – restatement of additional IRAP (pursuant to paragraph 5 of Art. 23 of Italian Law Decree no. 98 of 06.07.2011) | 2.7 | 0.0 | 2.7 |
| ***Total change in deferred tax assets and liabilities*** | ***(25.2)*** | ***(37.2)*** | ***12.0*** |
| Adjustment of prior-year taxes | (1.1) | (5.0) | 3.9 |
| **Total** | **344.2** | **232.1** | **112.1** |

### Current taxes

Current taxes include an increase of €96.2 million with respect to the balance of the previous financial year, due, as described above, to the increase in the IRES rate, from 27.5% to 38% as a result of the above manoeuvre (€81.3 million) and to the adjustment of the IRAP rate relating to the effects of the economic manoeuvre for concession holders (pursuant to Art. 23, paragraph 5 of Italian Law Decree no. 98 of 6 July 2011), which determined greater current taxes for €3.9 million. The item also reflects the value of substitute tax paid during the financial year (€16.3 million) for the release of goodwill, recognised on the consolidated financial statements of the Company with the 2009 acquisition of the subsidiary Terna Rete Italia (pursuant to Italian Law Decree no. 98 of 6 July 2011).

### Deferred tax assets and liabilities

Deferred tax assets and liabilities, totalling a negative €25.2 million, showed a change amounting to €12.0 million with respect to 2010. The change is mainly attributable to:

- application of greater tax rates that has, in fact, entailed the overall recalculation of deferred tax liabilities of the start of the financial year (€60.5 million, equal to €57.8 million as a result of the Robin Hood Tax and €2.7 million for additional IRAP);
- recognition of deferred tax assets (€39.8 million) for the release of the goodwill recorded on the consolidated financial statements of the Company following the acquisition of the company Terna Rete Italia;
- release of the share attributable to the year (€3.8 million) of the advances allocated for the release of the goodwill recorded on the financial statements following the merger of RTL (pursuant to Italian Legislative Decree no. 185/2008);
- the greater use of previous provisions to cover the difference between additional depreciation and amortisation calculated using ordinary technical rates (€10.6 million), including the reversal in respect of the amortisation/depreciation charge for the year attributable to the difference from merger eliminations allocated to property, plant and equipment following mergers carried out in previous years (€1.1 million).

### Adjustment of prior-year taxes

Adjustment of prior-year taxes, amounting to a negative €1.1 million, referring to greater current taxes paid in previous years, record a change for €3.9 million with respect to the previous year's figure (amounting to a negative €5.0 million).

The effective rate of income tax (which totalled €344.2 million) on profit before taxes came to 45.1% (amounting to 45.2%, without taking into account adjustments from previous years), with respect to 35% in 2010 (amounting to 35.8%, without taking into account adjustments from previous years).
The greater taxes recognised for the adjustment of the balance at the start of the financial year of the deferred tax liabilities have affected profit before taxes by 7.9 percentage points; the tax rate for the financial year, without considering this adjustment, of the corrections made in relation to previous years and net of the comprehensive tax effect of the release of goodwill relating to Terna Rete Italia stands at 40.4%, up 4.6% with respect to the figure of the previous financial year, basically as a result of the greater tax rates described above (9.3% for the "Robin Hood Tax" and 0.4% for additional IRAP, net of the tax effects deriving from the dividends distributed by the subsidiary SunTergrid (a negative 4.7%).
For a clearer presentation of the differences between the theoretical and actual tax rates, the table below reconciles the theoretical tax rate with the effective tax rate for the year:

| € million | Taxable income | Tax | % Change |
|---|---|---|---|
| Profit before taxes | 764 | | |
| IRES - theoretical tax charge (38%) | | 290.3 | |
| IRAP - theoretical tax charge (4.74% on operating profit of €772.8 million) | | 36.6 | |
| **Total** | | **326.9** | |
| **Theoretical tax rate** | | | **42.8%** |
| **Permanent IRES differences** | | | |
| Employee benefits | | 1.8 | 0.2% |
| Contingencies and non-deductible taxes | | 1.3 | 0.2% |
| Other increases/decreases | | 2.7 | 0.3% |
| IRAP - Art. 6 Law 28 January 2009 | | (2.4) | (0.3%) |
| Release of goodwill recognised on the consolidated financial statements (pursuant to Italian Law Decree no. 98 of 6 July 2011) | | (20.7) | (2.7%) |
| Dividends | | (36.1) | (4.7%) |
| Restatement pursuant to Italian Law Decree no. 138 of 13 August 2011 (Robin Hood Tax) | | 57.8 | 7.5% |
| **Permanent IRAP differences** | | | |
| Personnel expense | | 12.7 | 1.7% |
| Capitalised borrowing costs | | 1.2 | 0.2% |
| Other increases/decreases | | 0.2 | 0.0% |
| Release of goodwill recognised on the consolidated financial statements (pursuant to Italian Law Decree no. 98 of 6 July 2011) | | (2.8) | (0.4%) |
| Restatement for adjustment of IRAP (pursuant to paragraph 5 of Art. 23 of Italian Law Decree no. 98 of 6 July 2011) | | 2.7 | 0.4% |
| **Actual tax rate net of adjustments to income taxes of previous years** | | | **45.2%** |
| Prior year taxes | | (1.1) | (0.1%) |
| **Total taxes for the year** | | **344.2** | |
| **Actual tax rate** | | | **45.1%** |


6
8
MANOMETRO
10
12
14
15
kg/cm²

## 10. Net profit for the year from discontinued operations and assets held for sale - €33.8 million

In accordance with the provisions of accounting standard IFRS 5 – Non-current assets held for sale and discontinued operations, the item, amounting to €33.8 million, includes the partial release of the provision set aside in 2009 relating to the contractual obligations that have matured during the financial year, deriving from the sale of the majority share package in Terna Participações.
For comparative reasons, the item (€1.4 million) instead included the reclassification of the financial operating result of the company Rete Rinnovabile S.r.l. (€1.3 million) following the agreement signed in October 2010 for the transfer of 100% of the share capital of this company (as largely described in the 2010 annual financial report).

# D. Notes to the statement of financial position

## Assets

## 11. Property, plant and equipment - €7,514.0 million

Property, plant and equipment amount to €7,514.0 million (€6,687.7 million at 31 December 2010). The amount and changes for each category are reported in the following table:

| € million | Land | Buildings | Plant and machinery | Industrial and commercial equipment | Other assets | Assets under construction and payments on account | Total |
|---|---|---|---|---|---|---|---|
| **Cost at 01.01.2011** | **81.7** | **957.7** | **9,402.6** | **62.7** | **93.1** | **882.4** | **11,480.2** |
| Investments | 0.2 | 16.9 | 11.1 | 3.3 | 18.4 | 1,072.8 | 1,122.7 |
| Entry into use | 11.5 | 139.2 | 668.7 | 1.8 | 5.0 | (826.2) | 0.0 |
| Intra-group purchases | | | 22.2 | | | 5.1 | 27.3 |
| Infra-group sales | | (0.6) | (1.0) | | | | (1.6) |
| Disposals and impairment | | (0.6) | (39.7) | (0.3) | (10.8) | (1.9) | (53.3) |
| Other changes (grants) | | | (8.6) | | | (3.2) | (11.8) |
| Reclassifications | 0.1 | (0.1) | 0.0 | (0.4) | 0.4 | | 0.0 |
| **Cost at 31.12.2011** | **93.5** | **1,112.5** | **10,055.3** | **67.1** | **106.1** | **1,129.0** | **12,563.5** |
| **Accumulated depreciation and impairment at 01.01.2011** | | **(286.2)** | **(4,409.5)** | **(41.4)** | **(55.4)** | | **(4,792.5)** |
| Depreciation charge for the year | | (25.0) | (258.4) | (3.6) | (12.1) | | (299.1) |
| Intra-group purchases | | | (7.7) | | | | (7.7) |
| Infra-group sales | | | | | | | 0.0 |
| Disposals and impairment | | 0.6 | 38.9 | 0.2 | 10.1 | | 49.8 |
| Reclassifications | | | | | | | 0.0 |
| **Accumulated depreciation and impairment at 31.12.2011** | | **(310.6)** | **(4,636.7)** | **(44.8)** | **(57.4)** | | **(5,049.5)** |
| **Carrying amount** | | | | | | | |
| **At 31.12.2011** | **93.5** | **801.9** | **5,418.6** | **22.3** | **48.7** | **1,129.0** | **7,514.0** |
| **At 31.12.2010** | **81.7** | **671.5** | **4,993.1** | **21.3** | **37.7** | **882.4** | **6,687.7** |

The category "Plant and machinery" includes the energy transportation network as well as the transformation stations. The item shows an increase on the previous financial year amounting to €826.3 million, as a result of ordinary transactions made during the financial year, relating to:

- investments for the financial year (€1,122.7 million, of which €25.9 million for capitalised financial expense);
- depreciation for the year (a negative €299.1 million);
- divestments (a negative €3.5 million) and contributions directly reducing the value of the operating plants and plants under construction (a negative 11.8 million);
- infra-group transactions: acquisition of the transmission plants from the subsidiary Terna Rete Italia (€19.6 million) in order to carry out a series of urgent works for the development and renewal of the NTG in the Territorial Operative Areas of Milan, Padua, Florence and Naples and sale to the subsidiary SunTergrid (€1.6 million) of the MV/HV electrical substation for the connection of the photovoltaic plant of Lanuvio.

A summary of changes in property, plant and equipment during the year is provided in the table below:

€ million

| | |
|---|---|
| Investments | |
| - Transmission lines | 431.8 |
| - Transformation stations | 569.4 |
| - Other | 121.5 |
| **Total investments** | **1,122.7** |
| Depreciation | (299.1) |
| Disposals, impairment losses and other changes | (15.3) |
| Intra-group transactions | 18.0 |
| **Total** | **826.3** |

With reference to investments made during the financial year (€1,122.7 million), please note, in particular, the progress of works in relation to Sorgente-Rizziconi (€117.5 million), with the development of civil works of the stations of Scilla (Calabria) and Sorgente (Sicily) and the laying of the first out of six submarine cables between Villafranca and Favazzina for the development of the 380 kV double three-phase long-distance power line connection, the conclusion of preliminary works for the development of the tunnel in Favazzina and the development of the 380 kV long-distance power lines (overhead part) on the Calabria side; development of two new 380 kV power stations in the municipalities of Chignolo Po and Maleo and the new double three-phase power line between the stations along the "La Casella-Caorso" line (€69.0 million); the purchase of the armouring in the station of Piossasco with a view to developing the HVDC interconnection Italy-France (€39.7 million); works on 380 kV stations suited to reducing congestion and connection to new renewable fuel generating plants located in the areas of Maida, Bisaccia, Deliceto, Troia, South Brindisi, Castellaneta, Tuscania and Rotello; the installation of a PST (System Phase Shifter) in the Foggia power station (€27.7 million); progress of works for the development of the Avellino North station aimed at connecting Montecorvino-Benevento (€25.1 million); completion of the civil works and start of electromechanical assemblies in the Aliano station for the restructuring of the North Calabria grid (€21.6 million); development of foundations prior to starting assembly of the supports to the Trino-Lacchiarella power line (€17.9 million).

In terms of assets under construction at the end of the year, the main grid development and re-powering projects worth more than €5 million are listed below.

| Transmission lines | € |
|---|---|
| Sorgente-Rizziconi 380 kV Power Line | 83,346,291 |
| Rationalis. 380 kV In the Province of Lodi | 42,791,833 |
| Valcamonica (Phase A1) | 23,415,387 |
| Trino-Lacchiarella 380 kV Power Line | 17,767,292 |
| SA.PE.I. | 17,284,706 |
| Restructuring of the 220 kV Line in Naples | 14,960,900 |
| Restructuring of Metropolitan Area Of Rome | 10,473,773 |
| Paternò-Pantano-Priolo | 10,398,598 |
| Pot.150 kV Collect. Wind Pwr Prod. Campania | 7,798,939 |
| Alta Valtellina (Phase A2) | 7,712,546 |
| Restructuring Of Carpi Fossoli (Mo) Grid | 7,603,343 |
| **Transformation stations** | |
| Piossasco 380/220/132 kV station | 36,928,055 |
| Foggia 380 kV station | 27,712,675 |
| Avellino North 380 kV station | 17,119,347 |
| Maleo 380 kV station | 16,691,204 |
| Camporosso 220 kV station | 15,201,380 |
| Aliano 380 kV station | 14,408,214 |
| Rotello 380/150 kV station | 13,753,293 |
| Castellaneta 380/150 kV station | 12,378,073 |
| Villanova station | 11,828,989 |
| Chignolo Po 380 kV station | 9,510,754 |
| Troia 380/150 kV station | 9,172,910 |
| Scilla 380/150 kV station | 8,945,146 |
| Tuscania 380 kV station | 8,852,128 |
| Villafranca 380/150 kV station | 8,743,511 |
| Turin North 220 kV station | 7,962,087 |
| Sorgente 380/150 kV station | 6,811,194 |
| Sorgente 380/150 kV station | 6,768,097 |
| Meduno station | 6,660,380 |
| Cardano station | 6,369,747 |
| Fiumesanto station | 6,067,783 |
| Marianopoli 150 kV station | 6,016,355 |

## 12. Goodwill - €88.6 million

Goodwill amounted to €88.6 million and it is unchanged as compared to the balance of the previous year.

### Impairment testing

#### Cash Generating Unit - Terna

The recoverable amount of the goodwill arising from the acquisition of RTL (merged into Terna in 2008), recognised in the consolidated accounts in the amount of €88.6 million was estimated on the basis of the value of use criteria applying the unlevered version of the discounted cash flow method to Terna Cash Generating Unit.
The forecast of cash flows was prepared over the time frame 2012-2021; in particular cash flows were determined, up to 2016, on the basis of the business plan; while for subsequent years the cash flow projection was made assuming business development operations in line with the last year of the business plan and, for investment only, considering the information of the ten-year NTG development plan. The business plan has been developed considering the latest estimates of the electricity sector and the latest macroeconomic forecasting in addition to the news introduced by the latest review of the tariffs (IV regulatory period) and by Italian Law Decree no. 138/11 (introduction of the Robin Hood Tax with additional IRES of +10.5% in 2011-2013 and +6.5% from 2014).
The final value was assumed to be equal to the RAB (Regulatory Asset Base) at the end of 2021 and the adopted discount rate was equal to 4.85%. The value in use of the CGU determined as indicated above was €3,263 million higher than the carrying amount. The excess value in use of the CGU comes to zero, if WACC increases up to 9.04%.

## 13. Intangible assets - €274.0 million

Changes during the year in intangible assets are detailed below:

| € million | Infrastructure rights | Concessions | Other assets | Assets under development and payments on account | Total |
|---|---|---|---|---|---|
| **Balance at 31.12.2010** | **106.4** | **106.5** | **32.0** | **29.1** | **274.0** |
| Investments | | | 0.2 | 49.5 | 49.7 |
| Entry into use | 36.5 | | 15.1 | (51.6) | 0.0 |
| Depreciation | (25.1) | (5.6) | (19.0) | | (49.7) |
| Other changes (grants) | | | | | 0.0 |
| Reclassifications | | | | | 0.0 |
| **Balance at 31.12.2011** | **117.8** | **100.9** | **28.3** | **27.0** | **274.0** |
| Cost | 276.1 | 135.4 | 119.9 | 27.0 | 558.4 |
| Accumulated amortisation | (158.3) | (34.5) | (91.6) | | (284.4) |
| **Balance at 31.12.2011** | **117.8** | **100.9** | **28.3** | **27.0** | **274.0** |

Intangible fixed assets amount to €274.0 million and in particular, include:

- the infrastructure used for the dispatching service, recognised as of 1 January 2010 in accordance with IFRIC 12 (discussed in more detail in section "A. Accounting policies and measurement criteria"), with a net carrying amount at 31 December 2011 of €117.8 million for infrastructure already in use and €23.1 million for the infrastructure under construction classified under "Assets under construction and payments on account" caption, and a net carrying amount at 31 December 2010, of €106.4 million for infrastructure already in use and €25.1 million for the infrastructure under construction classified in the "Assets under construction and payments on account" caption;
- the licensing for the provision of electricity transmission and dispatching services in Italy (with net carrying amount of €100.9 million at 31 December 2011), recognised initially during 2005 at fair value and subsequently measured at cost.

Other intangible assets comprise application software developed internally or purchased when implementing systems development projects. Related investments (€15.3 million) are made essentially through internal development.
The item does not reflect any difference with respect to 2010, due to the combined effect of ordinary changes during the financial year, mainly referring to investments (€49.7 million, including €34.4 million in infrastructure rights) – mainly in application software – and amortisation (€49.7 million, of which €25.1 million in relation to dispatching infrastructure).
Among the investments for the year note in particolar those related to the development and evolution of application software, the remote management system for dispatching (€13.0 million), for the Power Exchange (€11.0 million) and for the protection of the electrical system (€0.8 million), as well as software applications and licenses (€14.3 million).

## 14. Financial assets

The following table details financial assets recognised by Terna S.p.A.:

| € million | Carrying amount 31.12.2011 | Carrying amount 31.12.2010 | Change |
|---|---|---|---|
| Investments in subsidiaries | 570.4 | 568.4 | 2.0 |
| Investments in associates | 51.8 | 14.9 | 36.9 |
| Other investments | 0.6 | 0.5 | 0.1 |
| Loan to Terna Rete Italia | 500.0 | 500.0 | 0.0 |
| FVH derivatives | 521.8 | 200.3 | 321.5 |
| **Non-current financial assets** | **1,644.6** | **1,284.1** | **360.5** |
| Other current financial assets | 158.2 | 2.9 | 155.3 |
| **Current financial assets** | **158.2** | **2.9** | **155.3** |

"Non-current financial assets", equal to €1,644.6 million, reported the value at 31 December 2011 of equity investments, the intercompany loan to Terna Rete Italia S.r.l. and the fair value of financial derivatives.

"Investments in subsidiaries" (€570.4 million) refer to investments in subsidiaries held directly by Terna S.p.A. and summarised below. The increase of €2 million derives from:

- incorporation on 22 June 2011 of the company Terna Crna Gora d.o.o., a limited liability company incorporated under the laws of Montenegro, with a share capital amounting to €2 million; the company's task is to carry out the activities relating to the authorisation, construction and management of transmission infrastructures comprising the Italy-Montenegro electrical interconnection in Montenegro territory;
- incorporation on 15 December 2011 of Terna Plus S.r.l. (hereinafter "Terna Plus"), with share capital of €50,000; the company object of Terna Plus is the design, construction, management, development, operation and maintenance of plants, equipment and infrastructures also on the grid and systems, including the diffused accumulation of energy and pumping and/or storage.

"Investments in associates" (€51.8 million) refers to:

- the interest held of 42.406% share in the share capital of CESI S.p.A. (amounting to €17.3 million), which recognises an increase on 2010 for €2.7 million, following the acquisition during the financial year of further equity shares from Tirreno Power S.p.A. for 1.5% and from SO.GI.N. - Società di Gestione Impianti Nucleari S.p.A. for 1% of the share capital;
- the interest held of 22.485% in the share capital of CORESO S.A. (€0.3 million) acquired in November 2010;
- the value of the equity interest in the associate CGES - CrnoGorski Elektroprenosni Sistem AD (€34.2 million), which was acquired in January 2011, representing a equity investment of 22.0889%.

CESI S.p.A. operates in the construction and management of laboratories and plants for tests, inspections, studies and experimental research relating to the electro-technical field in general and to the technical and scientific developments in that area.
The company CORESO S.A. is the first technical centre owned by various electrical energy transmission companies which implements joint TSO technical coordination activities in order to improve and strengthen security and coordination of the electrical system in central/western Europe; it prepares daily forecasts and analyses in real time of energy flows in the region, identifying potentially critical areas and promptly notifying the TSOs which are affected. For more information, please see the section "Significant events".
CGES is the electricity dispatch and transmission operator in Montenegro. The financial investment of Terna in CGES, which was made following an industrial cooperation and country system and included as part of inter-governmental understandings reached by Italy and Montenegro, sanctions the institutional commitment to the development of a new submarine electrical interconnection and the implementation of the partnership between national transmission operators.

"Other investments" (€0.6 million) refers to:

- the interest held of 5.6% in the share capital of Desertec Industrial Initiative ("DII") (€0.1 million) acquired in September 2010;
- the interest held of 8.3% in the share capital of CASC CWE S.A. (€0.3 million) acquired in November 2010;
- the 5% interest held in the share capital of Medgrid SAS (€0.2 million, which has increased by €0.1 million following the subscription of the capital increase of the subsidiary).

The following table summarises Terna S.p.A.'s direct investments in subsidiaries and associates at 31 December 2011, with data related to the last approved financial statements:

| Company | Registered office | Assets | Share/quota capital | Currency | % held | Carrying amount |
|---|---|---|---|---|---|---|
| SUBSIDIARIES | | | | | | |
| **Terna Rete Italia S.r.l.** | Rome | Design, construction, management, development, operation and maintenance of high-voltage power lines. | 243,577,554 | € | 100% | 557,666,437 |
| **SunTergrid S.p.A.** | Rome | Construction and maintenance of electricity transmission grids and plants for the generation of electricity, including renewables generation, for own use and sale in Italy and abroad. | 120,000 | € | 100% | 10,672,709 |
| **Terna Crna Gora d.o.o.** | Podgorica (Montenegro) | Activities relating to the authorisation, construction and management of transmission infrastructures comprising the Italy-Montenegro electrical interconnection in Montenegro territory. | 2,000,000 | € | 100% | 2,000,000 |
| **Terna Plus S.r.l.** | Rome | Design, construction, management, development, operation and maintenance of plants, equipment and infrastructures including grids and systems, including diffused energy accumulation, pumping and/or storage systems. | 50,000 | € | 100% | 50,000 |
| ASSOCIATES | | | | | | |
| **CESI S.p.A.** | Milan | Experimental electro-technical research. | 8,550,000 | € | 42.406% | 17,268,241 |
| **CGES AD** | Podgorica (Montenegro) | Electricity dispatch and transmission activities in Montenegro. | 155,108,283 | € | 22.0889% | 34,285,811 |
| **CORESO S.A.** | Brussels (Belgium) | Technical centre owned by various electrical energy transmission companies which implements joint TSO technical coordination activities in order to improve and strengthen security and coordination of the electrical system in central/western Europe. It prepares daily forecasts and analyses in real time on energy flows in the region, identifying potentially critical areas and promptly informing any affected TSOs. | 1,000,000 | € | 22.485% | 281,082 |
| JOINT CONTROL | | | | | | |
| **ELMED Études Sarl** (*) | Tunis (Tunisia) | Analysis and preliminary consulting for the preparation of tender documentation of the Tunisian government for construction tenders and the management of the electricity generation site in Tunisia involved in the project for the interconnection of Italy and Tunisia. | 2,700,000 | Tunisian Dinar | 50% | 0 |

(*) The value of the equity interest was brought to zero in 2010 (€0.7 million) as a result of the impairment of the Terna investment in ELMED Études Sarl, consequent to the altered political situation seen in Tunisia, which currently makes its recovery difficult.

The fair value of the FVH derivatives hedging the Company's bonds, equal to €521.8 million, is calculated by discounting forecast cash flow with the market interest rate curve at the date of reference. The increase in the fair value of derivatives (€321.5 million) as compared with 31 December 2010 is due to the lowering of the rates curve in the long-term part, which has impacted both the fair value of new fair value hedge derivatives subscribed to hedge the bond issued in March 2011 (€140.0 million) and the fair value of derivatives existing as at 31 December 2010 (€181.5 million).

"Current financial assets" of €158.2 million rose from the prior year by €155.3 million; this is mainly due to the subscription of deposit certificates, expiring on 14 June 2013 and for which early repayment may be requested every three months (€150 million), to interest accrued and not yet collected at the reporting date concerning the intercompany credit towards Terna Rete Italia S.r.l., and to short-term liquidity uses and deposit certificates (€5.1 million).

## 15. Other assets

"Other assets" are analysed below:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| Receivables due from others: | | | |
| - loans and advances to employees | 6.1 | 5.9 | 0.2 |
| - deposits with third parties | 0.5 | 0.3 | 0.2 |
| **Other non-current assets** | **6.6** | **6.2** | **0.4** |
| Other tax receivables | 7.9 | 3.9 | 4.0 |
| Receivables due from others: | | | |
| - advances to employees | 0.2 | 0.2 | 0.0 |
| - others | 9.0 | 14.5 | (5.5) |
| **Other current assets** | **17.1** | **18.6** | **(1.5)** |

"Other non-current assets" (€6.6 million) – which are reported in the table above – are essentially unchanged since the end of last year (€6.2 million) and mainly comprise loans and advances paid to employees (€6.1 million).
The item "Other current assets", equal to €17.1 million and whose composition is reported in the previous statement, decreased by €1.5 million compared to 31 December 2010 and is essentially due to the combined effect of:

- lower receivables from others (€5.5 million), mainly regarding:
  - lesser quotas of previously paid costs which accrue in subsequent years (a negative €3.9 million) and which are ascribable to insurance premiums;
  - collection of the receivable due for an insurance repayment, ascertained at the end of financial year 2010 (approximately a negative €1.9 million);
  - the booking of revenue which accrued during the year and which was not yet collected at the reporting date (€1.2 million) and relating to the rentals for the use by Enel Distribuzione of the Company's infrastructures, aiming to ensure power line communication;
- greater tax assets (€4.0 million) mainly for the withholdings and tax receivables from the tax office on interest income accrued on financial assets (€4.5 million), net of the VAT receivable at 31 December 2010 recovered during the financial year (€0.8 million).

## 16. Inventories - €12.4 million

Current inventories (€12.4 million) refer to a balance which has not undergone any significant changes with respect to the previous year (€11.4 million); it relates to materials and devices allocated for operational, maintenance and construction activities of plants.

## 17. Trade receivables - €1,684.0 million

Trade receivables are analysed as follows:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| Energy-related receivables | 1,257.1 | 1,116.2 | 140.9 |
| Grid transmission fees receivables | 356.7 | 304.8 | 51.9 |
| Other trade receivables | 64.4 | 64.2 | 0.2 |
| Receivables from subsidiaries | 5.8 | 10.4 | (4.6) |
| **Trade receivables** | **1,684.0** | **1,495.6** | **188.4** |

Trade receivables amount to €1,684.0 million. The increase (€188.4 million) with respect to the previous year mainly comprises pass-through amounts deriving from the electricity dispatching activities.
Receivables are measured net of impairment losses on items considered non-collectable that are covered by allowances for doubtful accounts (€16.8 million for energy items and €6.7 million), which is basically in line with the previous financial year.

### Energy-related receivables - €1,257.1 million

They mainly include receivables in relation to the "pass-through" energy items arising in respect of dispatching activities. This item also includes receivables for fees payable by market operators for dispatching activities (DIS fee as per AEEG Resolution no. 237/04 and its subsequent amendments and supplements).
The increase in this caption by €140.9 million vis-à-vis the end of last year was mainly due to:

- additional receivables for the accrued incentives associated with the reduction in volumes procured from the Market for Dispatching Services, made available under AEEG Resolution 213/09 (€66.0 million), partially offset by the collection of the receivable connected with the premium recognised on the basis of said incentive accrued in 2009, in accordance with AEEG Resolution 206/08 includes also the receivable related to the quality of the transmission service (€7.7 million);
- increased receivables for the sale of electricity within the Power Exchange (€77.0 million), mainly deriving from the net effect of increased receivables for the uplift component (€131.5 million), from the recognition of receivables booked on the market coupling mechanism for the management of congestion on the inter-connection with Slovenia (€14.3 million), for the greater receivables generated by the increased quantities and prices of the measurement of the imbalance (€32.0 million); partly offset, as described under "Trade payables" by the reduction in the volumes of resources attained from the energy market (€50.7 million), by the reduction in credit items relating to the price to cover the costs of the modulation of wind power production pursuant to Article 44-*bis* of AEEG Resolution 111/06 (€17.5 million), the reduction in receivables relating to the dispatch of electricity produced by non-programmable renewable sources envisaged by Resolution ARG/elt 5/10 (€11.3 million) and lower payables deriving from virtual inter-connection activities (€22.7 million);
- greater receivables for the sale of electricity outside the Power Exchange (€16.5 million), mainly as a result the recognition (€16 million) of the price for the transitory safeguarding service envisaged by Art. 25-*bis*, Resolution ARG/elt 107/09.

### Grid transmission fees receivable - €356.7 million

The grid transmission fees receivable, €356.7 million, reflect the remuneration paid to the Company and other owners for the use of the National Transmission Grid by distributors of electricity. Said receivable recognises a positive change amounting to €51.9 million with respect to the previous financial year, mainly as a net result of the recognition of the receivable due from CCSE for the optional adhesion to the "mitigation" mechanism established by Resolution ARG/elt 188/08 to cover the risk connected with a drop in consumption (€71.1 million) and by the receivable recognised to the Company for the grid transmission fee adjustment in previous years; partially offset (a negative €16.8 million) by the collection of the receivable due from CCSE for the incentive on the remuneration of investments in strategic transmission infrastructures recognised the previous financial year (Resolution ARG/2011/elt 87/10).

### Other trade receivables – €64.4 million

Other trade receivables mainly regard receivables due from third party clients of the Company for the diversified business; they reported an increase of €0.2 million with respect to the previous year and primarily due to the net effect of:

- increased receivables due from third party customers (€10.4 million) and which are primarily derived from orders underway in relation to stations and connections;
- greater receivables for diversified business mainly relating to rentals and optical fibre housing (€7.2 million);
- lesser receivables (a negative €14.2 million) for invoices to be issued to customers mainly following completion of the sale of photovoltaic panels on the basis of specific contractual agreements, to contracting companies appointed to build photovoltaic plants owned by Group companies sold during the financial year.

This item also includes receivables for contract work in progress (€1.7 million), highlighted in the table below, relative to works of multi-year duration which the Company has been implementing with third party customers and which increased with respect to the previous year by €0.6 million:

| € million | Payments on account | Contract value | Balance at 31.12.2011 | Payments on account | Contract value | Balance at 31.12.2010 |
|---|---|---|---|---|---|---|
| Others | (13.5) | 15.2 | 1.7 | (11.1) | 12.2 | 1.1 |

### Receivables from subsidiaries - €5.8 million

The item amounts to €5.8 million and regards receivables in respect of contracts for the coordination and operational management of the subsidiaries Terna Rete Italia S.r.l. (€5.6 million) and Terna Crna Gora d.o.o. (€0.2 million).

The amount of the guarantees issued to third parties by Terna at 31 December 2011 comes to €42.2 million and refers for €22.2 million to sureties issued to secure the contractual obligations arising under the scope of operations and for €20.0 million relating to a guarantee issued on Terna credit lines but in the interest of the subsidiary SunTergrid S.p.A. for commitments made under the scope of the sale of Nuova Rete Solare S.r.l..

## 18. Cash and cash equivalents - €933.0 million

Cash and cash equivalents at 31 December 2011 amount to €933.0 million of which €765.0 million are liquid funds invested in term deposits, €349.2 million as net liquidity on bank current accounts, €181.3 million to the debt position on the inter-company current account and cash provisions for the territorial operative units for €0.1 million.

## 19. Income tax assets - €4.2 million

Income tax assets amount to €4.2 million and refer exclusively to the receivable due from the tax office, recognised in 2010, in accordance with Art. 6 of Italian Law of 28 January 2009, for the greater income tax paid in previous years, as a result of the failure to deduct IRAP in the amount permitted by the legislation in question.

# Liabilities

## 20. Equity - €2,555.3 million

### Share capital - €442.2 million

The share capital of Terna is represented by 2,009,992,000 ordinary shares, par value €0.22 each. The increase of €1.2 million with respect to the previous year reflects the issue of 5,596,300 new shares, during 2011, in relation to the Stock Option Plan described later in this report.

### Legal reserve - €88.2 million

The legal reserve amounts to 20% of the share capital of the Company at 31 December 2010. The increase of €0.2 million from last year, which restores this ratio of legal reserve and share capital, was resolved by the Shareholders' Meeting on 13 May 2011, as they met to approve the separate financial statements and to allocate the net profit for financial year 2010.

### Other reserves - €678.7 million

Other reserves have decreased by €24.3 million due to:

- "Other comprehensive income" (€34.7 million): adjustment to fair value of derivatives hedging floating-rate loans of the Company (cash flow hedges), of €64.1 million, net of the related tax effect (a negative €29.4 million);
- transactions with shareholders (€10.4 million): increase in the share price premium reserve (€11.4 million) and decrease in the stock option reserve (a negative €1.0 million) to reflect the stock options exercised during the year.

### Retained earnings and losses - €1,053.4 million

The increase of €10.2 million of the item "Retained earnings/Losses carried forward" regarded the allocation of the residual profit for 2010, compared to the distribution of the dividend in the same year (€421.7 million). The opening balance incorporates the change to comparative data at 31 December 2010 (for €14.2 million) as a consequence to the change in the accounting policies relative to the booking of the release which took place in financial year 2009 in compliance with Art. 15 of Italian Legislative Decree no. 185/2008 of goodwill deriving from the incorporation into the Company of RTL.

### Interim dividend 2011

After receiving the report of the independent auditors PricewaterhouseCoopers required by Art. 2433-*bis* of the Italian Civil Code, on 9 November 2011 the Board of Directors approved the distribution of an interim dividend amounting to €160.8 million, equal to €0.08 per share, which is payable on 24 November 2011, with an ex dividend date (coupon 15) of 21 November 2011.
The following table reports the origin, availability and possibility of distribution of the components of equity:

| € million | 31.12.2011 | Possibility of use | Available portion |
|---|---|---|---|
| Share/Quota capital | 442.2 | - | - |
| Legal reserve | 88.2 | B | 88.2 |
| Other reserves | | | |
| - equity-related | 416.1 | A, B, C | 416.1 |
| - income-related (*) | 262.6 | A, B, C | 262.6 |
| Retained earnings | 1,053.4 | A, B, C | 1053.4 |
| Interim dividend | (160.8) | - | - |
| Result of the year | 453.6 | - | - |
| **Total** | **2,555.3** | | **1,820.3** |

Key:
A - for share capital increase
B - for coverage of losses
C - for distribution to shareholders

(*) Includes the negative reserve for the effective portion of changes in the fair value of cash flow hedges, amounting to, net of the tax effect, €70.0 million.

Of the total available portion, €548.6 million refers to untaxed income-related reserves.

### Stock Option Plans

On 21 December 2005, based on proposals presented by the Remuneration Committee, the Company's Board of Directors approved a Stock Option Plan for 2006 applicable to those senior managers of Terna who hold key roles in terms of achieving the Company's strategic objectives.
This plan is aimed at giving Terna – in line with international best practice and that of the leading Italian companies listed on the Stock Exchange – a management incentive and loyalty tool that imbues key employees with a sense of belonging to the corporate team, while ensuring they are constantly focused on creating value, with a view to melding the interests of shareholders and management.
The 2006 Stock Option Plan entailed the granting, on 21 December 2005, of 9,992,000 options with a strike price of €2.072 to 17 managers of the Company. The Board of Directors verified that the conditions to exercise were met when it approved the financial statements of 31 December 2006.
Options in circulation at the start of 2011, amounting to 5,596,300, were all exercised.

The weighted-average prices of the shares at their exercise dates were:
- €3.318 (*) at 21 February 2011;
- €3.292 (*) at 22 February 2011;
- €3.282 (*) at 23 February 2011;
- €3.298 (*) at 24 February 2011;
- €3.323 (*) at 25 February 2011;
- €3.338 (*) at 28 February 2011;
- €3.382 (*) at 27 April 2011.

(*) Source: Bloomberg.

Fair value at the grant date was determined using the Cox-Rubinstein pricing method, which takes account of Terna's stock price at the grant date, the volatility of the security, and the rate curve at the grant date considering the term of the plan. The following pricing parameters were used:

- closing price (underlying or spot price) for the stock on the grant date (source Bloomberg) of €2.058;
- strike price amounting to €2.072;
- rate curve for calculating the discount factors at the grant date (source Reuters);
- historical volatility of the stock identified at the grant date (source Bloomberg) of 14.860%.

## 21. Loans and financial liabilities

The following table details loans and financial liabilities recognised in the separate financial statements of Terna at 31 December 2011:

| | Carrying amount | | |
|---|---|---|---|
| € million | 31.12.2011 | 31.12.2010 | Change |
| Bonds | 4,303.9 | 2,728.2 | 1,575.7 |
| Bank loans | 2,434.8 | 2,419.3 | 15.5 |
| **Long-term loans** | **6,738.7** | **5,147.5** | **1,591.2** |
| CFH derivatives | 111.4 | 47.1 | 64.3 |
| **Non-current financial liabilities** | **111.4** | **47.1** | **64.3** |
| Short-term loans | 0.0 | 73.1 | (73.1) |
| Current portion of long-term loans | 59.7 | 59.7 | 0.0 |
| **Short-term loans and current portion of medium/long-term loans** | **59.7** | **132.8** | **(73.1)** |
| **Total** | **6,909.8** | **5,327.4** | **1,582.4** |

Gross debt for the year increased with respect to the previous year by €1,582.4 million to €6,909.8 million.
The increase in the value in bonds (€1,575.7 million) is due for €1,234.8 million to the new bond issue realised in 2011 net of the costs and issue discounts, for €321.8 million to the change in the fair value of the risk hedged and for €2.0 million to the amortised cost and for €17.1 million to the capitalisation of year inflation.
The change linked to the hedging of the interest rate risk comprises €48.1 million in relation to the inflation-linked bond issue, €91.8 million associated to the bonds 2014-2024, €41.7 million for the private placement and €140.2 million relating to the bond issued in 2011.
The fair value of the bonds is measured by discounting the projected cash flows along a yield curve of interest rate at the reporting date.
The latest official prices for the bonds listed on the Luxembourg Stock Exchange are detailed below:

- bond maturing 2024, 2011 price: 93.85; 2010 price: 104.23;
- bond maturing 2014, 2011 price: 102.42; 2010 price: 105.70;
- bond maturing 2023, 2011 price (*): 82.00; 2010 price: 96.57;
- bond maturing 2019, 2011 price: 96.86; 2010 price: 105.00;
- bond maturing 2021, price at 2011: 92.35

(*) Source: bank; for lack of up-to-date listings source: Reuters and Bloomberg.

The decrease of €57.6 million in the debt originally arranged at a floating rate was mainly due to:

- use on 8 April 2011 of the credit line of €500 million signed with Cassa Depositi e Prestiti (CDP) on 2 February 2009;
- repayment on 8 April 2011 of the syndicate bank loan (revolving credit facility) originally contracted on 13 December 2004 and subsequently renegotiated on 10 April 2006 for a total amount of €750 million;
- obtaining in August of an EIB loan totalling €325 million;
- a €59.7 million reduction in EIB (European Investment Bank) loans and other financing following repayments made on outstanding loans;
- repayment of a short-term loan for €50 million and the availability of credit facilities used during last year for €23.1 million.

## Long-term loans

The following table reports the book values of long-term debt and the repayment plan as of 31 December 2011, broken down by loan type, including amounts falling due within one year and average interest rate at year-end:

| € million | Maturity | 31.12.2010 | 31.12.2011 | Due within one year | Due beyond one year | 2013 | 2014 | 2015 | 2016 | After | Average interest rate as of 31.12.2011 |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Bonds - 10y and 20y | 2014-2024 | 1,518.8 | 1,611.0 | 0.0 | 1,611.0 | 0.0 | 640.5 | 0.0 | 0.0 | 970.5 | 4.62% |
| Bond - Inflation linked | 2023 | 589.7 | 654.8 | 0.0 | 654.8 | 0.0 | 0.0 | 0.0 | 0.0 | 654.8 | 2.75% |
| Bond - Private placement | 2019 | 619.7 | 662.0 | 0.0 | 662.0 | 0.0 | 0.0 | 0.0 | 0.0 | 662.0 | 4.87% |
| Bond - 10y (2011) | 2021 | 0.0 | 1,376.1 | 0.0 | 1,376.1 | 0.0 | 0.0 | 0.0 | 0.0 | 1,376.1 | 4.75% |
| **Total fixed rate** | | **2,728.2** | **4,303.9** | **0.0** | **4,303.9** | **0.0** | **640.5** | **0.0** | **0.0** | **3,663.4** | |
| EIB | 2014-2030 | 1,080.1 | 1,345.4 | 59.7 | 1,285.7 | 69.4 | 79.0 | 76.9 | 84.9 | 975.4 | 1.65% |
| Club Deal | 2015 | 648.9 | 649.1 | 0.0 | 649.1 | 0.0 | 0.0 | 649.1 | 0.0 | 0.0 | 1.89% |
| RCF | 2013 | 750.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | |
| CDP | 2019 | 0.0 | 500.0 | 0.0 | 500.0 | 0.0 | 0.0 | 0.0 | 0.0 | 500.0 | 2.58% |
| **Total floating rate** | | **2,479.0** | **2,494.5** | **59.7** | **2,434.8** | **69.4** | **79.0** | **726.0** | **84.9** | **1,475.4** | |
| **Total** | | **5,207.2** | **6,798.4** | **59.7** | **6,738.7** | **69.4** | **719.5** | **726.0** | **84.9** | **5,138.8** | |

To repay the nominal value of the bonds €600 million will be repaid on 28 October 2014, €600 million on 3 October 2019, €1,250 million on 15 March 2021 and €800 million on 28 October 2024; whilst the inflation-linked bond will be repaid, at maturity on 15 September 2023, with the nominal amount adjusted to reflect inflation.
For all other financial debt items the table above shows the related repayment plan.
The total amount of Terna's borrowings at 31 December 2011 is equal to €6,798.4 million, of which €5,138.8 million is due after more than five years.
The previous table shows the average interest rate for each type of financial liability. Below we also comment on the Group's hedging operations against interest rate fluctuations.
As regards the 2014-2024 bonds, with an average coupon of 4.62%, if fair value hedging operations are taken into account, the average interest rate is equal to 1.95%.
For the inflation-linked bonds – and taking hedges into account – and assuming a 3.22% inflation rate, the average interest rate paid in the year was 3.04%.
The fixed-rate private placement was synthetically transformed to a floating rate security by means of derivative contracts with the same maturity. Consequently, the average interest rate paid in the year was 2.69%.
The average coupon of the 2021 bond is 4.75%; if we consider FVH operations, the average interest rate amounts to 2.70%.
With regard to floating rate loans covered by fluctuations in interest rates – and taking into account the effect of derivative financial instruments booked as cash flow hedges – an average rate of 3.81% is reported for EIB financing while for the Club Deal financing totalling €650 million the average rate was 4.75% and for the CDP financing the average rate was 3.98%.

The following table reports changes in long-term debt for the year:

| Type of loan<br>€ million | Nominal at debt 31.12.2010 | Carrying amount at 31.12.2010 | Repayment and capitalisation | New issues | Delta fair value 31.12.2010 31.12.2011 | Change in carrying amount | Nominal debt at 31.12.2011 | Carrying amount at 31.12.2011 |
|---|---|---|---|---|---|---|---|---|
| Fixed-rate 10y and 20y bonds (2004) | 1,400.0 | 1,518.8 | 0.0 | 0.0 | 92.2 | 92.2 | 1,400.0 | 1,611.0 |
| Listed IL bond | 529.8 | 589.7 | 17.1 | 0.0 | 48.1 | 65.2 | 546.9 | 654.8 |
| Private placement | 600.0 | 619.7 | 0.0 | 0.0 | 42.2 | 42.2 | 600.0 | 662.0 |
| Fixed rate 10y bond (2011) | - | - | 0.0 | 1,234.8 | 141.3 | 1,376.1 | 1,250.0 | 1,376.1 |
| **Total bonds** | **2,529.8** | **2,728.2** | **17.1** | **1,234.8** | **323.8** | **1,575.7** | **3,796.9** | **4,303.9** |
| Bank loans | 2,480.1 | 2,479.0 | (809.7) | 825.0 | 0.2 | 15.5 | 2,495.4 | 2,494.5 |
| **Total bank loans** | **2,480.1** | **2,479.0** | **(809.7)** | **825.0** | **0.2** | **15.5** | **2,495.4** | **2,494.5** |
| **Total financial debt** | **5,009.9** | **5,207.2** | **(792.7)** | **2,059.8** | **324.0** | **1,591.2** | **6,292.3** | **6,798.4** |

As compared with 31 December 2010, long-term debt shows an overall increase of €1,591.2 million, due for €1,234.8 million to the issue of a new bond maturing in 2021, €500.0 million to the disbursement of the CDP loan maturing in 2019, €325.0 million to the disbursement of the EIB loan maturing in 2030, €17.1 million to the capitalisation of year inflation linked to the IL bond, for €323.8 million to the increase in the fair value of bonds, also considering the amortised cost, €750.0 million to the repayment of the revolving credit facility and for €59.7 million to the repayment in instalments on the EIB loans.
At 31 December 2011, Terna had unused credit lines exceeding €1,203.8 million, of which more than €703.8 million in short-term credit lines and €500.0 million in a medium-term credit line.

### Non-current financial liabilities

The table below reports the amount and changes in non-current financial liabilities with respect to value at the end of 2010:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| CFH derivatives | 111.4 | 47.1 | 64.3 |
| **Total** | **111.4** | **47.1** | **64.3** |

“Non-current financial liabilities” includes the fair value of cash flow hedges.
Fair value was measured by discounting the expected cash flows using the market yield curve at the reporting date. The change in the interest rate curve since 31 December 2010 resulted in a change amounting to €64.3 million.

### Current financial liabilities

Current financial liabilities, due to the net interest expense accrued on financial instruments but not yet settled, have increased by €15.9 million since the end of last year.
The following table details deferred liabilities on the basis of the financial liabilities to which they relate:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| **Deferred liabilities on:** | | | |
| Derivatives | | | |
| *- hedging* | *(43.2)* | *(6.5)* | *(36.7)* |
| Bond | | | |
| *- IL* | *4.4* | *4.3* | *0.1* |
| *- private placement* | *7.2* | *7.2* | *0.0* |
| *- ten-year* | *4.5* | *4.5* | *0.0* |
| *- twenty-year* | *7.0* | *7.0* | *0.0* |
| *- ten-year (2011)* | *47.4* | *0.0* | *47.4* |
| **Total** | **70.5** | **23.0** | **47.5** |
| Loans | 12.8 | 7.7 | 5.1 |
| **Total** | **40.1** | **24.2** | **15.9** |

### Net financial position

Pursuant to CONSOB Communication of 28 July 2006 and in compliance with Recommendation ESMA/2011/81 of 23 March 2011, the net financial position of the Company is as follows:

| | Carrying amount |
|---|---|
| € million | 31.12.2011 |
| A. Cash and current a/c position of intercompany treasury | 168.0 |
| B. Term deposits | 765.0 |
| C. Deposit certificates | 150.0 |
| D. Inter-company loan to Terna Rete Italia | 500.0 |
| **E. Cash and cash equivalents (A) + (B) + (C) + (D)** | **1,583.0** |
| F. Current portion of long-term payables | 59.7 |
| **G. Current financial debt (F)** | **59.7** |
| **H. Net current financial debt (G) - (E)** | **(1,523.3)** |
| I. Non-current bank debt | 2,434.8 |
| L. Bonds issued | 4,303.9 |
| M. Derivative financial instruments in portfolio | (410.4) |
| **N. Net non-current financial debt (I) + (L) + (M)** | **6,328.3** |
| **O. Net financial debt (H) + (N)** | **4,805.0** |

The debt/equity ratio of Terna stood at 1.88 in 2011.
For more details on the composition of the items in this table, please see Notes 14 and 18, as well as the information presented here in Note 22.

## Default risk and covenants on the debt

This risk is associated with the possibility that the loan contracts or bond rules to which the Parent Company is a party may contain provisions authorising counterparties to call in such loans immediately upon the occurrence of certain events, thereby generating liquidity risk.

Certain long-term loans obtained by Terna S.p.A. contain covenants that are typical of international practice. The principal covenants relate to:

1. the Company's bonds, comprising two issues of €600 million and €800 million in 2004, and three issues under the €4 billion (€4,000,000,000 Medium-Term Notes Programme), one of €500 million in 2007 and one in the form of a Private Placement, of €600 million in 2009 in addition to an issue of €1,250 million in March 2011;
2. bank payable, consisting of a revolving line of credit of €500, a "Club Deal" syndicated loan of €650 million, and a loan from Cassa Depositi e Prestiti (CDP) of €500 million that draws on EIB funds;
3. loans to the Company from the European Investment Bank (EIB) totalling €1,623 million.

The principal covenants relating to the issue of bonds and the €4 billion EMTN programme are summarised below:

- "negative pledge" clauses, under which the issuer or significant subsidiaries (consolidated companies whose total assets represent at least 10% of total statutory assets and, solely for the EMTN programme, whose registered offices are in an OECD country) may not establish or maintain mortgages, liens or other encumbrances on all or part of its assets in order to secure listed bonds, unless these guarantees are extended on the same basis to the bonds concerned. A number of exceptions apply (guarantees required by law, guarantees in place prior to the date of the loan, guarantees on new assets that only secure the payable arranged to acquire them etc.), in relation to which the Company is not bound by the above pledges;
- "pari passu" clauses under which the securities constitute a direct, unconditional and unsecured obligation of the issuer and are issued without preferential rights among them and have at least the same seniority as other present and future unsecured and unsubordinated borrowing of the issuer;
- "event of default" clauses, under which certain events (e.g. failure to pay, initiation of liquidation proceedings of the issuer, breach of contractual obligations etc.) are considered to represent potential default; in addition, under the "cross default" clauses, the occurrence of a default event in respect of any financial debt (above a threshold level) issued by the issuer also constitutes a default in respect of the loan concerned, which becomes immediately repayable;
- periodic or occasional reporting requirements on the occurrence of specified events.

The principal covenants for the revolving line of credit, the "Club Deal" syndicated loan and the €500 million loan from CDP are summarised below:

- "negative pledge" clauses, under which the Company and each significant subsidiary (consolidated companies whose total assets represent at least 10% of total statutory assets) agree not to establish new guarantees securing any type of financial debt, with the exception of permitted guarantees (guarantees required by law, guarantees in place prior to the date of the loan, guarantees on new assets that only secure the payable arranged to acquire them, guarantees given to governmental or international entities, including the EIB, guarantees on borrowing whose amount does not exceed 10% of total assets etc.);
- "pari passu" clauses under which the payment undertakings of the borrower in respect of loans are not subordinate to any obligation in respect of other unsecured and unsubordinated creditors, except in the case of statutory preferential rights;
- "event of default" clauses linked to the occurrence of specified events (such as, for example, failure to pay, false declarations, insolvency, termination of activities, seriously prejudicial events, breach of contractual obligations, including the equality of the conditions applied by lenders etc.) are considered to represent potential default; in addition, under the "cross default" clauses, the occurrence of a default event in respect of any financial debt (above a threshold level) also constitutes a default in respect of the loan concerned, which becomes immediately repayable;
- periodic or occasional reporting requirements on the occurrence of specified events;
- compulsory early redemption clauses under which the Company is required to repay the loan early if its long-term credit rating is reduced below investment grade (BBB-) by a majority of the rating agencies that monitor the Company, if the Company ceases to be monitored by one or more rating agencies.

The principal covenants governing the EIB loans are summarised below:

- "negative pledge" clauses, under which if the Company establishes, agrees, provides or decides to maintain restrictions in favour, whether directly or indirectly, of third parties (such as unsecured or secured guarantees, liens, encumbrances, charges or other rights), it must also extend equivalent guarantees to the Bank, upon simple request from the latter, except in the case of restrictions granted in relation to borrowing below a threshold level;
- clauses relative to the granting to the Bank of new guarantees in the event of a reduction in the rating according to which if the credit rating of the medium and long-term debt that is not subordinate and not guaranteed should be declassified (and consequently the rating is less than: A- by Standard & Poor's; or A3 by Moody's; or A- by Fitch), the Bank is entitled to require the Company to provide it with additional guarantees that are considered satisfactory at the sole discretion of the Bank, exercised on a reasonable basis;
- "pari passu" clauses, under which for the entire period of the loans the Company will ensure that the payment obligations have the same seniority as those relating to all other unsecured and unsubordinated creditors;
- periodic or occasional reporting requirements on the occurrence of specified events concerning both the projects being financed and the Company itself;

- clauses regarding early repayment/application of the acceleration clause/withdrawal/termination of the contract on which basis, where certain events occur (such as, for example, failure to pay, serious inaccuracies in documentation presented, insolvency, events resulting in negative consequences on the financial commitments made by the company, special administration, liquidation, etc.), the loan in question becomes immediately due; additionally, where the Company is required upon default to discharge in advance any other financial obligation deriving from loans, credit facilities, bank advances, discounting, the issue or subscription of any form of bond or security, such default shall also constitute default on the loan in question, triggering immediate repayment.

## 22. Employee benefits - €119.2 million

Terna provides benefits to its employees during their period of employment (loyalty bonus), at the termination of their employment (termination benefits, additional month's pay and indemnity for lack of notice), and in the period after the termination of employment (electricity discount and the ASEM health plan).
The loyalty bonus is awarded to employees and managers of the Company when they reach certain seniority levels (25 and 35 years of service).
The benefits granted at the termination of employment are recognised for all employees (termination benefits), managers hired or appointed before 28 February 1999 (indemnity for lack of notice), and employees (production workers, office staff and junior managers) hired before 24 July 2001 (additional month's pay indemnity).
Post-employment benefits consist of the following:

- discount on electrical energy consumed for domestic use. This benefit is offered to all employees hired before 30 June 1996 (electricity discount);
- a healthcare plan complementing the national health service, as agreed under the terms of the national contract for industrial managers (the ASEM health plan).

The composition of termination benefits and other employee-related provisions at 31 December 2011 is detailed below along with changes in the period:

| € million | 31.12.2010 | Provision | Interest cost | Utilisations and other changes | 31.12.2011 |
|---|---|---|---|---|---|
| **Benefits payable to employees** | | | | | |
| Loyalty bonus | 4.2 | 0.0 | 0.2 | (0.6) | 3.8 |
| **Total** | **4.2** | **0.0** | **0.2** | **(0.6)** | **3.8** |
| **Benefits payable upon termination of employment** | | | | | |
| Termination benefits | 67.9 | 0.0 | 2.4 | (5.9) | 64.4 |
| Additional months' pay | 6.7 | 0.4 | 0.4 | (1.0) | 6.5 |
| Indemnities for lack of notice and similar | 3.0 | 0.0 | 0.0 | (0.3) | 2.7 |
| **Total** | **77.6** | **0.4** | **2.8** | **(7.2)** | **73.6** |
| **Post-employment benefits** | | | | | |
| Energy discount | 29.3 | 0.8 | 1.3 | (0.5) | 30.9 |
| ASEM | 11.2 | 0.0 | 0.2 | (0.5) | 10.9 |
| **Total** | **40.5** | **0.8** | **1.5** | **(1.0)** | **41.8** |
| **Total** | **122.3** | **1.2** | **4.5** | **(8.8)** | **119.2** |

The item, equal to €119.2 million at 31 December 2011 (€122.3 million at 31 December 2010), decreased by €3.1 million on the previous year, due to the utilisations of the year (€8.8 million), partially offset by the allocations and the recognition of the discounting charge for the year (€5.7 million in total).

Below is the reconciliation of the current value of the obligation for employee benefits with respect to the assets and liabilities recognised on the financial statements:

| € million | Termination benefits | Indemnities for lack of notice and similar | Additional months' pay | Loyalty bonus | ASEM | Energy discount | Total |
|---|---|---|---|---|---|---|---|
| Current value of obligation | 58.3 | 0.9 | 8.3 | 3.8 | 5.7 | 28.9 | 105.9 |
| Net actuarial gains/losses not recognised | 6.1 | 1.8 | (1.8) | 0.0 | 5.2 | 2.0 | 13.3 |
| **Net liabilities recognised** | **64.4** | **2.7** | **6.5** | **3.8** | **10.9** | **30.9** | **119.2** |

Costs for liabilities in respect of employee benefits recognised in the income statement break down as follows:

| € million | Termination benefits | Indemnities for lack of notice and similar | Additional months' pay | Loyalty bonus | ASEM | Energy discount | Total |
|---|---|---|---|---|---|---|---|
| Service cost | 0.0 | 0.1 | 0.3 | 0.2 | 0.2 | 0.8 | 1.6 |
| Financial expense | 2.4 | 0.0 | 0.4 | 0.2 | 0.2 | 1.3 | 4.5 |
| Amortisation of actuarial gains/losses | (0.1) | (0.4) | 0.1 | (0.2) | (0.5) | 0.0 | (1.1) |
| **Total** | **2.3** | **(0.3)** | **0.8** | **0.2** | **(0.1)** | **2.1** | **5.0** |

The main assumptions made in the actuarial estimate of employee benefit obligations are as follows:

| Percentage figures | 2011 | 2010 |
|---|---|---|
| Discount rate | 4.1% | 4.1% |
| Rate of increase in personnel salary | 2.0% - 4.0% | 2.0% - 4.0% |
| Rate of increase in healthcare costs | 3.0% | 3.0% |

## 23. Provisions for risks and charges - €142.3 million

The items and changes of the provisions for risks and charges at 31 December 2011 are set out below:

| € million | Provision for disputes and litigation | Provisions for other risks and charges | Provision for early retirement | Total |
|---|---|---|---|---|
| **Balance at 31.12.2010** | **15.3** | **136.7** | **13.0** | **165.0** |
| Provision | 0.5 | 28.2 | 7.9 | 36.6 |
| Utilisations and other changes | (0.4) | (58.1) | (0.8) | (59.3) |
| **Balance at 31.12.2011** | **15.4** | **106.8** | **20.1** | **142.3** |

### Provision for disputes and litigation - €15.4 million

The provision is accrued to cover the liabilities at year end that may arise from lawsuits and out-of-court disputes relating to Company activities. The amount accrued takes into account the opinions both of internal and external legal counsel. The caption is substantially in line with the previous year. Litigation for which no potential charge can reasonably be calculated are described under "Off-balance sheet commitments and risks".

### Provision for other risks and charges - €106.8 million

The provision shows a net decrease of €31.2 million compared with last year, ascribable to accruals of €28.2 million and utilisations of a negative €58.1 million in the course of the year. More specifically:

- partial release of the fund accrued in 2009 for probable charges relating to the sale of the majority share package of Terna Participações (a negative €33.8 million inclusive of the exchange gain or losses), for the part of the contractual bonds that matured during the financial year;
- exchange rate adjustment (a negative €1.2 million) of the provision for probable expenses relating to tax obligations deriving from the sale of Terna Participações;
- a net accrual of €2.2 million relating to "Projects for urban and environmental renewal", the aim of which is to offset the environmental impact of the construction of long-distance power lines;
- a net accrual of €2.2 million for the charges due to distributing companies for power failures of the transformation plants linked to the NTG (in accordance with Resolution 341/07 – €1.1 million) as well as for the sharing of indemnities due to final users (€1.1 million).

**Provision for early retirement incentives - €20.1 million**

This provision reflects the estimated non-recurring charges related to the voluntary early termination of the working relationship of employees who are eligible for retirement. The item reflects an increase of €7.1 million for net accruals made during the financial year.

## 24. Deferred tax liabilities - €169.1 million

The changes in this provision are analysed below:

| € million | 31.12.2010 | Impact recognised in profit or loss | | Impact recognised in equity (*) | 31.12.2011 |
|---|---|---|---|---|---|
| | | Provisions | Utilisations | | |
| **Deferred tax liabilities** | | | | | |
| Property, plant and equipment | 298.5 | 78.4 | (48.2) | | 328.7 |
| Employee benefits and financial instruments | 3.5 | 0.8 | 0.0 | | 4.3 |
| **Total deferred tax liabilities** | **302.0** | **79.2** | **(48.2)** | **0.0** | **333.0** |
| **Deferred tax assets** | | | | | |
| Provisions for contingencies and charges | 14.2 | 12.8 | (3.5) | | 23.5 |
| Allowance for impairment accounts | 3.1 | 0.5 | | | 3.6 |
| Employee benefits | 22.9 | 14.5 | (10.5) | | 26.9 |
| FVH - CHF derivatives | 12.9 | | | 29.4 | 42.3 |
| Release of goodwill | 25.2 | 46.2 | (3.8) | | 67.6 |
| **Total deferred tax assets** | **78.3** | **74.0** | **(17.8)** | **29.4** | **163.9** |
| **Net deferred tax liabilities** | **223.7** | **5.2** | **(30.4)** | **(29.4)** | **169.1** |

(*) In the "Other comprehensive income".

This balance, equal to €169.1 million, reflects the net movements in the Company's deferred tax assets and liabilities.
Deferred tax liabilities totalled €333.0 million, up €31.0 million, essentially due to:

- allocation of deferred taxes as a consequence of the adjustment of the opening balance to the higher IRES rate established by the so called "corrective manoeuvre-*bis*" (€76.3 million) approved by Italian Law Decree no. 138 of 13 August 2011, enacted by Parliamentary Law on 14 September, amending regulations of the "Robin Hood Tax";
- adjustment of opening deferred taxes to the higher IRAP rate of concession holder companies established by Italian Law Decree no. 98 of 6 July 2011, Art. 23, paragraph 5 for €2.9 million;
- the use of previous provisions to cover the difference between additional depreciation and amortisation calculated using ordinary technical rates (€39.1 million), including the reversal in respect of the amortisation/depreciation charge for the period attributable to the difference from merger eliminations allocated to property, plant and equipment following mergers carried out in previous years (€2.8 million);
- release of the charge for year (€9.1 million) of the provision for deferred IRAP liabilities governed by Law no. 244 dated 24 December 2007 (the 2008 Finance Law), recorded in prior years in relation to economic/technical rates.

Deferred tax assets (€163.9 million) include the change to the opening balance in order to consider the change in the accounting principle relative to the booking of the release in financial year 2009, in compliance with Art. 15 of Italian Legislative Decree no. 185/2008, for an amount of €25.2 million, of goodwill deriving from the incorporation of RTL into the company. An increase is also seen of €85.6 million, mainly referring to the following changes:

- allocation of deferred tax assets as a consequence of the above-stated adjustment of the IRES rate to that established by the "corrective manoeuvre-*bis*" for €23.5 million;
- accrual of €39.8 million, for tax recognition of the goodwill recorded on the consolidated financial statements, transferred with the acquisition of the subsidiary Terna Rete Italia S.r.l. (formerly TELAT), established by Italian Law Decree no. 98 of 6 July 2011;
- accrual of €24.4 million, attributable to the tax effect, which has no impact on the income statement, in respect of changes in cash flow hedge instruments;
- net use, amounting to €3.8 million, of the share for the year of deferred tax assets allocated for the release of goodwill recorded following the merger of RTL;
- net use of €2.6 million relative to movements in provisions for employee benefits;
- net accrual for €4.3 million in relation to uses during the year of the provisions for risks and charges.

## 25. Other non-current liabilities - €129.1 million

The item, amounting to €129.1 million at 31 December 2011, encompasses the deferred portions of set-up grants.
The decrease of €7.5 million in the item with respect to the previous year regards:

- the release, in the amount of €5.2 million, of the portions of grants in connection with depreciation of the plants to which they refer;
- the release of the share of the year of the Company price for the remuneration of costs incurred during the financial year for the NTG Security Plan (€2.3 million).

## 26. Current liabilities

Current liabilities at 31 December 2011 break down as follows:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| Short-term loans (*) | 0.0 | 73.1 | (73.1) |
| Current portion of long-term loans (*) | 59.7 | 59.7 | 0.0 |
| Trade payables | 2,047.7 | 1,552.8 | 494.9 |
| Tax liabilities | 88.1 | 69.1 | 19.0 |
| Current financial liabilities (*) | 40.1 | 24.2 | 15.9 |
| Other current liabilities | 135.9 | 133.2 | 2.7 |
| **Total** | **2,371.5** | **1,912.1** | **459.4** |

(*) See the comments in Note 24. Loans and financial liabilities.

### Trade payables – €2,047.7 million

Trade payables at 31 December 2011 break down as follows:

| € million | 31.12.2011 | 31.12.2010 | Change |
|---|---|---|---|
| **Suppliers:** | | | |
| - Energy-related payables | 1,334.4 | 1,068.5 | 265.9 |
| - Non energy-related payables | 673.2 | 455.1 | 218.1 |
| Payables due to associates | 7.1 | 5.0 | 2.1 |
| Payables due to subsidiaries | 29.9 | 22.2 | 7.7 |
| Payables for contract work in progress | 3.1 | 2.0 | 1.1 |
| **Total trade payables** | **2,047.7** | **1,552.8** | **494.9** |

### Suppliers

### Energy-related payables

This item reports the effects on the balance sheet of payables for "pass-through" costs not ascribable to the Company, and refers mostly to purchase of energy relative to dispatching activities and the transport fee due to the owners of other sections of the NTG.
The increase of €265.9 million compared with the previous year is essentially attributed to:

- increased payables (€263.1 million) relative to "pass-through items" which are mainly ascribable to the joint effect of:
  - the increase in payables for the acquisition of electrical energy outside of the Power Exchange (€234.1 million) which is essentially due to the greater balance of net payables for capacity payment (€110.8 million), the increase in debt items awaiting definition on the part of the AEEG – in particular the availability of productive capacity (PC), totalling €34.9 million – as well as the rise in payables for the essential units for the safety of the electrical system (EUSES), totalling €84.7 million;
  - increased debt for the purchase of electricity within the Power Exchange (€29.0 million), mainly deriving from the net effect of the greater payables generated by the increased quantities and prices of the measurement of the imbalance (€97.2 million) and from the recognition of payables relating to the market coupling mechanism for the management of congestion on the inter-connection with Slovenia (€7.7 million); partly offset, as already described in the "Trade receivables" sections by the reduction in volumes of resources attained on the energy market (€19.6 million), by the reduction of the debt items relative to the dispatching of electricity produced by non-programmable renewable sources envisaged by the Resolution ARG/elt 5/10 (€14.3 million) and the lower payables deriving from the virtual interconnection activities (€44.3 million);

- greater payables not ascribable to the Parent Company (€2.8 million) to the Adjustment Fund for the Electricity Sector, deriving from the increased charges payable to the Exceptional Events Fund for power failures which occurred during financial year 2011 and as adjustment for the previous year (€1.2 million), in accordance with Resolution 341/07 and its subsequent amendments as well as the reimbursement of the grid transmission fees balance for previous years (€1.6 million) which was partially offset by the receivable booked by the Company for the same amount, as described in the paragraph relative to “Receivables for grid transmission fees” under trade receivables.

### Non energy-related payables

Amounts due to suppliers refer to invoices both already received and yet to be received for tenders, services and the purchase of materials and equipment.
The increase on previous year (€218.1 million) is essentially due to purchases and services in respect of increased capital expenditure in the last quarter of 2011 compared with the same period of 2010 and also as a result of payments made during the first few days of the next financial year.

### Associates

This item amounts to €7.1 million and includes payables to the associate CESI for services provided to the Company in the construction and management of laboratories and plants for tests, inspections, studies and experimental research in the general field of electricity technology and scientific and technical progress. The increase (€2.1 million) compared with 31 December 2010 is the result of an increase in services delivered in the final part of the year.

### Payables to subsidiaries

The increase in the item, equal to €7.7 million, is mainly due to the greater amount owing to the subsidiary Terna Rete Italia for the portion of NTG relating to December, by virtue of the tariff adjustments and in addition to the recording of the payable on the portion of NTG owned by the subsidiary linked to the mitigation mechanism established by ARG/elt Resolution 188/08.
Company commitments with suppliers totalled some €2,294.5 million and refer to purchase commitments relating to normal operating activities for the period 2012-2017.

### Payables for contract work in progress

The payables for contract work in progress concerning advances from customers amounted to €3.1 million at 31 December 2011 and was substantially in line with the balance at 31 December 2010 (+€1.1 million). It is composed as follows:

| € million | Payments on account | Contract value | Balance at 31.12.2011 | Payments on account | Contract value | Balance at 31.12.2010 |
|---|---|---|---|---|---|---|
| Other | (15.5) | 12.4 | (3.1) | (23.2) | 21.2 | (2.0) |

### Tax liabilities - €88.2 million

The caption refers to the Company’s liabilities for IRES and IRAP taxes for the financial year. It shows a net increase on the previous financial year, amounting to €19.1 million, mainly as a result of the adjustment to the new IRES tax regulations introduced by Italian Law Decree no. 138 of 13 August 2011. This new legislation has established an extension to the electricity transmission sector of the scope of the Robin Hood Tax, with an increase in the additional IRES rate from 6.5% to 10.5% for three financial years.

### Other current liabilities €135.9 million

Other current liabilities break down as follows:

| € million | 31.12.2011 | Due within one year | Due beyond one year | 31.12.2010 | Change |
|---|---|---|---|---|---|
| Payments on account | 37.1 | 21.9 | 15.2 | 29.3 | 7.8 |
| Other tax liabilities | 20.5 | 20.5 | | 6.0 | 14.5 |
| Payables to social security institutions | 22.3 | 22.3 | | 22.4 | (0.1) |
| Payables to employees | 31.2 | 31.2 | | 38.9 | (7.7) |
| Other payables: | | | | | |
| - third parties | 24.8 | 4.9 | 19.9 | 36.2 | (11.4) |
| - subsidiaries | 0.0 | 0.0 | 0.0 | 0.4 | (0.4) |
| **Total** | **135.9** | **100.8** | **35.1** | **133.2** | **2.7** |

### Payments on account

This caption (€37.1 million) includes the set-up grants related to assets collected by the Company in relation to assets under construction at 31 December 2011.
Compared to the 2010 book value (€29.3 million), there is an increase of €7.8 million, mainly due to the net effect of new payments on account received from third parties for €19.6 million and a decrease of €11.8 million in the grants reducing the book values of assets entered into operation during the financial year; in particular there are payments on account received in accordance with the mandate contract for the design of interconnection network "Interconnector" with abroad (€18.6 million, in accordance with Resolution ARG/elt 179/09 and its subsequent amendments).

### Other tax liabilities

Other tax liabilities, amounting to €20.5 million, show an increase of €14.5 million with respect to the previous financial year, mainly as a result of the recognition of the VAT payable for the year.

### Payables to social security institutions

Amounts payable to social security institutions, mainly relating to payables due to INPS, amount to €22.3 million (€22.4 million at 31 December 2010), basically in line with the previous financial year. The item also includes the payable due to Fondo Previdenza Elettrici – F.P.E. (€4.8 million).

### Payables to employees

Payables to employees came to €31.2 million (€38.9 million at 31 December 2010) and mainly refer to:
- accruals made for staff incentives to be paid the following year (€16.5 million);
- payments due to employees for unused holiday time and abolished public holidays (€8.8 million);
- termination indemnities due to employees whose employment was terminated before 31 December 2011 (€2.0 million).

### Other payables to third parties

Other payables, equal to €24.8 million (€36.2 million at 31 December 2010), mainly regard security deposits (€19.9 million) received from electricity market operators securing their obligations in respect of dispatching contracts. This item reports a decrease of €11.4 million which is essentially attributable to caution money described above (a negative €12.7 million).

# E. Commitments and risks

## Risk management

### Market and financial risks

During the financial year, in going about its business, Terna is exposed to various different financial risks: market risk (namely interest rate risk and inflation risk), liquidity risk and credit risk.
This section provides comprehensive information regarding Terna's exposure to all the above risks, along with a presentation of the objectives, policies and processes for managing those risks and the methods used to measure them, with further quantitative disclosures concerning the 2011 financial statements.
The risk management policies adopted by Terna seek to identify, analyse and monitor the risks to which the Company is exposed, establishing appropriate limits and controls, and checking compliance with such limits. These policies and related systems are revised on a regular basis in order to reflect any changes in market conditions and the Company's activities.
As a part of the financial risk management policies approved by the Board of Directors, Terna has established the responsibilities and operating procedures for financial risk management, specifically as concerns the instruments to be used and the precise operating limits in managing them.

| | 2011 | | | | | 2010 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| € million | Receivables | Receivables at fair value | Hedging derivatives | Assets available for sale | Total | Receivables | Receivables at fair value | Hedging derivatives | Assets available for sale | Total |
| **Assets** | | | | | | | | | | |
| Derivative financial instruments | - | - | 521.8 | - | 521.8 | - | - | 200.3 | - | 200.3 |
| Cash, short-term deposits, deposit certificates and inter-company loans | 1,583.0 | - | - | - | 1,583.0 | 668.7 | - | - | - | 669.0 |
| **Total** | **1,583.0** | **-** | **521.8** | **-** | **2,104.8** | **668.7** | **200.3** | **-** | | **869.3** |

| € million | 2011 Payables | 2011 Loans at fair value | 2011 Hedging derivatives | 2011 Other liabilities at amortised cost | 2011 Total | 2010 Payables | 2010 Loans at fair value | 2010 Hedging derivatives | 2010 Other liabilities at amortised cost | 2010 Total |
|---|---|---|---|---|---|---|---|---|---|---|
| **Liabilities** | | | | | | | | | | |
| Long-term debt | 2,494.5 | 4,304.0 | - | - | 6,798.4 | 2,552.1 | 2,728.2 | - | - | 5,280.3 |
| Derivative financial instruments | - | - | 111.4 | - | 111.4 | - | - | 47.1 | - | 47.1 |
| **Total** | **2,494.5** | **4,304.0** | **111.4** | **-** | **6,909.8** | **2,552.1** | **2,728.2** | **47.1** | **-** | **5,327.4** |

## Market risks

Market risk is the risk that the fair value or future cash flows of a financial instrument may fluctuate as a result of changes in financial market conditions. Market risks include three types of risks: exchange rate risk, interest rate risk and inflation risk.
Risk management must be performed with the objective of maximising financial income and minimising the related risks by selecting counterparties and instruments compatible with the corporate risk management policy. Speculative activity is not envisaged in the corporate mission.
Terna S.p.A. seeks to adopt a dynamic approach to financial risk management. This approach is characterised by risk aversion, aiming at minimising risk through continuous monitoring of financial markets in order to plan hedging transactions in favourable market conditions. The dynamic approach makes it possible to take action to improve existing hedges where changes in market conditions or in the hedged item make the latter unsuitable or excessively expensive. The concept of hedging transaction is not restricted to those hedges that qualify for hedge accounting, but rather encompasses the objective of total or partial hedging of the income statement or statement of financial position item from interest rate risk.
All derivative contracts have a notional amount and maturity date less than or equal to that of the underlying financial liability, so that any change in the fair value and/or estimated cash flows of the contracts is offset by a corresponding change in the fair value and/or estimated cash flows of the underlying position. The fair value of financial derivatives reflects the estimated amount that Terna would pay or receive in order to extinguish contracts at the closing date.
The fair value of instruments is determined in accordance with the fair value hierarchy envisaged under IFRS 7 (Level 2) by means of appropriate valuation techniques for each category of financial instrument, using market data as at the closing date (such as interest rates, exchange rates, volatility) and discounting projected cash flows on the basis of the market yield curve and inflation at the reporting date.
The financial assets and liabilities in respect of derivative instruments in place during the year can be classified as:

- cash flow hedge derivatives, essentially related to hedging the risk of changes in the cash flows associated with long-term floating-rate loans;
- fair value hedge derivatives, essentially related to hedging the exposure to changes in the fair value of a financial asset or liability associated with fluctuations in interest rates (fixed-rate bonds).

Below are the notional amounts and fair values of the derivative financial instruments subscribed by the Terna Group:

| € million | 2011 Notional amount | 2011 Fair value | 2010 Notional amount | 2010 Fair value | Change Notional amount | Change Fair value |
|---|---|---|---|---|---|---|
| FVH derivatives | 3,750.0 | 521.8 | 2,500.0 | 200.3 | 1,250.0 | 321.5 |
| CFH derivatives | 3,418.4 | (111.4) | 1,830.1 | (47.1) | 1,588.3 | (64.3) |

## Interest rate risk

Interest rate risk is represented by the uncertainty associated with interest rate fluctuations. This is the risk that a change in market rates may produce effects on the fair value or future cash flows of financial instruments.
In conducting its operations, Terna is exposed to the risk of fluctuations in interest rates. Its main source of interest rate risk is associated with items of net financial debt and the related hedging positions in derivative instruments that generate financial expense. Terna's borrowing strategy focuses on long-term loans whose term reflects the useful life of company assets. It pursues an interest rate risk hedging policy that aims to reconcile this approach with the regulatory framework, which every four years establishes the cost of debt as part of the formula to set the return on the Regulatory Asset Base (RAB).
Accordingly, the hedging instruments used, at various maturity dates, include both derivatives that transform fixed rates into floating rates and derivatives that transform floating rates into fixed rates.
In order to reduce the amount of financial debt exposed to the risk of fluctuations in interest rates and to optimise the temporal correlation between average cost of debt and regulatory rate used in the WACC formula, various types of plain vanilla derivatives are used, such as interest rate swaps.
Interest rate swaps are used in order to reduce the volume of debt exposed to fluctuations in interest rates and to reduce

the volatility of borrowing costs. With an interest rate swap, Terna agrees with a counterparty to exchange, at specific intervals, the floating-rate cash flows on a specified notional amount against the fixed-rate (agreed between the parties) cash flows, or vice versa.
The following table shows the financial instruments entered into by Terna, classified according to the type of interest rate (fixed or floating):

| | Carrying amount | | |
|---|---|---|---|
| € million | 31.12.2011 | 31.12.2010 | Change |
| Fixed-rate financial instruments: | | | |
| - assets | 0.0 | 0.0 | 0.0 |
| - liabilities | 4,415.3 | 2,775.3 | 1,640.0 |
| Floating-rate financial instruments: | | | |
| - assets | 2,286.1 | 869.0 | 1,417.1 |
| - liabilities | 2,675.8 | 2,552.1 | 123.7 |
| **Total** | **4,805.0** | **4,458.4** | **346.6** |

### Sensitivity to interest-rate risk

As regards the management of interest rate risk, Terna has, on the one hand, entered into fixed-to-floating interest rate swaps (FVH) to hedge the fair value of the fixed-rate risk bonds and, on the other, floating-to-fixed interest rate swaps (CFH) to hedge the expected cash flows in respect of all other floating-rate debt.
Since the hedging relationship between the derivative and the hedged item is formally documented and the effectiveness of the hedge, as verified initially and periodically over its life, is high (between 80% and 125%), the Company has elected to use hedge accounting to ensure the perfect temporal matching of the hedge and the hedged item. The aim of hedge accounting is to recognise the effects of the hedges and the hedged items in the income statement at the same time. Accordingly, for FVH derivatives, any changes in the fair value of the hedged item attributable to the risk being hedged must be booked in the income statement, thereby offsetting the changes in the fair value of the derivative booked in the income statement. For CFH derivatives, the changes in the fair value of the derivative must be booked in "Other comprehensive income" (recognising any ineffective portion of the hedge directly in the income statement) and then reversed through the income statement in the same period in which the cash flows of the hedged instrument materialise. The characteristics of the CFH derivatives mirror those of the underlying hedged asset so the related cash flows will materialise at the same maturities as the interest on the debt, with no impact of the changes in fair value on the income statement.

The following table reports the amounts booked in the income statement and in "Other comprehensive income" for positions that are sensitive to changes in interest rates, the theoretical value of the positions following a positive or negative shift in the yield curve and the differential impact booked in the income statement and in "Other comprehensive income" of such changes. A hypothetical 10% variation in interest rates with respect to market interest rates at the reporting date was assumed:

| | Profit or loss | | | Equity | | |
|---|---|---|---|---|---|---|
| € million | Current rates +10% | Current rates | Current rates -10% | Current rates +10% | Current rates | Current rates -10% |
| **31 December 2011** | | | | | | |
| Positions sensitive to interest rate variations (FVH, bonds, CFH) | 1.0 | (0.2) | (1.4) | (100.0) | (111.4) | (122.9) |
| *Hypothetical change* | 1.2 | - | 1.2 | 11.4 | - | (11.5) |
| **31 December 2010** | | | | | | |
| Positions sensitive to interest rate variations (FVH, bonds, CFH) | 2.9 | 2.2 | 1.7 | (44.5) | (47.1) | (49.9) |
| *Hypothetical change* | 0.7 | - | (0.5) | 2.6 | - | (2.8) |

## Inflation risk

As regards inflation rate risk, the rates established by Regulators to remunerate Terna S.p.A.'s activities are determined so as to allow coverage of the sector's recognised costs. Such cost components are updated on an annual basis to consider the accrued impact of inflation. In 2007, the Company used an inflation-linked bond issue to obtain an effective hedge of profit for the year; any decrease in expected revenue due to a decrease in the inflation rate would be offset by lower financial expense.

## Exchange rate risk

Generally Terna hedges exchange rate risk through the forward sale or purchase of currencies (forward contracts) or the use of options. Currency options give Terna the right or the obligation to buy or sell predetermined amounts of a currency at a specific exchange rate at the end of a specific period of time. Normally, both forward contracts and options have maturities of no more than 12 months.
Such contracts have a notional amount and maturity date less than or equal to that of the underlying financial liability, or the expected cash flows, so that any change in the fair value and/or estimated cash flows deriving from an appreciation or depreciation of the euro against other currencies is fully offset by a corresponding change in the fair value and/or estimated cash flows of the underlying position.
At 31 December 2011 (as at 31 December 2010), no financial instruments exposed to exchange rate risk were present.

## Liquidity risk

The liquidity risk is the risk Terna might encounter difficulty in discharging its obligations in respect of its financial liabilities and operational cycle. Liquidity risk management seeks to ensure adequate coverage of financial needs by obtaining adequate lines of credit and appropriate management of any surplus liquidity. As of 31 December 2011 Terna had €500 million in medium-term credit lines and €703.8 million in short-term credit lines. The table below shows the repayment plan at 31 December 2011 of the nominal long-term debt:

| € million | Maturity | Notional amount of debt 31.12.2011 | Maturity within 12 months | Maturity beyond 12 months | 2013 | 2014 | 2015 | 2016 | After |
|---|---|---|---|---|---|---|---|---|---|
| Bonds 10y and 20y | 2014-2024 | 1,400.0 | 0.0 | 1,400.0 | 0.0 | 600.0 | 0.0 | 0.0 | 800.0 |
| Bond - Inflation linked | 2023 | 546.9 | 0.0 | 546.9 | 0.0 | 0.0 | 0.0 | 0.0 | 546.9 |
| Bond - Private placement | 2019 | 600.0 | 0.0 | 600.0 | 0.0 | 0.0 | 0.0 | 0.0 | 600.0 |
| Bond - 10y | 2021 | 1,250.0 | 0.0 | 1,250.0 | 0.0 | 0.0 | 0.0 | 0.0 | 1,250.0 |
| **Total fixed rate** | | **3,796.9** | **0.0** | **3,796.9** | **0.0** | **600.0** | **0.0** | **0.0** | **3,196.9** |
| EIB | 2014-2030 | 1,345.4 | 59.7 | 1,285.7 | 69.4 | 79.0 | 76.9 | 84.9 | 975.4 |
| Club Deal | 2015 | 650.0 | 0.0 | 650.0 | 0.0 | 0.0 | 650.0 | 0.0 | 0.0 |
| CDP | 2019 | 500.0 | 0.0 | 500.0 | 0.0 | 0.0 | 0.0 | 0.0 | 500.0 |
| **Total floating rate** | | **2,495.4** | **59.7** | **2,435.7** | **69.4** | **79.0** | **726.9** | **84.9** | **1,475.4** |
| **Total** | | **6,292.2** | **59.7** | **6,232.5** | **69.4** | **679.0** | **726.9** | **84.9** | **4,672.3** |

## Credit risk

Credit risk is the risk a customer or one of the counterparties to a transaction in financial instruments could cause a financial loss by failing to discharge an obligation. It is mainly generated by trade receivables and the financial investments of the Company.
The credit risk originated by open positions on transactions in financial derivatives is considered to be marginal since the counterparties, in compliance with financial risk management policies, are leading international credit institutions with high ratings and such transactions are diversified in compliance with specific concentration limits.
Terna provides its services to counterparties considered solvent by the market, who therefore have a high credit standing, and does not have highly concentrated credit risk.
Credit risk management is guided by the provisions of AEEG Resolution no. 111/06, which, in Art. 49, introduced instruments for the limitation of risks related to the insolvency of dispatching customers, both on a preventive basis and in the event of actual insolvency. In particular, the Resolution establishes three instruments to safeguard the electricity market: a guarantee system (bank guarantees provided by individual dispatching customers, based on their sales revenue), the option of terminating dispatching contracts (in the event of insolvency or failure to replace enforced guarantees) and, finally, the possibility of recovering uncollected receivables, after having taken all other possible collection actions, through a specific fee defined by the Authority.

The following table summarises the exposure to such risk as at the reporting date:

| € million | Carrying amount | | Change |
|---|---|---|---|
| | 31.12.2011 | 31.12.2010 | |
| FVH derivatives | 521.8 | 200.3 | 321.5 |
| Deposit certificates | 150.0 | 0.0 | 150.0 |
| Inter-company loan to Terna Rete Italia | 500.0 | 500.0 | 0.0 |
| Cash and cash equivalents | 1,114.4 | 150.1 | 964.3 |
| Net current a/c position of intercompany treasury | - | 18.6 | (18.6) |
| Trade receivables | 1,684.0 | 1,495.6 | 188.4 |
| **Total** | **3,970.2** | **2,364.6** | **1,605.6** |

The total value of the exposure to credit rate risk at 31 December 2011 is represented by the carrying amount of financial assets (current and non-current), trade receivables and cash and cash equivalents.

The following tables provide qualitative information on customer receivables that are not past due and have no impairment:

GEOGRAPHICAL DISTRIBUTION

| € million | Carrying amount | |
|---|---|---|
| | 2011 | 2010 |
| Italy | 1,654.2 | 1,482.6 |
| Euro-area countries | 27.2 | 8.9 |
| Other countries | 2.6 | 4.1 |
| **Total** | **1,684.0** | **1,495.6** |

CUSTOMER TYPOLOGY

| € million | Valore contabile | |
|---|---|---|
| | 2011 | 2010 |
| Distributors (*) | 243.4 | 243.9 |
| Electricity Equalisation Fund (**) | 131.3 | 71.7 |
| Input dispatching contractors | 229.4 | 310.2 |
| Withdrawal dispatching contractors (non distributors) | 1,000.2 | 765.3 |
| Parties which have undersigned virtual import contracts and virtual import services (interconnectors and shippers) | 12.5 | 35.2 |
| Receivables from unregulated activities | 67.2 | 69.3 |
| **Total** | **1,684.0** | **1,495.6** |

(*) Includes receivable accrued in respect of Terna Rete Italia grid transmission fees.
(**) Of which €116.2 million from volume effect on grid transmission fees.

The following table breaks down customer receivables by age, reporting any potential impairment:

| € million | 2011 | | 2010 | |
|---|---|---|---|---|
| | Allowance for impairment accounts | Gross | Allowance for impairment accounts | Gross |
| Not yet past due | - | 1,560.0 | - | 1,430.9 |
| 0-30 days past due | - | 50.0 | - | 38.5 |
| 31-120 days past due | - | 37.9 | - | 3.5 |
| More than 120 days past due | (23.6) | 59.7 | (23.5) | 46.2 |
| **Total** | **(23.6)** | **1,707.6** | **(23.5)** | **1,519.1** |

Changes in the provision for bad debts in the course of the year were as follows:

| € million | 2011 | 2010 |
|---|---|---|
| Balance at 1 January | (23.5) | (27.0) |
| Reversal of provision | - | 3.5 |
| Impairment for the year | (0.1) | - |
| **Balance at 31 December** | **(23.6)** | **(23.5)** |

The value of guarantees received from eligible electricity market customers is illustrated below:

| € million | 2011 | 2010 |
|---|---|---|
| Input dispatching activity | 254.6 | 220.5 |
| Withdrawal dispatching activity | 763.0 | 831.3 |
| Grid transmission fees - distributors | 174.8 | 173.7 |
| Virtual importing | 280.2 | 338.0 |
| **Balance at 31 December** | **1,472.6** | **1,563.5** |

### Default risk and debt covenants

This risk is associated with the possibility that the loan contracts or bond rules to which the Company is party may contain provisions authorising counterparties to call in such loans immediately upon the occurrence of certain events, thereby generating liquidity risk. For more information on the contractual provisions of outstanding loans at 31 December 2011, please see the section “Loans and financial liabilities” in the notes of Terna S.p.A.

## Legal disputes

The main off-balance sheet commitments and risks of Terna S.p.A. at 31 December 2011 are as follows.

### Environmental and urban planning litigation

Environmental litigation originates from the installation and operation of electrical plants and primarily involves damages which could be derived from exposure to electrical and magnetic fields that are generated by long-distance power lines. The Company is involved in various civil and administrative suits requesting the transfer or change in operations of allegedly-harmful long-distance power lines, even though they were installed in full compliance with applicable legislation (Italian Law no. 36 of 22 February 2001 and Prime Ministerial Decree of 8 July 2003). Only a very small number of cases include claims for damages for harm to health caused by electromagnetic fields.

Only in a few cases have adverse judgements been issued against the Company. These have been appealed and the appeals are still pending, although adverse rulings are considered unlikely.

In addition, a number of cases relating to urban planning and environmental issues are pending in respect of the construction and operation of certain transmission lines. The possible effects of any unfavourable outcome to these cases are unpredictable and, accordingly, have not been considered when determining the “Provision for disputes and other risks”.

In a limited number of cases, the possibility of an adverse outcome cannot be entirely ruled out. The possible consequences could, in addition to the award of damages, include, inter alia, the costs of modifying lines and the temporary suspension of their use. In any case, any unfavourable outcome would not jeopardise line operations.

Examination of the above litigation, having regard for the information provided by the external legal consultants, suggests that the likelihood of adverse outcomes is remote.

### Litigation concerning concession activities

Given that it has been the licensee for transmission and dispatching activities since 1 November 2005, the Company has been involved in a number of cases appealing AEEG, MED and/or Terna measures relating to activities operated under the license. Only in those cases in which the plaintiffs not only claim defects in the measures, but also allege that Terna violated the rules established by such authorities has the Company appeared in court. Within the scope of this litigation, although a number of cases have seen the AEEG Resolutions struck down in the first and/or second-level court, together with the consequent measures adopted by Terna, it is felt that there is little risk of adverse outcomes for Terna, since the matters generally regard pass-through items. This position is supported by the information provided by the external legal counsel representing the Company in the cases involved. As the licensee for transmission and dispatching activities, the measures taken by the Company when applying the Resolutions adopted by the Authority are sometimes the subject of challenges. In appropriate circumstances, the economic costs of such challenges may be borne by the Authority.

# F. Business combinations

There were no business combinations during 2011.

# G. Related-party transactions

Terna's transactions with related parties during the year, taking account of the *de facto* control exercised over the Company by Cassa Depositi e Prestiti S.p.A. ascertained in 2007, regarded – in addition to the subsidiaries (Terna Rete Italia S.r.l., SunTergrid S.p.A., RTS S.r.l., Terna Crna Gora d.o.o. and Terna Plus S.r.l.) – the associate company CESI S.p.A., the employee pension funds (Fondenel and Fopen), Cassa Depositi e Prestiti as well as companies belonging to:

- the GSE Group;
- the Enel Group;
- the Eni Group;
- the Ferrovie dello Stato Group;

and those with ANAS S.p.A..

Related party transactions in 2011 are mainly services that are part of core business and regulated by market conditions. The scope of transactions with subsidiaries includes the acquisition from the subsidiary Terna Rete Italia of some transmission plants on which development and renewal works were made and the transfer to the subsidiary SunTergrid of a MV/HV utility electrical substation.
Terna supplies the operative management of all subsidiaries through specific Management fee contracts, which not only ensure administrative and financial coordination, but also coordination of institutional relations, giving it the option of acting, for and on behalf of the subsidiaries. With the subsidiary Terna Rete Italia, there is also an "Electrical service agreement in relation to power lines" in place for the management and maintenance of HV lines.
Terna is also involved in the management of cash demands of subsidiaries through specific Treasury contracts that ensure the guidance and coordination of all transactions in relation to financial resource and needs management and treasury services, as well as the implementation of all related transactions. Under the scope of the centralised treasury management of financial resources, we recall the loan of €500.0 million supplied by Terna to the subsidiary Terna Rete Italia in November 2009.
The following are the contractual terms and conditions of the financial transactions in place with subsidiaries:

| | Contractual conditions - interest rates | | |
|---|---|---|---|
| | | intercompany current a/c | |
| | Loan | Inventories | Utilisations |
| **Terna Rete Italia S.r.l.** | Euribor 6 months +2.50% | Euribor monthly average 1 month - 0.50% | Euribor monthly average 1 month + 1.00% |
| **SunTergrid S.p.A.** | - | Euribor monthly average 1 month - 0.50% | Euribor monthly average 1 month + 1.00% |
| **RTS S.r.l.** | - | Euribor monthly average 1 month - 0.50% | Euribor monthly average 1 month + 1.00% |
| **Terna Plus S.r.l.** | - | Euribor monthly average 1 month - 0.50% | Euribor monthly average 1 month + 1.00% |

The tables below specify the nature of the transactions implemented by the Company with related parties and the respective income and expense totalled during the period, in addition to the respective receivables and payables in place as of 31 December 2011:

| Related party | Revenue transactions | Cost transactions |
|---|---|---|
| **Terna Rete Italia** | **NTG transmission fees**<br>NTG transmission fees<br><br>**Non energy-related items**<br>Technical services and line maintenance, management fees, loan | **NTG transmission fees**<br>Grid remuneration<br><br>**Non energy-related items**<br>Acquisition of transmission plants, treasury services |
| **SunTergrid and RTS** | **Non energy-related items**<br>Provision of management fees, services for the development of photovoltaic plants, land lease, transfer of plants (electrical substation) | **Non energy-related items**<br>Treasury services |
| **Terna Plus** | **Non energy-related items**<br>Treasury services | |
| **Cassa Depositi e Prestiti S.p.A.** | | **Non energy-related items**<br>Credit line |
| **CESI S.p.A.** | **Non energy-related items**<br>Lease of laboratories and similar structures for specific purposes | **Non energy-related items**<br>Technical consultancy, studies and research, projects and experimentation |
| **GSE Group** | **Energy-related items**<br>MIS component, energy sale, rights of withdrawal, rights to use transport capacity for interconnections, dispatching prices<br><br>**Non energy-related items**<br>Specialist services, leases, IT services | **Energy-related items**<br>Purchase of energy, rights to use transport capacity for interconnections, fees for lost wind-powered generation |
| **Enel Group** | **Energy-related items**<br>Remuneration of the NTG and measurement aggregation, energy sale, rights of withdrawal, rights to use transport capacity for interconnections, dispatching prices<br><br>**Non energy-related items**<br>Leases and rentals, line maintenance | **Energy-related items**<br>Aggregation of measurements, purchase of energy, rights to use transport capacity for interconnections, EUSES remuneration<br><br>**Non energy-related items**<br>Return of electricity discount, staff administration, building services, supply of MV power to new stations, specialised services for connection to Terna control and protection systems |
| **ENI Group** | **Energy-related items**<br>Sale of energy, rights to use transport capacity for interconnections, dispatching prices<br><br>**Non energy-related items**<br>Line maintenance | **Energy-related items**<br>Energy purchase, coverage of joint management costs, interruptibility service |
| **Ferrovie Group** | **Energy-related items**<br>Dispatching prices, energy sale<br><br>**Non energy-related items**<br>Line moving | **Energy-related items**<br>NTG remuneration, energy purchase<br><br>**Non energy-related items**<br>Right-of-way fees |
| **ANAS S.p.A.** | **Non energy-related items**<br>Line moving | **Non energy-related items**<br>Right-of-way fees |
| **Fondenel e Fopen** | | **Non energy-related items**<br>Pension contributions borne by the Terna Group |

| Company<br>€ million | Income statement | | | | | | |
|---|---|---|---|---|---|---|---|
| | Income items | | | | Expenses | | |
| | Grid transmission fees and other energy-related items | Grid transmission fees for other owners and pass-through energy items | Non energy-related items | Dividends | Grid transmission fees and other energy-related items | Grid transmission fees for other owners and pass-through energy items | Non energy-related items |
| **Subsidiaries:** | | | | | | | |
| Terna Rete Italia S.r.l. | - | 141.5 | 87.8 | - | - | 141.5 | 0.1 |
| SunTergrid S.p.A. | - | - | 1.8 | 100.0 | - | - | 0.9 |
| RTS S.r.l. | - | - | 0.5 | - | - | - | - |
| Terna Crna Gora d.o.o. | - | - | - | - | - | - | - |
| Terna Plus S.r.l. | - | - | - | - | - | - | - |
| **Total subsidiaries** | **-** | **141.5** | **90.1** | **100** | **-** | **141.5** | **1.0** |
| **De facto parent company:** | | | | | | | |
| Cassa Depositi e Prestiti S.p.A. | - | - | - | - | - | - | 9.8 |
| **Total de facto parent company** | **-** | **-** | **-** | **-** | **-** | **-** | **9.8** |
| Associates: | | | | | | | |
| CESI S.p.A. | - | - | 0.1 | - | - | - | 2.3 |
| **Total associates** | **-** | **-** | **0.1** | **-** | **-** | **-** | **2.3** |
| **Other related companies:** | | | | | | | |
| GSE Group | 25.9 | 1,132.9 | 0.5 | - | - | 769.4 | - |
| Enel Group | 1,187.8 | 685.2 | 1.4 | - | - | 810.1 | 2.6 |
| Eni Group | 4.3 | 266.3 | 0.4 | - | - | 127.8 | 0.1 |
| Ferrovie Group | 1.5 | 39.4 | 0.1 | - | 6.8 | 194.5 | 0.1 |
| ANAS S.p.A. | - | - | - | - | - | - | - |
| **Total other related companies** | **1,219.5** | **2,123.8** | **2.4** | **-** | **6.8** | **1,901.8** | **2.8** |
| **Pension funds:** | | | | | | | |
| Fondenel | | | | | | | 0.4 |
| Fopen | - | - | | - | - | - | 1.8 |
| **Total pension funds** | **-** | **-** | **-** | **-** | **-** | **-** | **2.2** |
| **Total** | **1,219.5** | **2,265.3** | **92.6** | **100.0** | **6.8** | **2,043.3** | **18.1** |

| Company<br>€ million | Statement of financial position<br>Property plant and equipment<br>Capitalised costs | Receivables and other assets<br>Other | Receivables and other assets<br>Financial and position of inter-company current account | Payables and other liabilities<br>Other | Payables and other liabilities<br>Financial | Guarantees (*) |
|---|---|---|---|---|---|---|
| **Subsidiaries:** | | | | | | |
| Terna Rete Italia S.r.l. | 19.6 | 5.6 | 488.9 | 29.9 | - | - |
| SunTergrid S.p.A. | (1.6) | - | (167.7) | - | - | - |
| RTS S.r.l. | - | 0.2 | 0.1 | - | - | - |
| Terna Crna Gora d.o.o. | - | - | - | - | - | - |
| Terna Plus S.r.l. | - | - | - | - | - | - |
| **Total subsidiaries** | **18.0** | **5.8** | **321.3** | **29.9** | **-** | **-** |
| **De facto parent company:** | | | | | | |
| Cassa Depositi e Prestiti S.p.A. | - | - | 0.4 | - | 502.4 | |
| **Total de facto parent company** | **-** | **-** | **0.4** | **-** | **502.4** | **-** |
| Associates: | | | | | | |
| CESI S.p.A. | 16.0 | - | - | 7.1 | - | 3.2 |
| **Total associates** | **16.0** | **-** | **-** | **7.1** | **-** | **3.2** |
| **Other related companies:** | | | | | | |
| GSE Group | - | 0.1 | - | 0.1 | - | - |
| Enel Group | 3.1 | 119.3 | - | 27.4 | - | 390.9 |
| Eni Group | - | 0.4 | - | 2.8 | - | 15.9 |
| Ferrovie Group | 0.1 | 0.1 | - | 0.5 | - | 22.0 |
| ANAS S.p.A. | - | 0.1 | - | 0.4 | - | - |
| **Total other related companies** | **3.2** | **120.0** | **-** | **31.2** | **-** | **428.8** |
| **Pension funds:** | | | | | | |
| Fondenel | | | | | | |
| Fopen | - | - | - | 1.4 | - | - |
| **Total pension funds** | **-** | **-** | **-** | **1.4** | **-** | **-** |
| **Total** | **37.2** | **125.8** | **321.7** | **69.6** | **502.4** | **432.0** |

(*) The guarantees refer to the bank guarantees received on contracts.

# H. Significant non-recurring events and transactions, and atypical or unusual transactions

No significant, non-recurring, atypical or unusual transactions – with the exception of those described above – were carried out during 2011, either with third parties or with related parties.

# I. Notes to the statement of cash flows

The cash flow generated from **continuing operations** in the year amounted to €762.3 million, which reflects around €1,194.4 million in cash from operating activities (self-financing) and around €432.1 million in financial resources generated by the management of net working capital.
**Investing activities** used net financial resources of around €1,210.2 million, and included €1,110.9 million of investment in property, plant and machinery (€1,122.7 million net of plant grants totalling €11.8 million) and €49.7 million of investment in intangible assets.
Cash flow for investing activities also reflects the acquisition from the subsidiary Terna Rete Italia (formerly TELAT) of some transmission plants on which development and renewal works were made (€19.6 million), the transfer to the subsidiary SunTergrid (€1.6 million) of a MV/HV utility electrical substation. Financial investments include the equity interest amounting to 22.09% of the share capital of the Montenegro transmission operator CGES (a negative €34.2 million), the increase in the equity interest in the associate CESI (a negative €2.7 million) and the incorporation of the companies Terna Crna Gora and Terna Plus (a negative €2.0 million).
The **cash flows** from financing activities show a change of €1,212.2 million, mainly deriving from the net increase in financial debt (€1,368.1 million), from the extinction of financial relations with Rete Rinnovabile whose equity interest was sold during the year (€254.6 million), net of the disbursement of the 2010 dividend balance (€261.3 million) and the 2011 interim dividend (€160.8 million). More specifically, with reference to financial debt, please note the increase in medium/long-term debt (€1,591.2 million, including the short-term portion and net of FVH derivatives) – which, *inter alia*, reflects the March 2011 issue of a bond for a nominal value of €1,250.0 million – the repayment of a short-term loan taken out in late 2010 (€50 million) and the subscription in 2011 of deposit certificates with maturity of less than 12 months, for a total of €150 million.
The other changes in equity (€11.6 million in total) relate to the effects deriving from the exercise of stock options during the year. Consequently, the financial resources used in investing activities and the remuneration of equity led to total financial requirements of €1,620.7 million in the year, part of which (€762.3 million) was covered by the cash flows generated by operating activities and the remainder through new borrowings.

# L. Subsequent events

## Resolutions published by the AEEG for the new tariffs in regulatory period 2012-2015

On **2 January 2012**, the Authority for Electricity and Gas (AEEG) published Resolutions nos. 199/11, 204/11 and 197/11 thereby establishing, for the new regulatory period 2012-2015, the remuneration for the supply of electricity transmission, distribution, measurement and dispatching services and the regulation of the quality of the transmission service. The new features introduced by AEEG Resolution 199/11 include taking the weighted average cost of capital (WACC) from the previous 6.9% to 7.4% and establishing a review by November 2013, to apply from the second two-year period of the regulatory period (2014-2015). There will also be a new incentive category (category I4) for an extra remuneration of accumulation systems amounting to 2% for a period of 12 years subsequent to the coming into service of the investments. As from 2012, the AEEG has recognised a further 1% on the WACC, aimed at compensating for the effect of the “regulatory lag”, i.e. the delay with which the tariff remunerates investments made. Resolution 204/11 updates for 2012 the price for the electricity dispatching service, amounting to €0.0526 c/kWh. Resolution 197/11 on the regulation of the quality of service confirms the framework of the previous regulatory period, based on a premium/penalty mechanism. Quality of service will only be monitored by the Energy not supplied index. With this mechanism, the potential maximum impact is estimated for the Terna Group as ranging between a negative €12 and a positive €30 million per year.

## Terna alone in the Gold Class of the Sam Sustainability Yearbook 2012

On **30 January 2012** Terna, the only Italian electrical company and amongst the world's best, joined the Gold Class of the Sam - Sustainability Yearbook 2012, the yearbook of the international ratings agency that screens companies, assessing the possibility of their accessing, remaining in or being excluded from the prestigious Dow Jones indexes. If we compare this result with those of previous years (Silver Class in 2011, Bronze Class in 2010), we can see that Terna is reinforcing, indeed improving its position in a global top position, coming before some of the best international operators.

## 5-year bond issue for €1.25 billion

On **13 February 2012** Terna launched a bond issue on the market in euros, at a fixed rate, with expiry in 5 years, for a total of €1.25 billion under the scope of its Euro Medium Term Notes (EMTN) programme. This has been assigned an A- Credit Watch Negative rating for Standard and Poor's, A3 Outlook Negative by Moody's and A by Fitch.
The bond expiring on 17 February 2017 has an annual coupon of 4.125% and issue price of 99.809%. The bond has thus been priced with a spread of 257 basis points as compared with the mid swap. The securities, which will pay one coupon per year, will be listed on the Luxembourg Stock Exchange.
This transaction is intended for Institutional Investors and is placed by a pool of banks comprising BNP Paribas, Credit Suisse, Deutsche Bank, J.P. Morgan, Mediobanca, MPS Capital Services, Natixis and Unicredit Bank AG as joint-lead managers and joint-bookrunners; it closed successfully that same day and was 4.5 times oversubscribed compared to the offer, 80% of which came from abroad. The bond is intended to finance the grid development investments envisaged in the Company's business plan.

## Renewed Supervisory Body 231/2001

On **31 January 2012**, the Board of Directors of the Parent Company proceeded to appoint the members of the Supervisory Body pursuant to Italian Legislative Decree no. 231/2001, which had expired in financial year 2011. Prof. Bruno Assumma was confirmed Chairman while Mr. Ernesto Calaprice and Mr. Massimo di Noia, Mr. Alberto Bianchi and Ms. Filomena Passeggio were appointed members. The Board also resolved that Mr. Fulvio De Luca will act as secretary of the Supervisory Body, together with the audit function.

## Terna Cnra Gora share capital increase

On **10 February 2012**, Terna subscribed a share capital increase of the subsidiary Terna Cnra Gora for €5 million, in order to provide the company with the resources necessary to develop the business.

## Terna rating

On **30 January 2012** Fitch Ratings revised the rating for the senior unsecured debt of Terna S.p.A. from level A+ to A following the downgrading of the Italian Republic from A+ to A- with negative outlook. At the same time, Fitch confirmed both the long-term rating of the issuer as A with negative outlook and the short-term rating at F1.
On **8 March 2012** S&P confirmed the long and short-term rating of Terna S.p.A. at A- and A-2, respectively, and the senior unsecured debt rating at A-. In line with the Agency method for government related entities, these levels had been assigned to the Company on **20 January 2012**, following the downgrading from A to BBB+ of the Italian Republic. At the same time, the Agency removed the "CreditWatch" status with negative implications, the long-term rating of the Company and the rating of the senior unsecured debt, a status assigned by the agency in December 2011. The outlook is negative.

## The Business plan

On **20 March 2012**, Terna approved the Terna Group Business Plan for the period 2012-2016; guidelines are set out below:

- **core business:** over the next 5 years, €4.1 billion will be invested in the safety and modernisation of the electricity grid, of which 82% will be for the National Transmission Grid development with investments focused on maximizing the use of system capacity and reducing congestion, fostering the development of generation capacity from renewable sources;
- **non-core business:** up to approximately €1 billion will be used for the development of battery accumulation systems for 240 MW, at present awaiting authorisation and in any case as long as suitable remuneration is obtained. Additionally, both in Italy and abroad, investments of up to 900 million are planned in projects for private customers, with a forecast return that exceeds that of regulated business. In thus doing, the objective expenditure in non-core business is doubled (up to €1.9 billion), with respect to the previous plan;
- **improved margins (EBITDA margin):** it is expected that the increased revenue and the control of costs will allow to achieve an accumulated EBITDA over the period 2012-16, up approximately 19% with respect to the previous five-year plan. Average annual growth in EBITDA goes from 5% to 7.5%, showing a consistent improvement in operative cash flow. At the end of the period, the EBITDA margin will exceed 80% increasing with respect to the previous target of 78%;
- **a sound capital structure:** the commitment to strengthen equity coefficients continues. During the course of the plan, net debt is estimated as growing by approximately €1.6 billion to €6.7 billion, with a significant reduction of €1 billion with respect to the previous plan. The capital structure remains solid: during the plan, the ratio of net debt and RAB remains below 55% in all years of the plan and the ratio of net debt and EBITDA with respect to the 4.2 times of end 2011, remaining below the 4 times;
- **new dividends policy:** as from 2012, a basic dividend is envisaged from core business amounting to 19 euro cents per share, in addition to the contribution of non-core business (payout of 60% on results and/or gains).

# Disclosure pursuant to art. 149-*duodecies* of the CONSOB Issuers Regulation

The following table, prepared pursuant to art. 149-*duodecies* of the CONSOB Issuers Regulation, reports the fees for 2011 for the audit and the non-audit services provided to Terna S.p.A. by the same auditing companies.

| In euros | Entity providing service | | Prices due for the year |
|---|---|---|---|
| | KPMG S.p.A. | PWC S.p.A. (*) | |
| Statutory audit | 136,600.00 | 243,106.78 | 379,706.78 |
| Attestation services | 109,793.61 | 52,800.00 | 162,593.61 |
| **Total** | **246,393.61** | **295,906.78** | **542,300.39** |

(*) Appointment made by the Ordinary Shareholders' Meeting on 13 May 2011 for the nine years 1 January 2011-31 December 2019.

The CEO

***Certification of the separate financial statements pursuant to Art. 81-ter of CONSOB Regulation no. 11971 dated 14 May 1999 and subsequent amendments and additions***

1. The undersigned Flavio Cattaneo, as CEO, and Luciano Di Bacco, as Executive in Charge of the preparation of accounting documents for TERNA S.p.A., also considering that established by art. 154-*bis*, paragraphs 3 and 4 of Italian Legislative Decree no. 58 of 24 February 1998, certify:

- the suitability in relation to the business characteristics; and
- the effective application of the administrative and accounting procedures for the preparation of the separate financial statements during financial year 2011.

2. On this regard, no significant aspects emerged.

3. It is also specified that:

3.1 the separate financial statements at 31 December 2011:

a) are prepared in compliance with the applicable international accounting standards recognised in the European Community in accordance with Regulation (EC) no. 1606/2002 of the European Parliament and Council of 19 July 2002 and the provisions issued in implementation of art. 9 of Italian Legislative Decree no. 38/2005;

b) comply with the results of the accounts and accounting entries;

c) are suitable to providing a truthful, correct representation of the equity, economic and financial position of the issuer;

3.2 the report on operations includes a reliable analysis of the trend and operating result, in addition to the position of the issuer and a description of the main risks and uncertainties to which it is exposed.

Rome, 20 March 2012

# Reports

Report by the Board of Statutory Auditors to the shareholders' meeting of Terna S.p.A.

Auditors' Report in accordance
with articles 14 and 16 of Legislative Decree no. 39 of 27 January 2010
Financial Statements as of 31 December 2011

**Report by the Board of Statutory Auditors to Terna S.p.A.'s Shareholders Meeting**
(pursuant to Art. 153 of Legislative Decree no. 58/98)

Shareholders,

During the year that ended on December 31, 2011, we performed the supervisory activity required by the Law (Legislative Decree no. 58 dated February 24, 1998 – "Consolidated text for the provisions regarding financial brokerage activity" and Legislative Decree dated January 27, 2010 no. 39 "Implementation of Directive 2006/43/CE related to the legal auditing of annual accounts and consolidated accounts, modifying Directives 78/660/CEE and 83/349/CEE and abrogating Directive 84/253/CEE"), adapting our activity to the code of practice of the Boards of Statutory Auditors of capital-based companies with shares listed in regulated markets as recommended by National Board of Chartered Accountants and by CONSOB provisions regarding company auditing and activities conducted by the Boards of Statutory Auditors.

The auditing activity, pursuant to Legislative Decree 39/2010, was assigned and carried out by the PriceWaterHouse Coopers S.p.A. Auditing firm whose reports are referred to.

The Board of Statutory Auditors presently in office was appointed by the Shareholders Meeting on May 13, 2011 based on the provisions of the By-laws.

Also in compliance with the provisions issued by CONSOB with Notice DEM/125564 dated April 6, 2001 and subsequent updates, the following was carried out:

- We monitored that the Law and the By-laws were complied with.
- We attended the meetings of the Board of Directors and specific preparatory meetings regarding the items on its agenda, including the meetings of the Internal Control Committee and of the Remuneration Committee and were regularly informed by the Directors about the activities carried out, expected outlook and the most significant economic, financial and equity transactions of the Company, and we were satisfied that the resolutions adopted and implemented were in compliance with Law provisions and the By-laws and were not manifestly imprudent, risky, representing a potential conflict of interests, in contrast with the resolutions passed by the shareholders meeting or capable of compromising the Company's assets. During the assessments, no atypical and/or unusual operation emerged.

- The Board of Directors on its meeting on March 20, 2012, with the favorable opinion of the Human Resource and Remunerations Committee, has proceeded to approve the "*Annual Remunerations Report*" prepared, in accordance with Art. 123-ter of Legislative Decree no. 58/1998 and in compliance with the provisions of Art. 7 of the Self-Regulatory Code of Borsa Italiana.
- In the chapter "*Related-party transactions*" included into the Notes to the Consolidated and Separate financial statement, the directors highlighted the principal transactions that were conducted with related parties, identified on the basis of the international accounting standards and on the provisions issued on the matter by CONSOB. This chapter can be referred to, to identify the type of transactions and relative economic, financial and equity effects. The Board has also monitored the application of the "*Related party transactions procedure*", pursuant to Art. 4 of the Regulation adopted by CONSOB with Resolution no. 17221 of March 12, 2010 as subsequently amended and integrated and adopted by the Board of Directors on November 12, 2010.
- The Company drew up the 2011 Separate financial statement according to the International Accounting Standards (IAS/IFRS), as was also done for the previous one in 2010. The Notes include the accounting standards and the evaluation criteria adopted. Terna S.p.A.'s 2011 Separate financial statement was submitted to the evaluation of the PriceWaterhouseCoopers S.p.A. auditing firm, appointed by the Shareholders Meeting of May 13, 2011 for the financial years running from 2011 to 2019 in lieu of the previous appointment made to the auditing firm KPMG S.p.A., which had expired with no possibility of further renewal or extension in accordance with Art. 17 of Italian Legislative Decree no. 39 of January 27, 2010, which issued its auditing report on April 18, 2012 without anything significant to report. Significant events that occurred during 2011 are included in the Directors' Report and can be examined more in detail:
  - In financial year 2011, the Terna Group continued to develop the photovoltaic project, culminating in the stipulation of the sales contract between Terna, SunTergrid and Terra Firma Investments (GP) 3 Limited, through which on March 31, 2011, the entire share capital of Rete Rinnovabile S.r.l. was transferred. The sale generated comprehensive net income of around €196 million. Additionally, in 2011 the Terna Group undertook an investment programme named "New photovoltaic

project", which on October 24, 2011 culminated with the transfer to the private equity fund Terra Firma, of 100% of the share capital of the newly-established Nuova Rete Solare S.r.l. ("NRTS S.r.l."), for a total price in terms of enterprise value, of €264 million.

- the Authority for Electricity and Gas (AEEG), by Resolutions nos. 199/11, 204/11 and 197/11, for the 2012-2015 regulation period established remuneration for the provision of electricity transmission, distribution and metering services, the prices for dispatch and the regulation of the quality of the transmission service of the fourth regulatory period (2012-2015). The Report on Operations to the 2011 consolidated financial statements provides full details of the technical contents of the Resolution.
- On March 8, 2011, Terna launched a bond issue on the market in euros, at a fixed rate, with maturity at 10 years, for a total of €1.25 billion, under the scope of its Euro Medium Term Notes (EMTN) programme. The Bond matures on March 15, 2021 with annual coupon of 4.750% and issue price of 99.245.

➢ The Company drew up the 2011 Consolidated financial statement applying the International Accounting Standards (IFRS/IAS) as it did for the previous year; the Terna Group's Consolidated Financial Statement was submitted to the evaluation of the PriceWaterHouse Coopers S.p.A. Auditing firm that issued its auditing report on April 18, 2012 without anything significant to report.

➢ We collected information and monitored, as far as our authority allowed, the adequacy of the Company's organizational structure, compliance with the principles of proper management and the adequacy of the provisions issued by the Company to the subsidiaries pursuant to Art. 114, paragraph 2 of Legislative Decree 58/98 by acquiring information from the Heads of the designated company departments, through meetings held with the Auditing firm and through meetings held with the control bodies of subsidiaries in order to mutually exchange data and significant information.

➢ We monitored the administrative and accounting system, assessing the reliability of the latter in providing a true and fair view of operations; this activity was carried out by obtaining information from the heads of the various departments, by examining company documents and analyzing results of the work carried out by the PriceWaterHouse Coopers S.p.A. auditing firm. The Board of Directors appointed the Executive in charge of "preparing the Company's accounting documents" also verifying for him the existence of the necessary professional requirements. The CEO and the Executive in charge of preparing the Company's accounting documents certified with a specific report (attached to the Company's 2011 Separate financial statement) a) compliance and effective application of administrative and accounting procedures; b) compliance of the contents of the accounting documents with the international accounting standards IFRS /IAS approved by the European Commission, as well as with the provisions issued by CONSOB implementing Legislative Decree no. 38/2005; c) compliance of the documents with the data included in the books and the accounting records and their reliability in correctly representing the Company's economic, financial and equity situation. The same type of Certification Report is attached to the Terna Group's Consolidated financial statement.

➢ We monitored the adequacy of the internal control system also through a) the examination of the report by the Executive in charge of Terna's internal control system; b) the examination of the *Internal Audit* reports, as well as the informative report on the outcomes of the monitoring activity; c) the relationships with the Supervisory Bodies of the subsidiaries pursuant to of par. 1 and 2 of Art. 151 of Legislative Decree 58/98; d) the participation in all the Internal Control Committee meetings and acquisition of related documentation. The participation to the Internal Control Committee has also allowed the Board to coordinate with the activities of the same Committee, the exercise of its functions of "Committee for internal control and auditing of accounts" pursuant to Art. 19 of Legislative Decree 39/2010 and to proceed, in particular, to supervise i) the process of financial information reporting ii) the effectiveness of the internal control, auditing and risk management systems iii) on the legal auditing of the annual and consolidated accounts iv) on the aspects related to the independence of the Auditing firm. On the basis of the activity carried out, considering the evolutionary nature of the Internal Control System, the Board expresses an evaluation of adequacy of it and acknowledges, in quality of Committee for internal control and auditing of accounts, that there are no observations to report to the Shareholders Meeting. With reference to the provisions of par. 1 of Art. 19 of Legislative Decree 39/2010, the Auditing firm has notified used hours and invoiced fees for the Auditing of the Terna S.p.A.'s Separate and Consolidate financial statement as at December 31, 2011, besides the limited auditing of the Interim financial statement, for the activities of assessment of regular accounting activities, and for the other assignments; the fees for those assignments are shown in the table below:

| Client Company | Service description | Amount |
|---|---|---|
| Terna S.p.A. | 2011 Audit of Unbundling for AEEG (including expenses) | 35,200 |
| | 2011 Audit of reporting packages (including expenses) | 17,600 |
| | 2011 Opinion for interim dividend (including expenses) | 35,200 |
| | **Total** | **88,000** |

Moreover, PriceWaterHouse Coopers has notified that, based on the best information available, taken into account prescribed and professional requirements that discipline the auditing activity, has maintained in the reference period its position of independence and objectivity towards Terna S.p.A. and that there have been no variations in the inexistence of incompatibility causes with reference to the situations and the subjects provided for by Art. 17 of the Legislative Decree 39/2010 and of the articles of which to par. I-bis (Incompatibility) of Title VI of Issuers Regulation.

➢ We held periodic meetings with the representatives of the PriceWaterHouse Coopers S.p.A. Auditing firm, pursuant to Art. 150, paragraph 3 of Legislative Decree 58/98 and no facts worthy to be mentioned in this Report emerged. We also give notice that on April 18, 2012 the Auditing firm has submitted its report, pursuant to the third paragraph of Art. 19 of Legislative Decree 39/2010, reporting that on the occasion of the auditing activities, neither fundamental issues or meaningful deficiencies in the internal control system, with reference to the process of financial information reporting, have emerged.

➢ We have monitored the actual implementation of Terna S.p.A.'s Code of Conduct adopted by the Board of Directors without noticing anything significant to be mentioned in this report. Moreover, with reference to the provisions established by the Code of Conduct which refer to the tasks of the Board of Statutory Auditors, the following should be pointed out:

- we verified the correct application of the criteria and procedures for assessing Independence, adopted by the Board of Directors, with nothing significant to report;
- with regard to the "self-evaluation" of the independence requirement of its members, the Board of Statutory Auditors verified its existence during the meeting held on February 23, 2012;
- we complied with the provisions of the regulation for managing and handling confidential and privileged company information;

Furthermore, it should be pointed out that the Auditing firm expressed its opinion regarding coherence of information pursuant to paragraph 1) letters c), d), f), l), m) and to paragraph 2, letter b), of Art. 123-bis of Legislative Decree 58/98 as indicated by the amendments introduced by Article 5, paragraph 4, of Legislative Decree 173/2008.

➢ With reference to Legislative Decree n. 231/2001, the Company adopted an organizational and management model whose contents were in compliance with the best international practices. Furthermore, we met the Supervisory Board for the mutual exchange of information.

➢ During the year, no legal actions pursuant to Art. 2408 of the Civil Code were filed and received.

➢ We do not have the knowledge of any other facts or reports to be mentioned to the Meeting.

➢ We have verified compliance with the laws regarding the drawing up of the Group's draft Separate financial statement and of the Group's draft Consolidated financial statement, of the respective Illustrative Notes and the Directors' Report, directly and with the collaboration of the Heads of departments and through information obtained by the Auditing firm, and we have nothing significant to report.

➢ We have issued our opinions pursuant to Art. 2389, paragraph 3 and Art. 2386, paragraph one of the Civil Code; the Auditing firm issued its opinion pursuant the provisions of paragraph 5 of Art. 2433-bis of the Civil Code (interim dividends).

➢ The members of the Board of Statutory Auditors have complied with the obligation to notify administration and control assignments in Italian companies within deadlines and by means provided for by Art. 148-bis of Legislative Decree of February 24, 1998 no. 58 and by Art. 144-*duodecies* and following of the so-called Issuers Regulation adopted by CONSOB with Resolution no. 11971 of May 14, 1999.

- In carrying out the above-mentioned monitoring activity, during 2011, the Board of Statutory Auditors met 10 times, attended the 10 meetings of the Board of Directors and participated in the 4 meetings of the Internal Control Committee and in the 5 meetings of the Remuneration Committee.

During the above-mentioned activity, as well as on the basis of the information periodically exchanged with the PriceWaterHouse Coopers S.p.A. Auditing firm, no omissions and/or reproachable facts and/or irregularities were found that required reporting to the control bodies or that were worthy to be mentioned in this Report.

The Board of Statutory Auditors, following the monitoring activity carried out, requests your approval of the financial statement as of December 31, 2011 in compliance with the proposal of the Board of Directors.

Rome, April 19, 2012

THE STATUTORY AUDITORS

Luca A. Guarna

Lorenzo Pozza

Alberto Gusmeroli

pwc

**AUDITORS' REPORT IN ACCORDANCE WITH ARTICLES 14 AND 16 OF LEGISLATIVE DECREE NO. 39 OF 27 JANUARY 2010**

To the Shareholders of
Terna SpA

1 We have audited the separate financial statements of Terna SpA as of 31 December 2011 which comprise the statement of financial position, the separate income statement, the statement of comprehensive income, the statement of changes in equity, the statement of cash flows and the related notes. The directors of Terna SpA are responsible for the preparation of these financial statements in accordance with the International Financial Reporting Standards, as adopted by the European Union, and with the regulations issued to implement article 9 of Legislative Decree No. 38/2005. Our responsibility is to express an opinion on these separate financial statements based on our audit.

2 We conducted our audit in accordance with the auditing standards recommended by Consob, the Italian Commission for listed Companies and Stock Exchange. Those standards require that we plan and perform the audit to obtain the necessary assurance about whether the separate financial statements are free of material misstatement and, taken as a whole, are presented fairly. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the directors. We believe that our audit provides a reasonable basis for our opinion.

The separate financial statements of the prior year are presented for comparative purposes. As disclosed in the notes to the separate financial statements, the directors have reclassified certain comparative information related to prior year, compared to information previously presented and reviewed by other auditors, which issued their report dated 18 April 2011. We have examined the methods adopted to reclassify the comparative information of the prior year and related disclosure included in the notes to the separate financial statements for the purpose of issuing the audit opinion on the separate financial statements as of 31 December 2011.

3 In our opinion, the separate financial statements of Terna SpA as of 31 December 2011 comply with the International Financial Reporting Standards, as adopted by the European Union, and with the regulations issued to implement article 9 of Legislative Decree No. 38/2005; accordingly, they have been prepared clearly and give a true and fair view of the financial position, result of operations and cash flows of Terna SpA for the year then ended.

***PricewaterhouseCoopers SpA***

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4 The directors of Terna SpA are responsible for the preparation of the report on operations and the report on corporate governance and ownership structure in accordance with the applicable laws and regulations. Our responsibility is to express an opinion on the consistency of the report on operations and of the information referred to in paragraph 1, letters c), d), f), l), m), and paragraph 2, letter b), of article 123-bis of Legislative Decree No. 58/98 presented in the report on corporate governance and ownership structure, with the financial statements, as required by law. For this purpose, we have performed the procedures required under Italian Auditing Standard 1 issued by the Italian Accounting Profession (Consiglio Nazionale dei Dottori Commercialisti e degli Esperti Contabili) and recommended by Consob. In our opinion, the report on operations and the information referred to in paragraph 1, letters c), d), f), l), m) and paragraph 2, letter b), of article 123-bis of Legislative Decree No. 58/98 presented in the report on corporate governance and ownership structure are consistent with the separate financial statements of Terna SpA as of 31 December 2011.

Rome, 18 April 2012

PricewaterhouseCoopers SpA

Signed by

Paolo Caccini
(Partner)

*This report is an English translation of the original audit report, which was issued in Italian. This report has been prepared solely for the convenience of international readers.*

2011

# Report on Corporate Governance and Ownership Structure

(traditional administration and management model)

Issuer: «Terna – Rete Elettrica Nazionale Società per Azioni» (in brief Terna S.p.A.)
Website: www.terna.it
Reporting period: 2011
Date of approval: March 20, 2012

Terna

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# Report on Corporate Governance and Ownership Structure 2011

## Foreword

As of 2006, Terna has adopted the new Corporate Governance Code for listed companies published by Borsa Italiana in March 2006 and already since 2007 has approved the updates to the Corporate Governance system in place within the Company to meet its commitments arising therefrom, that were implemented also with respect to the updates of the Governance Code published in March 2010, and up to the approval date of the 2011 draft Financial statements, as illustrated here below.
Therefore, the Corporate Governance system in place at Terna is in line with the principles of the March 2006 edition of the Governance Code, updated in March 2010 (hereinafter "Governance Code"), with CONSOB recommendations in this respect and, more generally, with international best practices.
This Corporate Governance system is mainly based on creating value for shareholders, taking into account the social meaning of the Group's activities and the resulting need to adequately consider all stakeholders in the performance of those activities.
Since 2004, the year the Company's shares were listed on the Italian Stock Exchange, Terna provides, with an appropriate annual Report, information regarding the development of its Corporate Governance system with respect to the provisions of the Governance Code.
Furthermore, already as part of the annual report for 2008, Terna provides with its report on Corporate Governance a special section where it provides the information envisaged in Article 123-bis of Legislative Decree no. 58/98 (Consolidated Law on Finance).
This Report on the corporate governance was drafted - taking into account the indications by Borsa Italiana with the support of Assonime - also with the specific references in the provisions of the Consolidated Law on Finance and supplemented with an appropriate attachment that illustrates the main characteristics of the existing risk management and internal control systems with regard to the financial informative note.
Failure to comply with certain provisions of the Governance Code is explained in the section of the report that concerns the relative practice of governance otherwise applied by the Company.
All the information included in the report, unless otherwise specified, was updated on the basis of information available as of the date of the Report's approval.
With regard to amendments to the Governance Code published in December 2011 by the Corporate Governance Committee promoted by Borsa Italiana, ABI, Ania, Assogestioni, Assonime and Confindustria, this Report supplies information that the Committee deems must be provided during 2012 with respect to succession plans of executive directors. Information on acceptance of the remaining provisions of the 2011 edition of the Governance Code will be given in subsequent fiscal years based on the timetable for the adjustments provided for by the transitional rule. Therefore, all references to the recommendations of the Governance Code, if not otherwise specified, must be construed as referring to the Governance Code of listed companies published by Borsa Italiana in 2006, as amended in March 2010.

## Section I **Issuer's profile - Corporate structure**

### Issuer's profile

#### Mission

"Terna is a major electricity transmission grid operator. It provides services under concession agreements and ensures safety, quality and cost effectiveness over time. It ensures equal conditions of access to all grid users.
It develops market activities and new business opportunities with the experience and technical skills gained in the management of complex systems. It creates value for the shareholders with a strong commitment to professional best practices and with a responsible approach to the community, respecting the environment in which it operates."

#### Social Responsibility

Terna manages all its activities focusing on their possible economic, social and environmental consequences and in adopting a sustainable approach to business, has identified a method for creating, maintaining and consolidating a relationship of mutual trust with its stakeholders, that is useful for the creation of value for the Company, society and the environment.

Terna's main orientation for Social Responsibility can be found in the Code of Ethics and in the Company's mission, and entail defining its concrete and measurable responsibilities and objectives in economic, environmental and social areas, in addition to the one specific to Terna, that of responsibility for the electricity service.
From the point of view of sustainability, respect for the environment is particularly important. The physical presence of pylons, electricity lines and stations which interact with the landscape and biodiversity represent indeed the most significant impact of Terna's activities. That is why Terna has chosen the approach of negotiation and coordination with Local Authorities, also involving potentially significant stakeholders such as the main environmentalist associations to take environmental needs into consideration from the early stages of planning new lines. Terna has also developed a management system to control and limit the environmental impact of its activities. Thus, consideration of environmental issues matches the Company's interest in implementing grid development investments and in the more general interest of community for a reliable, inexpensive and environmentally safe electricity system.
The results of this management approach, oriented towards continuous improvement through the definition of economic, social and environmental responsibility objectives are presented in the Sustainability Report, indicated by the Code of Ethics as an instrument to give the stakeholders an account of the degree of implementation of its undertakings, and published yearly since 2006.
For its Sustainability Report, Terna adopts the international standard G3-Sustainability Reporting Guidelines of the Global Reporting Initiative (GRI), a leading global organization that develops guidelines on reporting sustainability, and then submits it for analysis to an external auditor and to the Board of Directors for approval.
Since the 2009 edition, the Sustainability Report has obtained an A+, the highest level provided for by the GRI standard, for transparency and completeness of information.
Among the main 2011 results for CSR it is worth mentioning:
- completion of environmental mitigation and compensation measures in three WWF Oases, which represent the first implementation of the action plan for the sustainable development of the National Transmission Grid (NTG) provided for in the strategic partnership agreement signed in 2009 between Terna and the WWF;
- the signing of a Memorandum of Understanding with Legambiente in order to promote a culture of energy sustainability that combines the development of the electricity systems with that of renewable resources. Terna and Legambiente undertake to foster and spread awareness of the world of energy and to mutually take action for an environmentally sustainable energy transfer, starting with the reduction of $CO_2$ emissions in the atmosphere;
- the fine tuning of guidelines for energy efficiency of Terna's buildings;
- the adaptation of monitoring instruments, as provided for by the LBG - The London Benchmarking Group methodology, for use in the Italian context and for Terna's specificities, in order to be able to completely measure contributions (in terms of money, work and in kind) for community initiatives and the actual consequent social results;
- the definition of rules for planning, carrying out and monitoring the free transfer of company equipment and devices - no longer needed by Terna, but still useful - to non-profit organizations for implementing solidarity projects in Italy and abroad.

Recognition of Terna's commitment to continually improve its economic, environmental and social performance has led to its inclusion in an increasing number of stock exchange sustainability indexes.
In 2011, Terna was present in all the main international stock exchange sustainability indexes, such as the Dow Jones Sustainability Index (World and Europe), and was included in the new STOXX Global ESG Leaders indexes, being present - the only Italian utility company - in all the relative sub-indexes specialized in environmental, social and governance fields (STOXX Global Environmental Leaders, STOXX Global Social Leaders and STOXX Global Governance Leaders).

## Company organization

In compliance with the provisions of the Italian legislation concerning listed companies, the Company's organization - based on the traditional administration and management model - includes the following:
- a Board of Directors responsible for the Company management. To such aim, the Board is entrusted with the widest powers so as to complete all the actions that deems appropriate for the performance and the attainment of the Corporate purpose, excluding only the action that the Law and the Bylaws reserve to the Shareholders' Meeting;
- a Board of Statutory Auditors responsible for monitoring: (i) that the Company complies with the Law, the Bylaws and the principles of correct administration in performing Company activities, (ii) the adequacy of the Company's organizational structure, Internal Control System and administrative/accounting system as well as those of the foreign subsidiaries outside of the EU. It is also responsible for carrying out all duties assigned to the Board of Statutory Auditors by Law and by the Governance Code; according to Article 19 of Legislative Decree 39/2010, it is the responsibility of the Board of Statutory Auditors to supervise the financial information process, the efficiency of the internal control systems, of internal reviews and risk management, the auditing of annual and consolidated results pursuant to law provisions and the independence of the auditing company.
- the Shareholders' Meeting – ordinary and extraordinary – that resolves upon, inter alia, (i) the appointment and revocation of members of the Boards of Directors and Statutory Auditors and their fees and duties, (ii) the approval of the Financial statements and allocation of the profits for the year, (iii) the purchase and sale of treasury shares, (iv) amendments to the Bylaws, and (v) the issuance of convertible bonds; (vi) authorizations for actions carried out by Directors concerning

Transactions with Related Parties for which there was no favorable opinion by the competent independent body, in compliance with governing regulations and based on procedures adopted by the Board of Directors as well as on urgent transactions submitted by the Directors to an advisory vote of the Shareholders' Meeting, and (vii) during consultations pursuant to Article 123 ter, paragraph 6 of the Consolidated Law on Finance, on Company Policy on matters of remuneration of members of administration bodies, of general directors and of executives with strategic responsibilities;
- an Executive in Charge of the preparation of the Company's accounting records, who is given all assignments and responsibilities provided by the Law and regulations as well as those provided for by the Governance Code (Article 8.C.3).

Statutory auditing activities are entrusted to a specialized company enrolled in a specific register, which is appointed by the Shareholders' Meeting on proposal by the Board of Statutory Auditors.
Terna's Auditors also have similar engagements with the Company's main subsidiaries.
It has been some time since the Organizational Model adopted by the Company pursuant to Legislative Decree no. 231/01 - which was recently updated based on the provisions of Legislative Decree 39/2010 - has provided that the auditing of the Company's Financial statements and that of any company of the Group and of the Consolidated financial statements is not compatible with consultancy activities for Terna or any company of the Group, extending to all network of the audit company as well as to shareholders, Directors, members of control bodies and employees of the audit company and of the other companies belonging to the same network. The assignments to the audit company are submitted to Terna's Internal Control Committee for any assignment other than the one given under Law provisions, in any event related to auditing activities. In order to ensure independence of the company and of the officer in charge of auditing, the assignment for the auditing of the Company's Financial statements and that of any company of the Group and of the Consolidated financial statements is not in any case given to audit companies that fall within one of the incompatibility situations pursuant to Article 17 of Legislative Decree no. 39/2010 and to Part III, Title VI, paragraph I-bis of the "Regulations implementing Legislative Decree no. 58 dated February 24, 1998, regarding the law on issuers" adopted by CONSOB (Issuer Regulations).

The Shareholders' Meeting held on May 13, 2011 approved the amendments to Articles 9.1 and 13 of the Company Bylaws for adapting, respectively, the provisions introduced by Article 1 of Legislative Decree no. 27 dated January 27, 2010 and for implementing the Procedure on Transactions with Related Parties pursuant to "Regulation containing provisions concerning transactions with related parties" (adopted by CONSOB with its resolution no. 17221 dated March 12, 2010 and subsequently amended by resolution no. 17389 dated June 23, 2010). The primary amendments regard: (i) the possibility for the Board of Directors to exercise the right to convene a Shareholders' Meeting on a single date, in place of the traditional first, second and (in the case of extraordinary Shareholders' Meetings) third calls; and this without prejudice to the rule, which then became residuary, for multiple calls, if the Board decided not to exercise said right; (ii) the introduction into the Bylaws of the provisions necessary to attribute full effectiveness to the "Procedure on Transactions with Related Parties" adopted by Terna according to the provisions in "Regulations containing provisions concerning transactions with related parties" adopted by CONSOB.

## Section II **Information on ownership structure (pursuant to Article 123-bis, paragraph 1 of the Consolidated Law on Finance)**

### Share capital structure (pursuant to Article 123-bis, paragraph 1, letter a) of the Consolidated Law on Finance)

The Company's share capital as of March 20, 2012 amounts to €442,198,240.00 and comprises exclusively nominal ordinary shares, for a total of 2,009,992,000 ordinary Terna's shares with a nominal value of €0.22 each. They are fully paid-up and bear voting rights at both the ordinary and extraordinary Shareholders' Meetings. Ordinary shares grant further administrative and financial rights provided for by the Law regulating the shares with right to vote.
As of June 23, 2004, Terna's shares have been listed in the Electronic Stock Exchange organized and managed by Borsa Italiana S.p.A. (Telematic Share Market - Blue Chip segment).
Pursuant to Article 5.2 of the Company Bylaws, the Shareholders' Meeting can approve capital increases through share issuance, also belonging to special categories, to be assigned free of charge pursuant to Article 2349 of the Italian Civil Code for employees, or rather as payment, and with the exclusion of the option right under Article 2441 of the Civil Code, in favor of subjects identified by shareholders.
In compliance with this provision of the Company Bylaws, the Shareholders' Meeting held on April 1, 2005 resolved only one share-based incentive plan that was utilized in full in 2011 and that included increasing the share capital according to the provisions in the subsequent paragraph "Powers to increase the share capital and authorizations for the purchase of treasury shares".
The Company did not issue other financial tools granting the right to subscribe newly issued shares.
Terna did not issue shares that were not negotiated on regulated markets of a country in the EU.

## Significant interests participations in share capital and shareholders agreements (pursuant to Article 123-bis, paragraph 1, letters c) and g) of the Consolidated Law on Finance)

On the basis of the shareholders' book, communications received pursuant to CONSOB Resolution no. 11971/99 and available information, and with reference to the Company's share capital as of March 20, 2012, equal to €442,198,240.00 for a total of 2,009,992,000 ordinary Terna's shares with a nominal value of €0.22 each, the following investors hold more than 2% of the share capital: Cassa Depositi e Prestiti S.p.A. (public limited company in which the Italian Ministry of Economy and Finance of the Italian Republic owns 70%), with 29.851% of the share capital; Romano Minozzi (directly and indirectly) with 5.580% of the share capital; BlackRock Inc. (through management company BlackRock Group, for savings management ) with 2.390% of the share capital.
No other investors own more than 2% of Terna S.p.A.'s share capital and the Company is not aware of the existence of any shareholders' agreement relating to the Company shares.

## Powers to increase share capital and authorization for the purchase of treasury shares (pursuant to Article 123-bis, paragraph 1, letter m) of the Consolidated Law on Finance)

The power granted to the Board of Directors to increase the share capital resolved by the extraordinary Shareholders' Meeting held on April 1, 2005 was exercised through the adoption of a share-based incentive plan aimed at Terna Group's executives and in force from 2006 up to its complete exhaustion, which took place in 2011, with the exercising of all the Stock Options still in circulation.
The abovementioned Stock Option plan brought about an increase in the share capital of € 2,198,240.00 through the issuance of 9,992,000 new ordinary Terna's shares, each with a nominal value of €0.22.
It should be remembered that the extraordinary Shareholders' Meeting of April 1, 2005 had resolved the assignment of a five-year proxy to the Board of Directors for a share capital increase for maximum €2,200,000 through the issuance of maximum 10,000,000 ordinary shares with a nominal value of €0.22 each, on a dividend-right basis, to be offered for subscription to Terna Group's managers as payment with exclusion of the option right under the combined provisions of Article 2441, last paragraph, of the Civil Code and Article 134, paragraph 2 of the Consolidated Law on Finance, as provided for by Article 5.3 of the Company Bylaws.
Pursuant to the Shareholders' Meeting resolution of April 1, 2005, on December 21, 2005, Terna's Board of Directors had adopted a share-based incentive plan. With reference to the adopted plan, the Board of Directors of March 21, 2007 had partially exercised the abovementioned proxy, approving a share capital increase regarding the 2006 Stock Option Plan up to maximum €2,198,240.00 through the issuance of maximum 9,992,000 new ordinary Terna's shares with a nominal value of €0.22 each, at €2.072 each, to be implemented in compliance with Article 5.4 of the Bylaws. Based on extraordinary Meeting resolution dated April 22, 2009, the maximum date for the total subscription of the increase was set for March 31, 2013.
No other proxies to increase capital have been assigned, pursuant to Article 2443 of the Civil Code.
No resolution authorizing the purchase of treasury shares under Article 2357 and following of the Civil Code has been submitted to Terna's Shareholders' Meeting.
Terna does not own, nor has purchased or sold during the year, not even indirectly, treasury shares or shares of its parent company.

## Employees' shareholding: system to express the right to vote (pursuant to Article 123-bis, paragraph 1, letter e) of the Consolidated Law on Finance)

The system for expressing the right to vote during the Shareholders' Meeting through shareholding associations, including employee's shareholding groups, is regulated based on the existing specific legal provisions on the subject.
Based on the provisions regarding the special legislation on listed companies, Terna's Bylaws introduced a special provision aimed at facilitating collecting voting proxies with its employees' shareholding groups as well as of its subsidiaries, encouraging in this way the relative involvement in the meeting decision-making processes (Article 11.1 of the Bylaws).
As of March 20, 2012 the Company had not received any notification of the establishment of employees' shareholding groups.

## Change of control clauses (pursuant to Article 123-bis, paragraph 1, letter h) of the Consolidated Law on Finance) and statutory provisions in takeover bid matters (ex Article 104, paragraph 1 ter, and 104 bis, paragraph 1 of the Consolidated Law on Finance)

As regards significant agreements Terna or any of its subsidiaries are parties of and that come into effect, are amended or expire in the event of shareholding change within Terna, the following should be noted.
The loan contracts stipulated with the European Investment Bank (EIB) include mandatory advance repayment clauses in the event the Company proceeds to or is involved in a merger, a split or transfer of a Company branch. Should such events occur, the EIB will have the power of requesting, and the Company will have the obligation to inform the Bank, any

information that the latter may reasonably require regarding the Company situation, in order to understand any changes and relative consequences in the Company's commitments towards the Bank. In such cases, should the EIB deem, according to its indisputable judgment, that these transactions may have negative consequences on the commitments undertaken by the Company, the bank itself will have the power to request the necessary changes in the loan contracts or alternative solutions that satisfy the Bank itself, such as early reimbursement of the loan.

With regard to takeover bids and public tender offers to exchange, the Company Bylaws do not provide for any derogation of the provisions in the Consolidated Law on Finance on the so-called passivity rule provided for by Article 104, paragraphs 1 and 1 bis of the Consolidated Law on Finance, nor are there neutralization rules as established Article 104 bis, of the Consolidated Law on Finance, without prejudice to - pursuant to Article 104 bis, paragraph 7 of the Consolidated Law on Finance - law and statutory provisions regarding special powers as provided for in Article 2 of Law Decree no. 332 dated May 31, 1994 converted with amendments by Law no. 474 dated July 30,1994, with subsequent modifications and amendments – the so-called "Law on Privatization", and concerning limits on share possession and the right to vote pursuant to Article 3 of the same Law Decree.

### Restrictions on share transfer and shares bearing special rights (pursuant to Article 123-bis, paragraph 1, letters b) and d) of the Consolidated Law on Finance)

No Bylaws limitations exist to the availability of shares except for the provisions stated by the Bylaws regarding rules for privatization based on the Law Decree no. 332 dated May 31, 1994 converted with amendments by Law no. 474 dated July 30, 1994 and subsequent changes – the so called "Privatization Law".

In particular, pursuant to Italian regulations concerning privatizations, Terna's Bylaws provides for the possibility for the Government to exercise certain "special powers" and establishes a "maximum limit of share ownership" – equal to a direct and/or indirect ownership of Terna's shares for more than 5% of the share capital – for subjects other than the Italian Government, state-controlled companies and entities subject to either control: the implementation of those provisions, in some circumstances as indicated by the Bylaws, has effects also on the voting right.

"Special powers" (indicated by Article 6.3 of the Bylaws, pursuant to Article 2, paragraph 1, of Legislative Decree no. 332 of May 31, 1994, converted with modifications by Law no. 474 of July 30, 1994 and following integrations and amendments – so-called "Privatization Law" – as provided for by Article 4, paragraph 227, of Law no. 350 of December 24, 2003) can be exercised by the Italian Government, represented in this case by the Ministry of Finance and Economy, notwithstanding the number of Terna's shares potentially owned by the Ministry itself.

In particular, the Ministry of Finance and Economy, as agreed with the Ministry of Productive Activities (now called Ministry for Economic Development), is assigned the following "special powers":

a) opposition to relevant ownership (that is equal or higher than 1/20th of Terna's share capital formed by shares bearing right to vote in Shareholders' Meetings) by entities subject to the ownership restriction presented above. The opposition must be expressed within 10 days from the date of the communication, which must be made by Directors at the request of subscription in the shareholders' book, only when this may jeopardize the vital public interest. In the meantime, the right to vote and non-financial rights related to shares representing the relevant ownership, are suspended;

b) opposition to shareholder agreements under the Consolidated Law on Finance, in case at least 1/20th of Terna's share capital, including shares bearing right to vote at Shareholders' Meetings, is thereby represented. Opposition must be expressed within 10 days from the date of communication that must be made by CONSOB. In the meantime, the right to vote and non-financial rights related to shares of shareholders that are parties of the agreements, are suspended;

c) veto, dutifully motivated, in relation to concrete jeopardy of the vital public interest, to the adoption of provisions for the winding-up of the Company, of transfer, merger, division, moving abroad of the registered offices, of Company Corporate purpose change, of Bylaws amendments suppressing or modifying powers indicated by the same Article 6.3 of the Bylaws;

d) appointment of one Director with no right to vote. In case of termination of the assignment of the appointed Director, the Ministry of Economy and Finance, in agreement with the Ministry for Productive Activities (now called Ministry for Economic Development), will appoint the substitute.

The power of opposition under letters a) and b) can be exercised with reference to each aspect. It can also be exercised when ownership, also through single purchase acts, records an increase which is equal or higher than expectations. Such power can also be exercised every time the need to protect mandatory public interest arises, within ten days from their actual occurrence. In this case, the act of exercising the State power must include explicit and motivated reference to the date such causes arose.

The special powers under letters a), b), c) and d) are exercised with respect of the criteria provided for by the Prime Minister Decree of June 10, 2004.

The "maximum limit of share ownership" (provided for by Article 6.4 of the Bylaws and pursuant to Article 3 of Legislative Decree no. 332 of May 31, 1994, converted with modifications by Law no. 474 of July 30, 1994 and following amendments and additions ("Privatization Law") is calculated also considering total share ownership related to the Parent Company, natural person or legal entity or company; to all direct and indirect subsidiaries as well as the subsidiaries under the same

controlling subject; to all associated subject as well as to natural persons bound by parental or affinity relationships up to second grade and by marriage, in the event that husband/wife are not legally separated. Control occurs, also with reference to subjects other than companies, in cases provided for by Article 2359, paragraphs 1 and 2, of the Civil Code. Association occurs in cases under Article 2359, paragraph 3, of the Civil Code, as well as between subjects who, directly and indirectly, through subsidiaries other than those managing common investment funds, join, also with third parties, agreements related to the exercise of the right to vote or to the transfer of shares or portions of third companies or, anyway, to agreements or pacts as per Article 122 of the Consolidated Law on Finance, with reference to other companies, if these agreements or pacts refer to at least 10% of the share capital with right to vote, in case of listed companies, or 20% in case of non-listed companies. With reference to the calculation of the abovementioned limit of share ownership (5%), shares owned through trustees and/or through a third person and, generally, through an intermediary person are also considered.
Such limit of share ownership terminates, if exceeded due to a takeover bid carried out under articles 106 or 107 of the Consolidated Law on Finance.
The right to vote related to share ownership exceeding the abovementioned maximum limit cannot be exercised and proportionally reduces the right to vote of each subject to whom the limit in share ownership refers to, except in the event of joint communications by the involved shareholders. In case of non-compliance, decision can be appealed under Article 2377 of the Civil Code if the requested majority would not be achieved without the votes exceeding the abovementioned limit. Shares for which the right to vote cannot be exercised are calculated anyhow for the regular formation of the Shareholders' Meeting.

### Voting Restrictions (pursuant to Article 123-bis, paragraph 1, letter f) of the Consolidated Law on Finance)

Pursuant to privatization regulations, restrictions exist (under articles 6.3 and 6.4 of the Bylaws) to the right to vote related to the exercise of "special rights" of the Italian State and to the limits of share ownership as mentioned earlier.
Further restrictions are applied to operators of the electricity sector (as provided for by Article 3 of the Prime Minister's Decree dated May 11, 2004 as regards "criteria, modalities and conditions for the unification of ownership and management of the National Electricity Transmission Grid") for which a limit equal to 5% of the share capital was established for exercising the right to vote in case of Directors' appointment (Article 14.3, letter e) of Company Bylaws).

### Appointment and substitution of Directors and Bylaws amendments (pursuant to Article 123-bis, paragraph 1, letter l) of the Consolidated Law on Finance)

#### Appointment, requirements and term of office of Directors

Terms for appointing members of the Board of Directors are ruled by Article 14 of the Bylaws.
As determined by the Shareholders' Meeting, the Board of Directors is made up of seven to thirteen members (art 14.1 of the Bylaws), who are appointed for a period not longer than three years and they may be reappointed at the end of their term. Another Director without voting right may be appointed by the Italian Government, pursuant to privatization regulations; up to now, the Italian Government never exercised the power of appointment.
The Chairman is appointed by the Shareholders' Meeting among the members of the Board (Article 16.1 of Bylaws and Article 2380-bis, paragraph 5 of the Civil Code): in case of impossibility, by the Board itself. The Board can appoint a Deputy Chairman. In no case such positions can be held by the Director appointed by the Italian Government under the Privatization Law (Article 16.1 of the Company Bylaws).
The appointment of the entire Board of Directors takes place – in compliance with the privatization regulation, under Prime Minister's Decree of May 11, 2004 and in compliance with the provisions of the Italian Law for listed companies – according to the mechanism of the "list voting", aiming at guaranteeing the presence in the management body of members designated by minority shareholders equal to 3/10th of the Directors to be appointed with rounding, in case of lower fractional number to the unit, to the following unit (Article 14.3 of the Bylaws).
On October 18, 2010, Terna's Board of Directors approved the amendments to the Bylaws necessary for adjusting the Company Bylaws to the novelties introduced by law provisions regarding shareholders' rights of listed companies aiming at favoring the participation of shareholders in the life of the Company (Directive 2007/36/EC and relative implementing Legislative Decree no. 27 dated January 27, 2010). Among other things, amendments involved Article 14.3 of the Bylaws regarding the appointment procedure for the Board of Directors and the terms and modalities for depositing the lists.
Such amendments were applied for the first time on occasion of the Meeting which was held on May 13, 2011 that resolved the renewal of the company bodies which had expired.
On the basis of the provisions and references in the Bylaws, the deposit and publication of lists are ruled by existing applicable laws.
Such appointment system – which does not apply to the appointment of a Director indicated by the Italian Government – states – in line with the provisions of Article 4, paragraph 1 bis of Legislative Decree no. 332 dated May 31, 1994 converted into Law no. 474/94 (so called "Privatization Law") and modified by Legislative Decree no. 27 dated January 27, 2010, by Article 147 ter of the Consolidated Law on Finance and by the implementing regulations of the abovementioned law

provisions included in articles 144 ter and following of the Issuer Regulations – establishes that the lists of candidates can be submitted by the outgoing Board of Directors or by shareholders who, alone or with other shareholders, represent at least 1% of the share capital as provided for by the law – or a lower amount, as established by the law, of the shares with voting right in the Meeting. On this matter CONSOB, implementing the provisions of Article 147 ter of the Consolidated Law on Finance and of articles 144 ter and following of the Issuer Regulations - with Resolution no. 17633 dated January 26, 2011 and for the year ended on December 31, 2010 - established the participation stake necessary for submitting candidate lists for the appointment of Terna's administration and control bodies at 1% of the share capital, taking into account the Company's capitalization, floating capital and owned assets and without prejudice to the lower share contemplated by the Bylaws.

The lists must be submitted and filed at least 25 days prior to the day set for the Shareholders' Meeting on first call.

Ownership of the minimum share required to submit lists shall be determined by taking into account the shares that are registered in the name of the Shareholder(s) on the day in which the lists are filed with the Company.

In order to prove the legitimacy of presentation of the lists, entitled Shareholders must present and/or deliver the documentation proving the ownership of the number of shares required, even after the lists have been filed but within the time period set for the publication of the lists (i.e., at least 21 days prior to the day set for the Shareholders' Meeting on first call).

Each Shareholder may present or assist in the presentation of one single list and each candidate may be on one list only or he will be considered ineligible.

The lists must indicate candidates according to a progressive number and which of them are in possession of the independence requirements as provided for by the law and the Bylaws, and any other information or statement required by the applicable rules and regulations and the Bylaws pertaining to their respective offices.

Together with each list, a statement shall be filed, whereby individual candidates accept their candidature and represent, under their responsibility, the inexistence of any of the causes for ineligibility and incompatibility, as well as any other information required by the applicable rules and regulations and the Bylaws.

On the basis of a clause in the notice of call for the Meeting and pursuant to Article 6 of the Governance Code, together with the lists, a detailed description of the candidates' personal and professional characteristics must be provided, accompanied by a statement indicating as to whether or not the candidates qualify as independent according to Article 3 of the Governance Code.

It is also provided that the lists, together with the information on the characteristics of candidates, are made available to the public at the registered office, on the Company's website and based on other modalities as provided for by CONSOB, at least 21 days before the Shareholders' Meeting - guaranteeing a transparent procedure for the appointment of the Board of Directors as recommended by Article 6.C.1 of the Governance Code.

According to the provisions of Article 147-ter, paragraph 3 of the Consolidated Law on Finance, at least one of the members of the Board of Directors should be appointed by the minority list that has obtained the highest number of votes and is not connected in any way, not even indirectly, with the members who have submitted or voted the list that won for a number of votes. Shareholders that submit a "minority list" are the recipients of CONSOB Communication no. DEM/9017893 dated February 26, 2009 having as its subject "Appointment of the members of administration and control bodies".

In compliance with the provisions of Prime Minister's Decree dated May 11, 2004, the Bylaws envisages for operators of the electricity sector a limit equal to 5% of the share capital as regards the exercise of the voting right during the appointment of the Directors according to the abovementioned rules.

Any replacement of Directors will be carried out pursuant to Article 2386 of the Civil Code.

In any case, the replacement of Directors whose office has ended will be carried out by the Board of Directors guaranteeing the presence of the necessary number of Directors in possession of the requirements of independence established by the Law and by Article 15.4 of the Bylaws.

If the majority of the Directors appointed by the Shareholders' Meeting is not reached, the entire Board of Directors is considered as having resigned and the Shareholders' Meeting must be called without delay by the Directors still in office for appointing a new Board.

The Director must meet the requirements of integrity, professionalism and independence.

The Company's Directors must meet certain integrity and professionalism requirements, similar to those required by the Statutory Auditors of listed companies (Article 15.2 of the Bylaws). The appointed Directors must communicate without hesitation the loss of requirement as per current regulations and according to the Bylaws to the Board of Directors, as well as any possible cause of ineligibility or incompatibility (Article 14.3 of the Bylaws).

As regards the requirements of professionalism, the Bylaws (Article 15.3) provides that those who have not accrued experience of at least three years cannot be appointed as Director and, if so, they must resign:

- activities of administration, control or management in companies having a share capital not lower than €2 million; or
- professional activities or university teaching in legal, economic, financial and technical-scientific subjects and closely related to the activities of the Company as defined in Article 26.1 of the Bylaws; or
- managing roles in public bodies or public authorities in the finance and insurance fields or, however, in fields closely related to that of the Company, as defined by the Article 26.1 of the Bylaws (subjects such as business law, tax law, business economy and finance, as well as subjects linked to energy in general, the network communications and structures, are to be considered as closely related to the Company's scope of activities).

With stricter application compared to the provisions of Article 147-ter paragraph 4 of the Consolidated Law on Finance, at least 1/3rd of the Directors in force must also be in possession of specific requirements of independence under Article 15.4 of the Bylaws that recalls the requirements of the Auditors indicated by Article 148, paragraph 3 of the Consolidated Law on Finance; furthermore, in line with the provisions of Article 3 of Prime Minister's Decree dated May 11, 2004, Executive Directors, taking into account the specific activity carried out by the Company, can be applied the independence requirements established by Article 10 of Directive 2003/54/EC as stemming from Article 15.5 of the Bylaws.
The presence of "Independent" Directors as provided for by the Governance Code becomes important in the composition of the Board Committees, as provided for by the Code itself and by the Committee for Related Party Transactions established within Terna for implementing the provisions of CONSOB Regulations that include provisions regarding related party transactions issued with Resolution no. 17221 dated March 12, 2010 and subsequently amended with Resolution no. 17389 dated June 23, 2010.
The Board of Directors assesses the presence of integrity, professionalism and independence requirements, for every one of its members and periodically assesses the presence of requirements of independence for every one of its non-executive members, on the basis of the information supplied by each member.
The Company is equipped with a specific internal procedure that defines the criteria for the assessment of independence of the non-executive members and for the assessment of the requirements necessary according to the Bylaws and the Governance Code ("Criteria of application and procedure for the assessment of independence of the Directors pursuant to Article 3 of the Governance Code"). Such procedure demands the assessment of requirements following the appointment, that is every time events take place that can interfere with the independence of a Director and however at least once a year (generally in the 30 days before the approval of the financial statements).

### Succession Plans

According to CONSOB's previous recommendation with Communication no. 11012984 dated February 24, 2011 and recently provided for within paragraph VIII of the "Guidelines and Transitional Regime" of the new edition of the Governance Code published in December 2011, it should be noted that the Board of Directors, taking into account assets owned by Terna and the concentration of ownership, did not consider any succession plans for Executive Directors.

### Bylaws Amendments

With regard to regulations applicable to the amendments of the Bylaws, the extraordinary Shareholders' Meeting resolves on the matter with the majority envisaged by the Law.
The Bylaws (Article 21.2), according to Law provisions, attributes the Board of Directors the power to adopt any resolutions pertaining to the Shareholders' Meeting that can determine Bylaws amendments such as:
a) the merger and the split, in cases envisaged by the Law;
b) the establishment or elimination of other offices;
c) stating which of the Directors represents the Company;
d) the reduction of the share capital in case one or more members withdraws;
e) the amendment of the Bylaws according to regulations;
f) the transfer of the Company headquarters in the national territory.
Article 6.3 of the Bylaws, in compliance with the regulations on privatization, attributes to the Italian Government, represented for this purpose by the Ministry of Economy and Finance, the "special power" to veto, duly motivated with reference to effective detriment of the Government's vital interests, on the adoption of a series of resolutions adopted by the Shareholders' Meeting of significant impact on the Company, capable of amending the Bylaws, as previously described in "Restrictions in share transfer and shares bearing special powers".
Furthermore, as provided for by Article 3, paragraph 3 of Legislative Decree no. 332 of May 31, 1994, converted with modifications by Law no. 474 of July 30, 1994 and Article 3, paragraph 2, letter c) of the Prime Minister's Decree dated May 11, 2004, Terna's Bylaws provides that the measures as per Article 6.4 of the Company Bylaws relative to the abovementioned "maximum limit of share ownership" as described under "Restrictions in share transfer and special powers" and those included in the Bylaws that have the purpose to ensure protection of the share minorities, cannot be modified for a period of three years from the date of effectiveness of the transfer to Terna of the activities, functions, assets and obligations relative to the management of the National Electricity Transmission Grid as per Article 1, paragraph 1 of the Prime Minister's Decree dated May 11, 2004 (November 1, 2005).

### Indemnities for Directors in case of resignation, discharge or cessation of relation following a public take-over bid (pursuant to Article 123-bis, paragraph 1, letter i) of the Consolidated Law on Finance)

With reference to the agreements entered into between Terna and the Directors that provide indemnities in case of resignation or dismissal/revocation of assignment with no just cause, following the renewal of the Board of Directors resolved by the Shareholders' Meeting held on May 13, 2011, it is pointed out that:.

a) agreements exist regarding the financial compensation recognized to Terna's CEO, who is also an employee of Terna S.p.A. as a manager, in his capacity as General Manager, on the basis of which indemnities are envisaged in case of early resignation from the appointment. No other indemnities are envisaged in case of termination of the work relation for the other members of the Board of Directors;
b) on the basis of criteria established as part of these agreements, it should be noted that the Company will pay:
    - for the administration relation pursuant to Article 2389 of the civil code, an amount equal to the total emoluments expected up to the expiration of the mandate (as agreed upon, June 30, 2014) as fixed compensation, variable compensation and severance pay –TFM- (equal to 1/12th for each year of the total emoluments received during the mandate as Director);
    - for the employment relation:
        i in the event of cessation upon the expiration of the mandate, an amount as incentive to leave, equal to 3 years compensation defined as the fixed compensation plus variable compensation (in the maximum amount provided for) and long term incentive "cash" (in the maximum amount provided for);
        ii. in the event of cessation before the expiration of the mandate (conventionally scheduled for June 30, 2014) in addition to the amount under point i), a pro rata temporis amount calculated on the fixed component until the natural expiration of the mandate, plus the variable retribution quota accrued in relation to reaching specific assigned objectives;
c) the right to the indemnity is not accrued in the case of voluntary resignation (not requested by the majority shareholder) or of revocation for a just cause;
d) within the abovementioned agreements, assigning non monetary benefits is not envisaged. Furthermore, entering consulting agreements is also not envisaged;
e) the abovementioned agreements do not include compensation for undertakings not to compete.

In the "Annual Report on Remuneration" - published by Terna in fulfillment of the provisions in Article 123 ter of the Consolidated Law on Finance and CONSOB resolution no. 18049 dated December 23, 2011 (published in the Official Journal no. 303 dated December 30, 2011) which, inter alia, introduced Article 84 quater to the Issuer Regulations – there is a summary of the information required by Article 123 bis, paragraph 1, letter i) of the Consolidated Law on Finance regarding agreements stipulated between Terna and the Directors which provide for indemnities in the case of resignation or dismissal/revocation with no just cause.

### Management and coordination

Terna is subject to the de-facto control of Cassa Depositi e Prestiti S.p.A. with 29.851% of the share capital. The assessment, from which the existence of such control emerged, has been carried out by Cassa Depositi e Prestiti S.p.A. itself and made public on April 19, 2007. As of today, no managing and coordination activity has been officialized nor exercised; Terna carries out its activity either directly or through its subsidiaries under management and negotiation independence.

It should be noted that the additional information on the Company's Corporate Governance envisaged in Article 123-bis, paragraph 2 of the Consolidated Law on Finance regarding:

- compliance, (pursuant to Article 123-bis, paragraph 2, letter a) of the Consolidated Law on Finance) are illustrated in the section of the Report specifically devoted thereto (section III);
- the principal characteristics of existing risk management and existing internal control systems in relation to the financial informative note, also consolidated (pursuant to Article 123-bis, paragraph 2, letter b) of the Consolidated Law on Finance), and further Corporate Governance practices (pursuant to Article 123-bis, paragraph 2, letter a) of the Consolidated Law on Finance) are illustrated in the section of the Report devoted to internal control system (section XI) and in Attachment 1 therein;
- the Shareholders' Meeting activity (pursuant to Article 123-bis, paragraph 2, letter c) of the Consolidated Law on Finance) in the section of the report devoted to the Shareholders' Meeting (section XVI);
- the composition and the role of the Board Members as well as those relative to the appointment and composition of the control body (pursuant to Article 123-bis, paragraph 2, letter d) of the Consolidated Law on Finance and 144 decies of the Issuer Regulations), are illustrated in the Report respectively in the section devoted to the Board of Directors (section IV) and in subsequent sections devoted to the Board Internal Committees (sections VI, VII, VIII and X) and in the sections devoted to the appointment and composition of the Board of Statutory Auditors (sections XIII and XIV).

## Section III **Compliance**

The Corporate Governance system of the Company is substantially in line with the principles included in the Governance Code of listed companies published by Borsa Italiana in March 2006 (which can be consulted in Borsa Italiana S.p.A.'s website: http://www.borsaitaliana.it) that Terna has adopted, as illustrated before, with resolution by the Board of Directors of December 21, 2006.
Further action aimed at improving the Group's system of governance are being carried out and others will be taken into consideration for the constant update and adjustment of the Terna governance system to the best practices for the Company's acceptance of the amendments to the Governance Code published in December 2011 by the Committee for Corporate Governance promoted by Borsa Italiana according to the timetable for adjustment envisaged by the transitional provision.
The Company is not subject to non-Italian laws that influence its Corporate Governance structure.

## Section IV **Board of Directors**

### Composition

In compliance with the ordinary Shareholders' Meeting held on May, 13, 2011, the Board of Directors currently in office is comprised of nine members, whose term will expire with the approval of the financial statements as of 2013.
In compliance with the Shareholders' Meeting resolution on May 13, 2011, the Board of Directors currently in office is composed of Luigi Roth, Flavio Cattaneo, Paolo Dal Pino, Matteo Del Fante, Michele Polo (Directors appointed within the majority list submitted by Cassa Depositi e Prestiti S.p.A.), Fabio Buscarini, Salvatore Machi' and Romano Minozzi (Directors appointed within the minority list submitted by shareholders Romano Minozzi and companies controlled by him).
The Directors appointed represent two of the three lists submitted for the indicated Shareholders' Meeting. Further information concerning the lists of candidates that were submitted and the results of the voting are available on the Company's website at www.terna.it in the section "Investor Relations/Corporate Governance/Shareholders' Meeting/ May 13, 2011".
Following the resignation of Director Andrea Camporese (appointed by the abovementioned Shareholders' Meeting from the majority list), the Board of Directors in its meeting on July 29, 2011, resolved to appoint by co-optation Francesco Pensato (subject to indications from the same majority shareholder Cassa Depositi e Prestiti S.p.A. that had expressed the resigning Director).
On the basis of the statements made for the appointment, of the vote count and of the end of voting, the appointed Board of Directors, also following appointment by co-optation of Director Pensato, largely meets the requirements envisaged by Article 147-ter, paragraph 3 of the Consolidated Law on Finance and three members of the Board of Directors appointed by the Meeting on May 13, 2011 were taken by the minority list that has obtained the highest number of votes and is not connected in any way, not even indirectly, with the members who have submitted or voted the list that won for a number of votes.
A brief description of the Board members' professional background is provided:

- **Luigi Piergiuseppe Ferdinando Roth, 71 years old - Chairman**
  [born in Milan on November 1, 1940]

With a degree in Business Administration from the Luigi Bocconi University, Milan, he is a registered auditor. Since November 2005, he has been Chairman of Terna S.p.A. and since November 2009, he has been Chairman of Terna Rete Italia S.r.l. (formerly TELAT S.r.l.), a subsidiary of Terna S.p.A.. Since April 2007, Mr. Roth has been Independent Director at Pirelli & C. S.p.A. and since April 2009 he has been President of Banca Popolare di Roma (CARIFE Group).
Mr. Roth began his career as a business manager with the Pirelli Group, handling activities in Italy and abroad. He then joined Metropolitana Milanese as Director of Planning. Since 1980, he has managed mid-sized companies both in the manufacturing and real estate sectors, in the positions of General Manager and CEO. From 1986 to 1993, he served as CEO at Ernesto Breda S.p.A.; from 1993 to 2001 he was Chairman and CEO of Breda Costruzioni Ferroviarie S.p.A.. From April 1996 to January 1998, he was Chairman of Società Ferrovie Nord Milano S.p.A. of which he was CEO from December 1996 to January 1998. From December 1996 to January 1998 he was Chairman and CEO of Società Ferrovie Nord Milano Esercizio S.p.A.. From May 1998 to December 2000 he was CEO of Ansaldo Trasporti S.p.A. and transmission agent for Finmeccanica S.p.A.. From 2002 to 2006, he was Board Member at the Luigi Bocconi University. From January 2004 to April 2007 he was Deputy Chairman at Cassa Depositi e Prestiti S.p.A. From May 2004 to April 2007 he was Board Member at TELECOM Italia S.p.A. and from 2001 to 2009 he was President of the Fondazione Fiera Milano. From May 2006 to November 2009 he was Deputy Chairman of Terna Participações S.A., a subsidiary of Terna S.p.A..

- **Flavio Cattaneo, 48 years old - CEO**
  [born in Rho (Milan) on June 27, 1963]

With a degree in Architecture from the Milan Politecnico, Mr. Cattaneo has also received specialized training in business management. Since November 2005, Flavio Cattaneo has been CEO of Terna S.p.A.. Since January 2008 he has been Independent Director in Cementir Holding S.p.A. Since October 2008, he has been Deputy Chairman in Charge of Energy and Environmental Policies at UIR, Union of Industrialists and Companies in Rome.
He has held important managerial and administrative positions in various Italian companies in the building, radio and television, service, new technologies, public service and facilities sectors. He became head of the former Ente Autonomo Fiera Internazionale di Milano as Extraordinary Commissioner in 1999 and went on to oversee its stock market listing as Fiera di Milano S.p.A., serving as Chairman and CEO until 2003. Flavio Cattaneo has been Director of many energy companies (from 1999 to 2001), including: AEM S.p.A. of Milan (as Deputy Chairman), Serenissima Gas S.p.A., Triveneta Gas S.p.A., Seneca Srl and Malpensa Energia Srl. He was appointed head of Italy's public television network RAI S.p.A. in April 2003, in the position of General Manager, which he held until August 2005. He also oversaw the merger with Rai Holding and the unbundling of accounts. From May 2006 to November 2009 he was Chairman of Terna Participações S.A., a subsidiary of Terna S.p.A..

- **Fabio Buscarini, 64 years old - Director**
  [born in Ancona on February 6, 1948]

He has a degree in Sociology from the University of Trento. Since January 1, 2007 he has been the Managing Director and General Manager of INA Assitalia S.p.A., positions individually held from the previous year in both companies before their merger. From 1969 he was with Assicurazioni Generali, where he held various positions, including General Manager in April 2005.
He currently holds other important corporate positions in companies of the Generali Group, such as Generali Business Solutions S.p.A. and, moreover, he is Vice President at ImpreBanca Finanziaria d'Impresa S.p.A. and is on the Board of Directors at Burgo Group S.p.A. and Compass S.p.A.. He is a representative for ANIA at the CONSULTA for Rome Businesses Association.
He has also held the following positions: Member of the Board of Directors at Banca Generali (April 2009 – May 2011), at FATA Assicurazioni Vita e Danni S.p.A. (December 2006 – April 2009) and at Banca di Credito dei Farmacisti (February 2006 – July 2008); Italian Member of the International Management Board - sponsor of Operational Excellence (2005 - 2006); President of Risparmio Assicurazioni (December 2004 – August 2006); Member of the Board at Generali Vita (April 2003 – April 2006), Europ Assistance (March 2003 – April 2004) and Finagen (March 2003 – April 2004).

- **Paolo Dal Pino, 49 years old - Director**
  [born in Milan on June 26, 1962]

He has a degree in Economics from the University of Pavia. He is presently the President of Pirelli Latin America. Since April 2008 he has been a member of the Board of Directors of Terna S.p.A.. From January 2006 to June 2007 he was CEO of Wind Telecomunicazioni after having been CEO at SEAT Pagine Gialle from July 2001 to 2004, and Chairman of Telecom Italia in Latin America and Chairman of Tim Brazil from February 2004 to 2005.
From 1990 to 2001 he has held various positions within the Espresso Group, among which – from 1991 to March 1995 – that of Financial Director of the newspaper la Repubblica S.p.A., and from 1995 to July 2001, of General Director of the Editorial Group L'Espresso, CEO of Kataweb S.p.A. and Director and member of the Executive Committee at ANSA.
In 1986, he began his career in the Fininvest Group and from 1987, until 1990, he joined the Mondadori Group where he was CFO of the Verkerke Group in The Netherlands.

- **Matteo Del Fante, 44 years old - Director**
  [born in Florence on May 27, 1967]

He has a degree in Economic Policy from the Luigi Bocconi University in Milan. He began his career at J.P. Morgan in 1991 holding positions for Italy and foreign countries in the sector of fixed income markets. From 1999 to 2003, as Managing Director in London, he managed significant financial and strategic operations in Europe.
Since June 2010 he has been General Director at Cassa Depositi e Prestiti S.p.A., where he previously was Head of the Financial Department and of the Real Estate Department.
Since July 2010, leaving the position of CEO, he took on the position of chairman of the Board of Directors of "CDP Investimenti SGR", a savings management company which founded and manages the "Fondo Investimenti per l'Abitare" operating in the private social construction sector. Since May 2007, he has been a Board member of the consulting firm SINLOC, a subsidiary of bank-based Foundations. Since April 2008 he has been a Board member of Terna S.p.A. and member of the Internal Control Committee. Since July 2011, he has been a member of the Supervisory Board of "EEFF – European Energy Efficiency Fund S.A." fund for energy efficiency promoted by Cassa Despositi e Prestiti, the European Commission, European Investment Bank (BEI) and Deutsche Bank.

- **Salvatore Machì, 74 years old - Director**
  [born in Palermo on May 28, 1937]

He holds a degree in Electronic Engineering and has received specialized training at the Istituto Superiore di Telecomunicazioni, in addition to his professional experience with Esso and IBM. He joined Enel in 1965 and held various positions up to 1999, including Manager of the Transmission Department, National Manager of Thermoelectrical Energy Generation and Purchase and Tender Manager.
He was CEO (from July 1999 to April 2000) and, then, Chairman (up to July 2003) of the Gestore della Rete di Trasmissione Nazionale S.p.A., and Director of Gestore del Mercato Elettrico S.p.A. during that time. He has been Chairman of the Board of Directors of CESI S.p.A. since March 2003, where he previously (from July 1999 to October 2001) served as CEO. He is currently Director of Api Energia S.p.A. and, since September 2004, a Director of Terna S.p.A. as well.

- **Romano Minozzi, 77 years old - Director**
  [born in Castelnuovo Rangone (Modena) on March 6, 1935]

He has a degree in Business and Economics from the University of Bologna.
He began his career at the Banca Commerciale Italiana. In 1961 he was one of the founders of Iris Ceramica, where he holds the position of President and is still the principal reference person.
Presently, in addition to being President of Iris Ceramica, since April 2004 he has been a Board Director of GranitiFiandre S.p.A. and is also President of Fincea S.p.A. and Domfin S.p.A., he is the Sole Director of IRIS Due S.p.A., Sole Director of R.M. Finanziaria S.p.A. and Board member of Castellarano Fiandrea S.p.A. and Canalfin S.p.A..
Romano Minozzi has received recognition for his activities, including the “Innovazione 2000” award by the Academy of Ceramics. In the past, he held various positions: for 10 years he was a Board member of Banco S. Geminiano and S. Prospero, then incorporated into Banco Popolare; from July 2002 to May 2005 he was an independent Director of Ferrari Automobili S.p.A. in Maranello (Modena), appointed by Mediobanca and member of the shareholders agreement of Mediobanca from its formation.

- **Francesco Pensato, 65 years old - Director**
  [born in Casalpusterlengo (Lodi) on February 17, 1947]

He holds a Law Degree from the University of Milan with a Master’s Degree in Corporate and Tax Law from the IPSOA Business School. He is a professional Supreme Court of Cassation lawyer, and since 2001, has been Senior Partner at the Associated Legal Office Franzosi-Dal Negro-Pensato-Setti, as head of the department of corporate law and bankruptcy procedures and is presently owner of the “Pensato & Partners Avvocati” associated law firm. His professional experience in the field of legal consulting and assistance in corporate and commercial matters for medium and large Italian and foreign companies also includes various legal corporate appointments such as Chairman of Arbitration tribunals, as well as Adjustor and Extraordinary Commissioner with management functions upon appointment by the Ministry for Economic Development. As a legal appointment, he is also the Common Representative of Telecom Italia S.p.A’s bondholders. Since 2005, he has been a member of the Commission for Reforming Bankruptcy Procedures on appointment of the Ministry of Justice and since 2009, has been a member of the Commission for reforming the extraordinary administration of the large groups facing critical situations formed by the Ministry for Economic Development. Since 2010 he has also been Board Member at Mediocredito Italiano S.p.A.
From 2001 to 2004 he was Vice President of the Organismo Unitario dell'Avvocatura Italiana (OUA) and President of the Internal Study Commission for reforming laws on bankruptcy procedures. From 1998 to 2001 he was joint President of the Joint Commission for relations between the Magistracy and the Bar in Milan.

- **Michele Polo, 54 years old - Director**
  [born in Milan on August 7, 1957]

He has a degree in Business and Economics from the Luigi Bocconi University in Milan, and graduated in Economic Policy with a Masters in Economic Sciences from the London School of Economics. From 2003 he has been Ordinary Professor of Economic Policy and from 2007, Vice-Chancellor at the Luigi Bocconi University. He is Director of the Institute for Economics and Policy of Energy and the Environment (IEFE) of the Bocconi University and carries out other scientific and academic activities: he is Director of the Journal of Economists and member of the Editors Committee of Economy of Energy Sources and the Environment and of the Editor’s Committee of Market, Competition, Regulations. He is scientific advisor of the publishing house “Il Mulino”, in Bologna.
From 2003 to 2006 he was Economic Advisor of the General Management of Competition of the European Commission.
Since April 2008 he has been a Board member of Terna S.p.A..
He is also the author of numerous essays and monographs on themes such as antitrust, liberalization and energy sectors.

During its term, the Board of Directors has confirmed the existence of the requirements of integrity and professionalism held by each of its members.
The evaluation regarding the existence of the requirements of independence for each of the non-executive members was

made, taking into account the information provided by each person, during the appointment and during the meeting held on March 20, 2012 according to the terms stated in the following paragraph “Independent Directors”.
The attached table 1 includes the information regarding the composition of the Board of Directors as of March 20, 2012. del 20 marzo 2012.

### Maximum number of positions in other companies

All the Directors accept their appointment to office when they believe they can devote the necessary time to the diligent performance of their duties – also considering the positions they hold outside the Company in other companies listed on regulated markets (also abroad), financial companies, banks, insurance companies and significantly large companies – and to devote the necessary time to the diligent performance of their duties, as they are well aware of the responsibilities of the office held.
To this end, since February 2007, in compliance with Article 1.C.3 of the Governance Code, Terna’s Board of Directors approved its own guidelines regarding the maximum number of positions as Director or Statutory Auditor in significantly large companies that can be held still enabling the efficient performance of the duties as Director of Terna S.p.A. included in the internal document “Orientations concerning the maximum number of positions that can be held by Directors of Terna S.p.A.” After more than four years since its adoption, following constant monitoring of the governance choices by the Company, and in line with the practices of similar companies, at its meeting held on October 7, 2011 the Board of Directors revisited said orientations.
To this purpose, “significantly large companies” were defined as:
a) companies with shares listed on regulated markets, in Italy or abroad;
b) Italian or foreign companies with shares not listed on regulated markets, and operating in the insurance, banking, brokerage, asset management or financial sectors;
c) other Italian or foreign companies with shares not listed on regulated markets, not operating in the sectors listed in letter b), having net assets exceeding 1 billion euros.
The Board has identified different general criteria for the commitments required of each role (CEO, Executive Director - for example Executive Chairman, Managing Director, i.e. with special proxy - Non-executive and/or Independent Director and Standing Statutory Auditor), considering the nature and size of the Company in which the positions are held and whether they are part of the Terna Group or are Terna’s investees (which, originating from the assignment itself, are not calculated in the total number). A “weight” was assigned to each type of position for the purposes of assessing the commitment required, and the Directors also established that the role of CEO at Terna is incompatible with the same role in other significantly large companies.
When more than one position is held within the same group, including employment by one of the Group companies, only the position with the greatest “weight” is considered.
All the Directors in office that were appointed by the Meeting on May 13, 2011 informed about the positions they held at the time the lists were submitted and subsequently when they accepted their appointment. Likewise, the Director that was co-opted at his appointment on July 29, 2011. Based on the updated information delivered to the Company in compliance with the approved guidelines, as of March 20, 2012, all Directors held a number of positions that is compatible with the guidelines set by the Board.
In the summaries of each Director’s personal characteristics, all the positions held by them are indicated. The total number of positions held as Directors or Statutory Auditors in significantly large companies is provided in the attached table 1.
There have not been exceptions, issued by Terna’s Shareholders’ Meeting, to the prohibition of competition by the Directors provided for by Article 2390 of the Civil Code.

## Role of the Board of Directors

The Company’s Board of Directors holds a crucial role in its organization. It has strategic and organizational functions and responsibilities with respect to the Company and the Group. It is also responsible for verifying that the necessary controls are in place to monitor the performance of the Company and its subsidiaries.
In addition to exercising the powers that are attributed to it by the Law, the Company’s Bylaws (Article 21.1), according to the law, attributes the Board the competence to resolve on issues pertaining to the Shareholders’ Meeting that can determine amendments to the Bylaws as previously described in “Bylaws amendments.”
Within the limits as per Article 2381 of the civil code, the Board of Directors may delegate its tasks to an executive committee and/or to one or more of its members (Article 22.1 of the Bylaws).
In this context and in compliance with the Law and the provisions of specific resolutions, and considering the provisions of Article 1 of the Governance Code, the Board of Directors carries out the following:

- delegates and revokes powers to one or more Directors, defining the content, limitations and methods of such powers. The current structure of the Board of Directors provides for only one CEO. The powers currently assigned to him give the CEO the widest powers for the administration of the Company, except for those assigned by the Law or the Bylaws or reserved for the Board of Directors by its resolutions (Article 1.C.1, letter c) of the Governance Code);

- receives, similarly to the Board of Statutory Auditors, constant and exhaustive updates from the CEO on activities performed during the year in compliance with powers, through specific quarterly reports. In particular, with respect to all significant transactions carried out by the Company and its subsidiaries (including any related party transactions of lesser importance as identified in the specific Procedure adopted by Terna, and which are not exempt from application of the same, which do not require approval by the Board of Directors) the CEO reports to the Board of Directors on the (i) characteristics of the transactions, (ii) the parties involved and their relationship with the Company or its subsidiaries (Article 1.C.1, letter c) of the Governance Code);
- on the basis of the proposals by the specific Committee, approves Company Policy concerning remuneration of members of administration bodies, general directors and executives with strategic responsibilities, which is then submitted to the Shareholders' Meeting for an advisory vote, and after having heard the Board of Statutory Auditors, determines the remuneration of the CEO and of other Directors covering special offices (Article 1.C.1, letter d) of the Governance Code) which it indicates annually in a specific report;
- evaluates the adequacy of the general organizational, administrative and accounting structure of the Company and its subsidiaries that hold strategic importance (in compliance with the Board's Resolution of February 22, 2007, these are: a) subsidiaries listed on regulated markets and b) subsidiaries that have a significant foreign market share in the Group's core business), with specific reference to the Internal Control System, whose guidelines are defined by the Board, and to the management of conflicts of interest (Article 1.C.1, letter b) of the Governance Code). The adequacy and actual operation of the Terna Group's Internal Control System is reviewed at least on an annual basis. With regard to this matter, reference should be made to section XI;
- examines and approves strategic, business and financial plans. In this respect, the current structure of Company powers provides that, in particular, the Board of Directors approves the Company's annual budget and long-term plans (which include the combined annual budgets and long-term plans of the subsidiaries) (Article 1.C.1, letter a) of the Governance Code);
- defines the Corporate Governance system within the Company, provides for the appointment, role definition and rules of the Board's Internal Committees (Article 1.C.1, letter a) of the Governance Code);
- examines and approves transactions with a significant impact on the Company's financial position and results, especially if they are related party transactions or could otherwise give rise to a potential conflict of interest. In particular, the following transactions, inter alia, are submitted to the Board of Directors in advance "significant transactions" carried out also through subsidiaries (i) for which the underlying item, consideration, method or timing could have an impact on safeguarding the Company assets or the completeness and accuracy of Terna's accounting and other information which require Terna to disclose to the public an informative document in compliance with the supervisory authorities of financial markets and/or (ii) transactions for more than €50 million euros, except for those approved in the budget and in financial plans as well as in agreements relating to dispatching and all other related services. Furthermore: subscription of loans, granted and received, of any type, medium and long term, for an amount exceeding €100 million euros that were not included in the approved budget and financial plans and not aiming at implementing measures that were already approved by the Board in the Electricity Transmission Grid's Development Plan and/or in the Strategic Plan (Article 1.C.1, letter f) of the Governance Code);
- resolves regarding the establishment of new companies, the purchase and transfer of shares in companies, namely in companies or company branches with a value exceeding €30 million euros (Article 1.C.1, letter a) of the Governance Code);
- assesses the general performance of Company operations, with specific reference to situations of conflict of interest, on the basis of the information received from the CEO and the Internal Control Committee, periodically checking that planned results have been achieved (Article 1.C.1, letter e) of the Governance Code);
- at least once a year, evaluates the size, composition and performance of the Board of Directors and its committees (Article 1.C.1, letter g) of the Governance Code);
- reports to the shareholders during the meeting.
- The activities of the Board of Directors are coordinated by the Chairman. The latter summons the Board's meetings, sets the agenda upon request by the CEO and guides meeting's running, making sure that the Directors are timely provided with the documentation and the necessary information so that the Board can consciously express on the matters submitted to examination. Moreover, he verifies compliance with resolutions, chairs the meeting and – in the same way as the CEO – has powers of legal representation of the Company.

### Board of Directors Meetings

The Directors gather regularly and carry out tasks based on their full knowledge and in autonomy, pursuing the objective of creating value for shareholders, taking into account the social aspects of the Group's activities and the resulting need to adequately consider all stakeholders in the performance of those activities.
During 2011, the Board met ten times and each meeting lasted an average of one hour and twenty minutes with the Directors regularly participating as well as the Board of Statutory Auditors (Article 1.C.1, lett h) of the Governance Code).
Due to the renewal of the Board of Directors (May 13, 2011), the first three meetings were carried out by the outgoing members and the subsequent meetings were carried out by the newly appointed members.
For 2012, a Board meeting is expected every month and all the meetings have been scheduled relative to the examination of the economic and financial data by the Board of Directors according to what officially communicated to the market on January 16 and February 6, 2012. In the current year and as of the date of approval of the present Report, the Board of Directors met three times.

### Assessment of the Board of Directors activity

In compliance with the Governance Code published by Borsa Italiana, Terna's Board of Directors also for 2011 assessed the Board size, composition and performance, as well as that of its Committees. The Board conducted such assessment, drawing on the assistance of the company Egon Zehnder International S.p.A. as an external consultant to ensure the utmost objectivity of its evaluations. This initiative follows similar ones that were undertaken by Terna's Board of Directors as of 2006.
The independent consultant's analysis started during the first quarter of 2012 and carried out through qualitative questionnaires and individual interviews with each Director and through subsequent quantitative and qualitative analysis of the information gathered, focused on various aspects regarding: a) the decision-making process; b) the flow of information and presentations; c) participation in the definition of a strategic direction and d) the atmosphere inside the Board and relations with the Chairman and the CEO. Such analysis highlighted how Terna's Board of Directors is totally in line with the Governance Code to the point that it fully represents a best practice both at the Italian and international level, confirming the positive judgment that there was compliance with said requirements.
On the basis of the results of the analysis carried out, the Board of Directors passed an overall positive evaluation on the size, composition and performance of the Board and its Committees having positively evaluated all the principal profiles examined and committed to exercising their role as best as possible.
In particular, the Board deemed that the new Board's operation during 2011 confirmed its high efficiency level and the general trend to continuously improve some organizational issues, which constitute the excellence of the Board. In particular, it acknowledged improvements in: internal cohesion and independence for the Board; stronger support by the Board to Top Management and attention to investment projects; enhancement of internal Board Committees; effectiveness in the information process between the Chairman, the CEO and Board members.

## Delegated bodies and other Executive Directors

### CEOs

The current structure of the Board of Directors provides for only one CEO, to which the Board has attributed powers, defining their content, limits and any exercise modalities; no executive committee was established.
The CEO has powers of legal representation of the Company and is entrusted with the widest powers for the administration of the Company, pursuant to Board Resolution, with exception of those differently attributed by the Law, by the Bylaws or reserved for the Board of Directors.
The CEO informs the Board of Directors and the Board of Statutory Auditors of the activities and of the management of the Company as well as of the resolutions passed in exercising his powers pursuant to Article 21.3 of the Bylaws, at least on a quarterly basis and on occasion of Board meetings.
On a quarterly basis, specific reports are prepared in order to inform the Board on major action and activities. In addition, the Directors are kept constantly informed by competent departments on the main legislative and regulatory innovations concerning the Company and the exercise of own functions. On occasion of the appointment, they are adequately informed about the existing Corporate Governance system and the fundamental lines of governance.
Exception made for the CEO, the other 8 members of the Board of Directors (Luigi Roth, Fabio Buscarini, Paolo Dal Pino, Matteo Del Fante, Salvatore Machì, Romano Minozzi, Francesco Pensato and Michele Polo) must all be considered as non-executive. It must be noticed that also the Chairman does not play an executive role, since no proxies are attributed to him.
For their number, competence, authority and availability of time, the Non-executive Directors (since they are not provided with operating proxies and/or managing roles in the Company) are capable of guaranteeing that their judgment can have a significant weight in Board's decisions in line with what provided for by the Governance Code (Article 2.P.3 of the Governance Code).
The Non-executive Directors enrich with their specific competences the Board's discussions, so as to favor the examination of the subjects according to various perspectives and subsequently pass deeply analyzed, conscious and respectful resolutions in line with social interests.

During 2011, and up until the date on which this Report was approved, the Directors participated in specific meetings with the Company's management in relation to the core business activities with particular reference to the preparation of the Development Plan for the National Transmission Grid, in which also members of the Board of Statutory Auditors participated.

### Independent Directors

A suitable number, also for competence, of Non-executive Directors is independent.
The Board of Directors has evaluated the existence of the requirements of independence provided for by the Law, the Bylaws and the Governance Code which Terna has adopted, for each Director in the first useful occasion after their appointment. Moreover, the Board of Directors' meeting of March 20, 2012 – on the basis of the criteria previously defined for the assessment of independence of its non-executive members, in compliance with the criteria indicated by the Governance Code and on the basis of the information supplied by the persons involved – confirmed the existence of the requirement of independence in each of the 6 Non-executive Directors: Fabio Buscarini, Paolo Dal Pino, Salvatore Machì, Romano Minozzi, Francesco Pensato, Michele Polo (Articles 3.C.1, 3.C.2 and 3.C.4 of the Governance Code).
At the same time, the correct application of the defined criteria and the procedures adopted by the Board of Directors was verified by the Board of Statutory Auditors (Article 3.C.5 of the Governance Code).
Although independence characterizes the activity of all the Directors, executives and non-, the presence of Directors that can be qualified as "independent" in compliance with the abovementioned criteria - and whose role is significant both within the Board and its Committees - suitably ensures adequate consideration of all shareholding members' interests.
Among the assessments carried out by the Board, with reference to the 6 Directors, the existence is proven of the requirement of independence envisaged for in Article 15.4 of the Bylaws that requires that at least 1/3rd of the Directors in force – with rounding, in case of fractional number lower than the unit, to the following unit – meets the requirements of independence established for Auditors by Article 148, paragraph 3, of the Consolidated Law on Finance.
Following the composition and the work method of the Board of Directors, as well as the presence of Independent Directors in the composition of the Committees, in the operating system a constant exchange of information between the same Independent Directors has been taking place, both at meetings of the Internal Committees and at the Board meetings, which has not required a specific meeting to be held for them.

### Lead independent director

The work method of the Board of Directors has assured the suitable coordination of the contributions and the requests of the Non-executive Directors and, in particular, of the Independent Directors; it also guaranteed a preventive exchange of information that rendered the work of the Board productive and focused on the true requirements of the Company. On the basis of such assumptions, confirmed by the outcomes of the Board review which the Board was subject to, and since the assumptions indicated by the Governance Code were not present, the position of Lead Independent Director was not established within Terna.

## Section V **Management of company information**

During the meeting of December 21, 2006, the Company's Board of Directors - in compliance with the provisions on the management of privileged information aimed at preventing insider trading and with the provisions of Article 4 of the new Governance Code, of Article 114, paragraph 1, and of Article 181 of the Consolidated Law on Finance, approved a specific regulation for the management and treatment of confidential information, which also includes the procedures for disclosing documents and information on the Company and its subsidiaries outside of the Company, with specific reference to the confidential information provided for by paragraph 1, Article 114 of the Consolidated Law on Finance.
This regulation represents an update to the measures included in the regulation that Terna approved as of April 2004, with specific reference to "price sensitive" information. It aims at maintaining the secrecy of confidential and privileged information while at the same time ensuring the disclosure of correct, complete, adequate, timely and objective Company information to the market relating to Company's data. The regulation also sets the guidelines for the subsidiaries, so that they will provide Terna with all the necessary information for it to meet the disclosure requirements of the Law. The Directors and Statutory Auditors of Terna and its subsidiaries are required to comply with the provisions of this regulation and, in any case, keep all documents and information acquired in the performance of their duties, as well as the content of any discussions during Board meetings, confidential.
The regulation generally entrusts the Company's CEO and the delegated bodies of the subsidiaries with the management of confidential information for which they are responsible, providing that such information on individual subsidiaries should be disclosed with the prior authorization of the Company's CEO.
Moreover, the regulation establishes specific procedures to be followed when disclosing Company documents and information outside the Company - with particular focus on the disclosure of privileged information. It also scrupulously

governs the way in which members of the Company should deal with the press and other mass communication means (i.e. financial analysts and institutional investors).
Lastly, the new regulation introduced specific "Measures for persons committing violations" into the regulation's provisions.

In compliance with the provisions of Article 115-bis of the Consolidated Law on Finance and with the regulatory measures issued by CONSOB, Terna's Board of Directors created a specific Register of people with access to privileged information within Terna. It also prepared a specific regulation to govern how the Register should be held and updated. The same regulation requires that subsidiaries also create their own Registers.
As of April 2004, the Company's Board of Directors also approved the internal dealing Governance Code, in compliance with the regulatory measures laid down by Borsa Italiana S.p.A., establishing the market transparency requirement for listed companies with respect to significant transactions, involving the financial instruments of these companies or their subsidiaries, carried out by people with significant decision-making powers in the companies and with access to price sensitive information ("relevant persons").
Following the entrance into force of the new internal dealing regulations that were introduced by Law no. 62 dated April 18, 2005 ("2004 Community Law" that integrated the provisions of Article 114 of the Consolidated Law on Finance) and of the relative implementing provisions (articles from 152 sexies to 152 octies and Attachment 6 of the Issuer Regulations), Terna adopted a specific internal Procedure to identify Terna's "relevant persons" and to manage, handle e disseminate to the market information regarding financial instruments of the Company.
Within this Procedure – that was updated on March 19, 2010 based on CONSOB explanations and on the structural asset of the Company – Terna deemed appropriate to maintain, for the "relevant persons" identified, the obligation to refrain – either directly or indirectly – from carrying out transactions that are subject to internal dealing regulations during two blocking periods in concomitance with the approval of the draft financial statement and of the half-year report by Terna's Board of Directors.
This procedure is available in the Company's website www.terna.it in the "Investor Relations/Corporate Governance/Internal Dealing" section. The procedure includes the following qualifying elements, which are considered adequate in heightening its qualitative content:
- application of internal dealing transparency obligations towards "relevant persons" within the Company and its subsidiaries as identified in the procedure (in addition to Terna's Directors and Standing Auditors);
- "relevant persons" are not allowed to carry out transactions (other than the exercise of options) during the 30 days before the approval of the draft financial statements and half year report by Terna's Board of Directors. Moreover, the Board can establish additional blocking periods during the year, following specific events;
- an adequate penalty system was created for "relevant persons" identified as violating the measures of this procedure.

Adjustments to the Procedure adopted by Terna are underway, in order to incorporate the simplification changes to legislation made by Article 152 septies of the Issuer Regulations pursuant to CONSOB resolution no. 18079 dated January 20, 2012, published in the Official Journal on February 7, 2012, aimed at combining market competitiveness and the necessary protection of investors, and relative to the reporting thresholds of transactions subsequent to those which were already reported.

## Section VI **Committees within the Board**

Within the Board of Directors, the Remuneration Committee and the Internal Control Committee have been set, both with proposal-making and advisory functions, and made up of at least three Directors, the majority of which independent, pursuant to the Governance Code. At least one member of the Remuneration Committee possesses adequate knowledge and experience in financial matters, and at least one member of the Internal Control Committee possesses adequate knowledge in accounting and finance matters.

The Committees have been attributed the tasks provided for by the Governance Code. The criteria for the composition, the tasks and the responsibilities attributed in compliance with the Governance Code and the modalities of carrying out the meetings have been ruled through proper internal organizational Regulations adopted by the Board of Directors as of January 24, 2007.

Within the Board of Directors another Committee was set up (Transactions with Related Parties Committee) as the body that plays the role required by "Regulation containing provisions concerning transactions with related parties" issued by CONSOB in March 2010 and subsequently amended and on the basis of the provisions in "Procedure for Transactions with Related Parties" adopted by the Company and illustrated in the special Section XII of this Report. The Committee is assigned preliminary, proactive and advisory duties and powers in evaluations and decisions concerning the abovementioned Transactions with Related Parties both for the approval of greater importance transactions and of those of lesser importance indicated in Terna's Procedure, as well as in relation to possible proposals for amendments of the Procedure adopted by Terna. Said Committee is composed of at least three Directors, all independent, according to the provisions of the Governance Code.

The meetings of the Committees include the drawing up of minutes. Each Committee has also the faculty to access the information and the necessary departments to carry out its tasks and can use possible external advisors in the limits provided for by the Board of Directors.

Within the Company budget, adequate financial resources are allocated for the implementation of the tasks of each Committee. On invitation of the Coordinator of each Committee, other subjects, whose presence can contribute to the best performance of the Committee, can participate in the meetings.

## Section VII **Appointment Committee**

Currently, Terna has not set up, within the Board of Directors, a specific Appointment Committee, since up to now shareholders have not met difficulties in presenting adequate candidacies, such as to allow a composition of the Board in line with the provisions of the Governance Code for listed companies.

## Section VIII **Remuneration Committee**

### Functions of the Remuneration Committee

As of 2004, within the Board of Directors a Remuneration Committee was set up, responsible for making proposals to the Board (i) for the remuneration of the CEO and of other Directors covering particular offices monitoring the implementation of the Board's resolutions, and (ii) for determining the remuneration criteria of the top management of the Company and its subsidiaries, periodically evaluating its criteria on the basis of indications provided by the CEO and submitting general recommendations to the Board on the matter.

Following the renewal of the Board of Directors during the meeting held on May 13, 2011, the Remuneration Committee was also renewed as well as its members.

Upon the renewal, the Committee's tasks were reconfirmed as already identified by the Board within "Terna S.p.A.'s Organizational Rules for the Remuneration Committee" which was approved with resolution dated January 24, 2007. Subsequently, on November 9, 2011, the Board of Directors approved amendments to "Terna S.p.A.'s Organizational Rules for the Remuneration Committee" adopted in order to ensure full consistency with the new indications of Article 7 of the Governance Code. Furthermore, the provisions pertaining to the composition and the competencies of the Remuneration Committee were updated, with particular regard to: (i) the competencies of the Committee concerning the general policy adopted for remuneration and (ii) concerning proposals for remuneration of executive Directors and other Directors covering particular offices, as well as (iii) setting performance objectives connected to the variable component

of said remuneration, (iv) monitoring the application of decisions made by the Board and (v) verification of the actual achievement of performance objectives.
Moreover, it is also required that the Committee Coordinator, or another member of the Committee, inform the shareholders concerning the methods of the exercising of their functions and that, to this end, the Coordinator or another member of the Committee be present at the annual Shareholders' Meeting.
No Director takes part in Remuneration Committee meetings where proposals intended for the Board are formulated on matters concerning its own remuneration, unless proposals are presented that regard general Committee members as established within the Board.
The Remuneration Committee is currently composed of Salvatore Machì (as Coordinator), Romano Minozzi and Paolo Dal Pino, all non-executive independent Directors; at least one member possesses adequate experience in financial matters.
In 2011, the Remuneration Committee held five meetings, with the regular participation of all members. The meetings lasted an average of forty-five minutes each. None of the Directors participated in the Committee meetings in which proposals regarding their remuneration were submitted to the Board of Directors. As a result of the renewal of the Board of Directors and the new composition of the Committee with other members (May 13, 2011), the first two meetings were held by outgoing members and subsequent meetings were held by newly appointed members.
In 2012, the Committee will hold as many meetings as are sufficient for carrying out the duties assigned.
During the current year, up to the date of approval of this Report, the Committee has held one meeting.
As part of its duties, and with respect to the remuneration of the CEO and other Directors covering particular offices, during 2011 the Remuneration Committee made specific proposals to the Board of Directors, with the support of a consultancy company that set the remuneration benchmark, that provided for a portion of the Executive Director's compensation to be based on the Company's results and the achievement of specific objectives indicated in advance by the Board. Moreover, by collaborating with a consultancy company, it formulated a special proposal for the "Remuneration Policy" adopted by Terna for the remuneration of executive Directors, other Directors covering particular offices, Auditors, the General Directors and Executives with strategic responsibilities for the fiscal year 2011, pursuant to Article 7 of the Governance Code. In addition, during the meetings held in 2011, the Remuneration Committee examined the incentive plans for the Company's top management. In 2012, the Committee also formulated proposals for the "Remuneration Policy" for the fiscal year 2012 approved by the Board and submitted to the shareholders pursuant to Article 123 ter, paragraph 6 of the Consolidated Law on Finance.
During the meeting of March 20, 2012, the Board of Directors evaluated the duties and performance of the Committee. The altogether positive evaluation on the size, composition and operation of the Committee was confirmed by the Board of Directors, within the yearly review of the Board and the Committees.
The Committee has been granted adequate financial resources.

## Section IX **Remuneration of Directors**

The compensation of the Directors is established by the Shareholders' Meeting for each Director (Article 24.1 of the Bylaws). Extra compensation for the members of the Committees formed within the Board of Directors in compliance with the Governance Code of Borsa Italiana was resolved, following the evaluation by the Board of Statutory Auditors, in compliance with Article 2389, paragraph 3, of the Civil Code and with Article 24.2 of the Bylaws, by the Board itself; the overall compensation for the Chairman and the CEO is also identified by the Board of Directors based on the proposal submitted by the Remuneration Committee and following the evaluation by the Board of Statutory Auditors.
The total emoluments received by the members of the Board of Directors during the year are indicated in the note to the financial statements.
As proposed by the "Remuneration Committee", the Board of Terna adopted its own "Remuneration Policy" at its meeting held December 13, 2011, in implementation of the provisions of Article 7 of the Governance Code. Following the entry into force of the regulatory provisions of implementation under Article 123 ter of the Consolidated Law on Finance issued with the CONSOB resolution no. 18049 dated December 23, 2011 (published in the Official Journal no. 303 on December 30, 2011), in its meeting held March 20, 2012, Terna's Board, as proposed by the "Remuneration Committee", approved the updating of the adopted Policy to be submitted to the shareholders for an advisory and non-binding vote pursuant to Article 123 ter, paragraph 6 of the Consolidated Law on Finance.
All information on Company Policy concerning remuneration of members of administration bodies, of general directors and executives with strategic responsibilities with reference to at least the subsequent fiscal year and the procedures used for the adoption and implementation of said Policy will be summed up in the "Annual Report on Remuneration", published by Terna in fulfillment of the provisions of Article 123 ter of the Consolidated Law on Finance and of the aforesaid CONSOB resolution which, inter alia, introduced Article 84 quater to the Issuer Regulations, which will be submitted to the annual Shareholders' Meeting. With respect to the "Annual Report on Remuneration", also the information required by article 7

of the Governance Code, which Terna adopted, will be summarized.
The "Annual Report on Remuneration", based on the provisions of the rules under reference, provides an adequate representation of each of the entries that comprise the remuneration, including action provided for in the event a member leaves the position or the employment relation is terminated, highlighting the consistency with the Company Policy on remuneration approved in the previous fiscal year, and analytically illustrates the compensation paid by the Company and by subsidiaries or affiliated companies during the fiscal year of reference, for any reason and in any form whatsoever, on the basis of the provisions in Article 123 ter of the Consolidated Law on Finance and the abovementioned CONSOB resolution. Finally, based on the provisions of Article 84 quater, paragraph 4, of the Issuer Regulations, the Report shall include information concerning compensation plans provided for by Article 114 bis and information on shareholdings in Terna and in subsidiaries held by members of the administration and control bodies, by general directors, and by other executives with strategic responsibilities, as well as by spouses not legally separated and by minor children, directly or through subsidiaries, trust companies or through a third parties.

## Section X **Internal Control Committee**

### Functions of the Internal Control Committee

As of 2004, within the Board of Directors, a specific Internal Control Committee was created, with advisory and proposal-making functions.
Following the renewal of the Board of Directors during the meeting of May 13, 2011, the Internal Control Committee was re-established and its members were appointed. The Committee was assigned the following duties, as already identified within "Terna S.p.A.'s Organizational Rules for the Remuneration Committee" which were approved on January 24, 2007:

- assisting the Board of Directors in establishing Internal Control System guidelines and periodically checking the adequacy and actual implementation of the System (Article 8.C.1 of the Governance Code);
- assessing, together with the Executive in Charge of the preparation of accounting documents and the Auditors, the correct application of accounting principles and their uniformity for the preparation of the consolidated financial statements (Article 8.C.3, letter a) of the Governance Code);
- expressing opinions on request of the CEO, on specific aspects concerning identification of main Company risks and planning, implementation and management of the Internal Control System (Article 8.C.3, letter b) of the Governance Code);
- examining the work plan prepared by the Executive in Charge of internal control as well as the periodical reports prepared by him. (Article 8.C.3, letter c) of the Governance Code);
- evaluating the proposals coming from the auditing companies to obtain assignment, as well as the results presented in the report and in the suggestion letter (Article 8.C.3, letter d) of the Governance Code);
- reporting, at least every six months, to the Board of Directors about activity carried out and adequacy of the Internal Control System (Article 8.C.3, letter g) of the Governance Code);
- carrying out further duties potentially assigned by the Board of Directors especially concerning relations with the auditing company.

Additional specific duties are assigned to the Committee based on the Organizational Model adopted by Terna in compliance with Legislative Decree no. 231/01 and with Terna's Code of Ethics.
The Internal Control Committee is currently composed of Paolo Dal Pino (as Coordinator), Salvatore Machì, Matteo Del Fante, Francesco Pensato and Michele Polo, who are all non-executive and mostly Independent Directors. At least one member has adequate accounting and financial experience.
In 2011, the Internal Control Committee met 4 times, with the regular participation of all members. Each meeting lasted an average of fifty minutes; the Chairman of the Board of Statutory Auditors or another Statutory Auditor appointed thereby was present at each meeting, given the Board's specific supervisory functions with respect to the Internal Control System, as required by current legislation concerning listed companies (Article 8.C.4 of the Governance Code). As a result of the renewal of the Board of Directors and of the new composition of the Committee with new members (May 13, 2011), the first meeting was held by outgoing members and subsequent meetings were held by the newly appointed members.
Upon the Committee's request, the meetings were also attended by Directors of the Company whose presence was deemed helpful for the best information regarding the items on the agenda.
In particular, in 2011, the Internal Control Committee evaluated the operation of the internal control system linked to and involving various interested parties and bodies, providing support to the Board of Directors for analyzing and following the photovoltaic Project, providing a positive opinion on the main financing transactions, positively examining the approach to managing the Company's risks regarding security and examining and monitoring the audit activities for 2011 and it also met with the Independent Auditors to evaluate auditing activities with particular attention to the methods used in carrying out said activities, and the results obtained. Furthermore, it examined the progress of financial risk management. Pursuant

to what provided for by the Governance Code, the committee assessed, together with the Executive in Charge, the correct use of the accounting standards and received information on control activities implemented for compliance with the provisions of law 262/05 and subsequent amendments. The Committee also received due information from the Vigilance Body under Legislative Decree no. 231/01 with reference to the adequacy and the development of the Model and the activity carried out by this Body.
At the beginning of 2012, the Committee conducted a preliminary analysis of novelties concerning the internal control system introduced by the Governance Code of Italian listed companies (December 2011) which should be applied during 2012.
In 2012, the Committee will hold as many meetings as are sufficient for carrying out the duties assigned. During the year up to the date of approval of this Report, the Committee has held two meetings.
During the meeting of March 20, 2012, the Board of Directors evaluated the duties and operation of the Committee. The generally positive evaluation of the composition, size and responsibilities of the Committee was confirmed by the Board of Directors within the yearly review of the Board itself and of the Committees.
The Committee was granted adequate financial resources.

## Section XI **Internal Control System**

With respect to internal control, on the basis of the resolution already adopted on December 21, 2006 and of preliminary assessments, the Board of Directors updated the “Terna Group’s Internal Control System” (ICS) definition, in line with national and international best practices, as the set of rules, procedures and organizational structures which, through an adequate identification, measurement, management and monitoring process of primary risks, enable the Company to correctly and consistently manage operations in line with its objectives (articles 8.C.1 and 8.C.2 of the Governance Code).
With reasonable certainty, the Group’s ICS contributes to reaching strategic objectives, to safeguarding Company assets, the efficiency and effectiveness of Company transactions, the reliability of financial statements, compliance with the Law and regulations, the reliability of Company and financial reporting, the safeguarding of the electricity service continuity and guaranteed impartiality in carrying out activities under concession. It is based on the following elements: control environment; risk management system; control activities; information, communication and monitoring. The coordinated implementation of these elements makes the ICS effective overall.
The “control environment” at the basis of all other elements, consists of the Group’s Corporate Governance model and its ethical principles, which are set out in the Code of Ethics which the Group’s managerial style, personnel management policies and all employees’ conduct must be in compliance with.
The “risk management system” implemented by top executives and management enables the Group to manage its main risks within acceptable limits, using wide-ranging risk management policies defined in specific procedures. In order to implement an integrated “risk management system”, in 2007 Terna created a Corporate Security Department significantly integrating its security tools and defining a transversal system for identifying, analyzing and controlling Corporate risks.
The importance of using a structured method and a dedicated internal organization (Corporate Security Department), that promotes and supervises its implementation, derives from the fact that risks can influence Corporate activities, which, being of a varied type, are also characterized by the time variable between the moment a threat presents itself and the moment in which this threat materializes.
In addition to ensuring absolute compliance with legal provisions, this integrated model allows reaching Corporate security levels that exceed the regular standards attainable through a sectoral and fragmented security management.
The “control activities” are carried out by management and employees to achieve specific objectives on the basis of principles, such as self-control, hierarchical control, accountability, opposing interests and segregation of duties.
The “communication and information processes” ensure that the Company’s expected objectives, culture, values, roles, responsibilities and conduct are clearly disclosed internally, while guaranteeing that disclosures to stakeholders outside the Company are correct and transparent.
“Monitoring” aims at constantly verifying the effectiveness of the Internal Control System through “continuous” activities carried out by personnel in the performance of their work, and through separate assessments that are regular, but not continuous, and typical, but not exclusive, of the Audit Department.
Terna has indeed an appropriate structure dedicated to preventing and managing Corporate fraud activities also aimed at spreading the culture of legality and respecting Corporate regulations. Continuously monitoring processes, verifying and managing reports of illegalities have led to introducing specific controls aimed at reducing such risks and at defining, for certain critical processes, specific procedures aimed at preventing illegal conduct.
With the support of the Internal Control Committee, the Board of Directors establishes the guidelines for the Internal Control System, so that the main risks are identified, monitored and managed on a compatible basis and in line with sound and correct management principles. The Board also evaluates the adequacy and effective implementation of the Internal Control System, on the basis of adequate preliminary assessments (Article 8.C.1 lett a) of the Governance Code).

Attachment 1 to this Report includes the principal characteristics of existing risk management and internal control systems with respect to the financial information note, also consolidated (pursuant to Article 123-bis, paragraph 2, letter b) of the Consolidated Law on Finance).
Terna's Board of Directors' meeting of March 20, 2012, in compliance with the opinion rendered by the Internal Control Committee on the basis of the analyses made during 2010 and in the first six months of 2011, judged the Terna Group's Internal Control System suitable to achieve an acceptable risk profile, in consideration of the field in which Terna operates, of its size, organizational and Corporate structure (Article 8.C.1, letter c) of the Governance Code).
In its report, the Internal Control Committee also discussed in relation to the report of the Vigilance Body appointed pursuant to Legislative Decree no. 231/01 on the implementation of the Organizational Model within Terna and other Group companies.

### Executive Director in Charge of the Internal Control System

The CEO supervises the functionality of the ICS of the Group, implementing the guidelines defined by the Board of Directors and planning, implementing, managing and dealing the identification of the main risks for the Group through the designated Company structures; he then periodically submits such risks to the Board of Directors (art. 8.C.1, letter b) and 8.C.5, letters a), b) and c) of the Governance Code).

### Executive in Charge for internal control

Within Terna, the Executive in Charge for internal control is the person responsible for the Audit function, who is not responsible of any operating areas (articles 8.C.6, letter b), and 8.C.7 of the Governance Code).
The Audit manager reports the results to the CEO, to the Internal Control Committee and to the Board of Statutory Auditors concerning the audit activity results relative to risk management and to the suitability of the Internal Control System in order to achieve an acceptable overall risk profile (Article 8.C.6, letter e) of the Governance Code). He operates through audit activity, whose field of application is extended to the whole Group. The activities of Internal audit can be carried out in connection with the departments that carry out activities of internal control in subsidiaries.
The Audit Department has free access to all information systems, deeds and business data, useful to express an independent judgment with respect to the suitability of the Internal Control System to achieve an acceptable risk profile (Article 8.C.6, letter c) of the Governance Code). For the exercise of its own tasks, the Audit Department is assured the availability of adequate means (Article 8.C.6, letter d) of the Governance Code).
Audit activities can be conducted on the basis of a yearly activity plan examined by the Internal Control Committee or can be determined each time by the Company's top management in relation to specific facts or as a result of particular events.
In February 2009, as envisaged by the international standards issued by the Institute of Internal Audit (IIA), the External Quality Assessment of Terna's Audit Department ended that assessed the effectiveness of the Audit Department in bringing forth its mission and compliance of the activities carried out with the standards for the practice of Internal Auditing issued by the IIA, obtaining the result of "general compliance", the highest positive assessment obtainable according to the IIA.
The Board of Statutory Auditors, within its own activities, can request the Audit Department to carry out assessments on specific operating areas or Company operations.
The Board of Statutory Auditors and the Internal Control Committee timely exchange important information for the accomplishment of the respective tasks.

## Code of Ethics

In May 2002, aware of the moral aspects involved in its core activities, Terna's Board of Directors resolved to adopt its Code of Ethics (that was updated in March 2004) to allow employees and all those having relations with Terna, to operate in the right way in order to establish trust, strengthen the Company's positive reputation and create value.
In 2006, the Code of Ethics underwent an updating process to provide Terna, following the change that rendered it an independent operator in the electricity transmission market, with a set of rules and principles to follow on the basis of its new context of reference.
The new Code of Ethics, which was approved by the Board of Directors on December 21, 2006, explains also in ethical terms, Terna's uniqueness. It underlines the need to respect universal ethical principles, that can be immediately recognized by everybody, and that should be fully adopted by companies. It is not by chance that the Code of Ethics is inspired by the 10 principles of the Global Compact, the most important expression of this vision.
Terna's Code of Ethics is broken down into five sections, which discuss, in this order:

- Terna's fundamental ethical principles, which are organized into general ethical principles (legality, honesty and accountability), that are universal and therefore to be recognized and shared by all, and into four main principles that Terna believes are particularly important, given its activities and nature (good management, respect, fairness and transparency);
- the conduct required, especially from employees, based on three important elements: loyalty to the Company, conflicts of interest and the integrity of Company assets;
- general instructions for the conduct to follow in relations with stakeholders, broken down into eight groups in which Terna requires consistent conduct;
- Terna's commitment to comply with the Code and the conduct required in relation to certain stakeholders;
- the rules implementing the Code and the relevant people responsible for updating it and gathering reports, who should be contacted for any clarifications.

The Code of Ethics was approved in December 2006. It applies to all of Terna Group's subsidiaries for sections 1 (Principles), 2 (Conflicts of interest, Company loyalty and the integrity of Company assets) and for section 3 (Relations with stakeholders) limited to the initial guidelines for the conduct to be followed with the individual categories of stakeholders.
On December 16, 2009 Terna's Board of Directors, based on sustainability, undertook an additional and coherent step resolving to officially join the Global Compact, the multi-stakeholder network promoted by the UN Organization that joins governments, companies, UN agencies, trade union organizations, non-profit organizations and the civil society with the aim of globally promoting the 10 universal principles of human rights, employment, environmental protection and anti-corruption measures.
The establishment of the Ethical Committee between the end of 2009 and the beginning of 2010, was another occasion to focus the contents and give new impulse to the complete implementation of the Code of Ethics by means of a dissemination campaign involving the entire Company.
In completing its ethical commitments towards its stakeholders as set out in the Code of Ethics, Terna annually takes account of its own operations, on a voluntary basis, through the Sustainability Report.

### Organizational Model under Legislative Decree no. 231/2001

Since December 2002, Terna's Board of Directors resolved to adopt an Organizational and Management Model that met the requirements of Legislative Decree no. 231 of June 8, 2001, which introduced into the Italian Law a system of administrative (and criminal) liability for companies with respect to certain types of offences committed by their Directors, managers or employees in the Company's interest or to its benefit. The Model was updated in June 2004, after the Company's shares were listed.
During 2010, the Model was amended following changes in law provisions as per Article 24 ter regarding "organized crime offences" and article 25 bis, 25 novies and 25 novies (bis) regarding, respectively, "offences against industry and trade", "crimes related to the violation of copyright" and "crime of incitement to refrain from issuing statements or to issue false statements", introducing the new Special Section I, relative to organized crime offences and updating the "General Section" and the "Special Sections" "A", "B", "G" and "H" for the other types of offences.
In addition to identifying areas deemed to be mostly at-risk for committing offences (so called "At-risk Areas"), the activity also involved defining conduct principles which all company representatives must comply with in order to prevent such offences, in addition to the provisions already included in the existing procedures within the Company.
This project went hand-in-hand with the Code of Ethics, as the Company believes that the adoption of this Model – regardless of the regulations that made it optional rather than mandatory – is a valid tool in increasing the awareness of those operating in the name and on behalf of Terna and its Group, so that their conduct be correct and transparent in the performance of their activities, to prevent the risk of the offences provided for by the Decree from being committed.
In 2011, due to the extension of the predicate offences category to environmental crimes, pursuant to Article 25 undecies of Legislative Decree no. 231/2001, an assessment was carried out, as well as the mapping of company areas, the roles and responsibilities, indentifying the so-called "At-Risk Areas" and the definition of principles of conduct which company representatives must comply with in order to prevent the occurrence of new predicate offences. Therefore, following said activity, the Model 231 was further broadened through the introduction of the Special Section "L" in connection with "Environmental Offences".

The Model is currently organized into eleven sections:

- a "general section" which describes, inter alia, the content of Legislative Decree no. 231/2001, the objectives of the Model and its implementation, the duties of the Vigilance Body – structured as a collective body – required to monitor the implementation and compliance of the Model, information flows and the penalty system;
- a "special section A", which covers offences committed in dealings with the public administration;
- a "special section B", which discusses Corporate offences;
- a "special section C", which deals with offences of terrorism or subversion of the democratic order;
- a "special section D", on offences against individuals;
- a "special section E", concerning market abuse offences, with the addition of specific "Compliance regulations for the prevention of offences and administrative market abuse offences";
- a "special section F", regarding dealing in stolen goods, money laundering and use of money or assets coming from illegal sources as introduced in Decree no. 231/01 consequent to Legislative Decree no. 231/07 becoming effective;
- a "special section G", regarding manslaughter and serious or very serious injuries committed in violation of the rules on occupational health and safety;
- a "special section H", regarding computer-related offences.
- a "special section I" relative to organized crime offences;
- a "special section L", concerning environmental offences.

The content of this Model is consistent with the guidelines prepared for this purpose by trade associations. It is also in line with the best practices, and represents the final step towards complete accuracy, transparency and accountability in internal and external relations, while offering shareholders a guarantee of efficient and correct management.
Together with the Model, already in 2008, Terna had also approved a specific "Compliance Regulation for the prevention of crimes and administrative offences of market abuse" aimed at providing recipients of the Model another operative tool for evaluating the capacity of its conduct to integrate crimes and administrative offences of market abuse and consequently avoid conduct that could potentially be a source of administrative liability for the Company.
In order to guarantee wider diffusion of the knowledge of the adopted Model, the same is published in the Company's website (www.terna.it) under the Investor Relations section and, since 2010, a widespread training and customized campaign has been carried out involving all employees. In particular, in 2011 an awareness raising campaign based on "At-risk areas" for crimes where everyone operates, and other activities were undertaken aimed at ensuring an effective awareness of regulations and conduct to be followed by all company representatives. Moreover, a manual was drafted and distributed throughout the territory on the "Model for Organization and Management of Procedures" - intended for Terna's personnel called on to implement Model 231 - in order to facilitate a simple reading of the Model but complete in its fundamental elements by clearly indicating proper conduct and conduct to be avoided so as not to incur liability.

### Independent Auditors

The assignment of auditing the annual report and the consolidated financial statements was entrusted, pursuant to the resolution passed by the Shareholders' Meeting of May 13, 2011 on proposal of the Board of Statutory Auditors, to the audit company PriceWaterhouse&Coopers S.p.A. for the 2011-2019 period in replacement of the company KPMG S.p.A., whose appointment expired with no possibility for renewal or extension pursuant to Article 17 of Legislative Decree no. 39 of January 27, 2010.
In drafting the auditing assignment proposal submitted to the Meeting of May 13, 2011, the Board of Statutory Auditors preliminarily assessed the independence requirements of such company with reference to Terna and the Group.

### Executive in Charge of the preparation of the company's accounting documents

In implementation of Article 154-bis of the Consolidated Law on Finance – introduced by Law no. 262 of December 28, 2005 and subsequently modified by Legislative Decree no. 303 of December 29, 2006 – Terna's Shareholders' Meeting of May 24, 2007 provided for in the Bylaws (Article 21.4) the position of the Executive in Charge of the preparation of the company's accounting documents (Executive in Charge), delegating his appointment to the Board of Directors, following the indication by the Board of Statutory Auditors, based on specific requirements of professionalism.
The choice to reserve the appointment and revoking of the Executive in Charge to the Board of Directors was carried out in line with Law provisions that directly acknowledge the Board of Directors a specific task of supervision (Article 154-bis, paragraph 4 of the Consolidated Law on Finance).
The Executive must also be in possession of requirements of integrity indicated by the Law and of professionalism indicated in the Bylaws.
In particular, the Executive in Charge of the preparation of accounting documents must have a total experience of at least three years in:

a) administration activities, finance and control and/or managing functions inherent to the activity of preparation and/or analysis and/or evaluation and/or verification of company documents whose complexity is comparable to accounting documents of the Company; or

b) activity of legal control of the accounts in companies listed in Italian regulated markets or in those of other countries of the European Union; or
c) professional activities or university teaching in financial or accounting subjects.

The Board of Directors, in compliance with the regulations, has immediately appointed as Executive in Charge Luciano Di Bacco, Head of the Administration Department of Terna, after verification of the requirements of integrity and professionalism. Such appointment has also involved the adjustment of the organizational structure of the Company attributing to the Executive autonomy and authority regarding the structure of his Department and granting him a top role directly reporting to the CEO.

The Executive in Charge has certified, as of the 2007 half-year report, compliance, under Article 154-bis, paragraph 2 of the Consolidated Law on Finance, with the action and communications of the Company provided for by the Law or communicated to the market, with reference to the report, even half-year, of the Company, to documents, and the accounting books and records.

The Executive carries out all the activities necessary to give the Board of Directors the possibility to comply with its supervision tasks as per Article 154-bis, paragraph 4 of the Consolidated Law on Finance.

Under Article 154-bis, paragraph 3 of the Consolidated Law on Finance, the Executive prepares suitable administrative and accounting procedures for the preparation of the financial statements, consolidated financial statements and half-year reports, and certifies, together with the delegated administrative bodies, their adequacy and effective application, under paragraph 5 of Article 154, according to the model established with CONSOB regulations, as of the financial statements of the year closing on December 31, 2007.

During 2011, in compliance with the provisions of both Law no. 262/2005 and of the Model adopted by the Company, activities were implemented relating to the adjustment of administrative and accounting procedures, consequent to the normal changes made to processes. Testing operations were also conducted for verifying the implementation of the actual control.

According to the Governance Code, the Executive in Charge assessed, together with the Internal Control Committee, the correct use of the accounting standards.

## Section XII **Directors' interests and related party transactions**

Within the Company and its subsidiaries, Terna, even before listing its shares in the stock market, deemed appropriate to establish the conditions for ensuring that related party transactions were carried out in compliance with the principles of procedural and substantial correctness, in its own interest and as a duty to the market (Article 9.P.1 of the Governance Code).

As of February 22, 2007, in implementing the provisions of the new Governance Code, Terna defined these conditions as part of specific internal procedures submitted in advance to the Internal Control Committee and approved by the Board of Directors. Among other things, these procedures established for the entire 2011 a specific reporting to the Board of Directors and Board of Statutory Auditors that was periodically implemented.

Following the publication of "Regulations regarding related party transactions" issued by CONSOB with resolution no. 17221 dated March 12, 2010, subsequently amended with resolution no. 17389 dated June 23, 2010 ("CONSOB Related Party Regulations"), Terna's Board of Directors – as announced to the market on November 12, 2010 – defined these conditions within a new Procedure ("Procedure for Related Party Transactions"), effective as of January 1, 2011, taking into account the new regulations regarding the provisions of the Civil Code and those of the Governance Code of listed companies (Article 9.P.1 of the Governance Code). The resolution was approved unanimously following the positive opinion of the Committee established for this purpose and formed by independent Directors only (as established by Article 4, paragraph 3, of CONSOB Regulations for Related Parties) whose members were identified among the then Internal Control Committee (Article 9.C.1 of the Governance Code). The new Procedure was published, as of November 12, 2010, on the Company's website (www.terna.it, under the Investor Relations/Corporate Governance section).

Within the new Procedure and pursuant to article 4 of CONSOB Related Party Regulations, the following was implemented:

- Related Parties were identified, Related Party Transactions were defined and the new terms for identifying, approving and implementing the various categories of Related Party Transactions were ruled;
- lower amount Transactions were identified as well as those cases in which the provisions of the Procedure should not be applied (in line with the provisions of articles 13 and 14 of CONSOB Related Party Regulations) having taken into account the size of the Company and the sector it operates in, as well as the ownership structure;
- the terms for forming the Director Committee were identified called upon to express its opinion on the single Transactions of greater or lesser importance, as well as the contents of such opinion and the independence requirements of the Committee member. Furthermore, specific measures were identified should at least 3 independent, non related Directors not be present;
- the rules were established regarding cases in which Terna shall examine or approve transactions of Italian or foreign subsidiaries;
- the terms and time frames were established with which Directors and the Committee for Related Party Transactions should be provided with information on Related Party Transactions and relative documentation;

- the choices were identified as made by the Company with reference to the possibilities included in CONSOB Related Party Regulations.

Compared to previous conduct principles regarding Related Party Transactions adopted by Terna, the new Procedure envisaged lowering the relevance thresholds regarding certain types of Transactions which should be reported to the Board of Directors, so that an enlargement of entitled Related Party Transactions could be obtained, according to the definition indicated by CONSOB in the abovementioned resolution - as transactions of lesser importance.

In 2011, with the shareholders' resolution of May 13, 2011, the statutory amendments required by the Procedure were approved and a census of the Related Parties was conducted, as provided for by Article 4 of the Procedure.

According to the provisions of the document, as a first application, the "Procedure for Related Party Transactions" was submitted for verification of possible amendments to the Board of Directors of Terna, which, on the basis of the opinion provided by the special Committee and taking into account that no criticalities have arisen, did not deem it necessary to change it. Further verifications of the "Procedure for Related Party Transactions" are envisaged, based on such procedure, where deemed necessary, and at least every three months also considering the organizational structure of the Company and of the Group, the assets owned and the effectiveness of the Procedure in its application.

The Related Party Transaction Committee, following the renewal of the outgoing Board of Directors, is presently composed of Salvatore Machì (acting as Coordinator), Romano Minozzi and Paolo Dal Pino, all non-executive and independent Directors; at least one member is also in possession of adequate experience in accounting and finance matters.

The Board identified such Committee as the body in charge of carrying out the role required by "Regulations on Related Party Transactions" issued by CONSOB with resolution no. 17221 of March 12, 2010, subsequently amended with resolution no. 17389 of June 23, 2010, both for the approval of greater importance transactions and for those of lesser importance in the Terna Procedure. The Committee is assigned preliminary duties and powers, proactive and advisory, in evaluations and decisions regarding the aforesaid Related Party Transactions, as well as in relation to possible amendment proposals by the Procedure adopted by Terna. A special "Organizational Regulation of the Related Party Transaction Committee of Terna S.p.A." approved by resolution on December 12, 2010 and in force since January 1, 2011, governs the composition, the duties and the operation of the Committee.

The Company's budget provides for adequate financial resources for carrying out the duties of the Related Party Transactions Committee. Moreover, for purposes of its own evaluation, said Committee may require the Company to utilize specialized, independent experts external to the Company, who are designated by this committee; costs for services rendered by consultants are shouldered by the Company. The methods for holding meetings are governed by the internal ad hoc Organizational Regulations adopted by the Board of Directors on November 12, 2010 and in force since January 1, 2011. Upon invitation by the Coordinator, other people whose presence could be helpful for the smooth performance of the Committee's functions may participate in the meetings of the Related Party Transactions Committee.

During 2011, the Related Party Transactions Committee held four meetings, with the regular participation of its members for a duration of approximately 20 minutes each, in which Company executives were in attendance, whose presence was considered helpful for the best information on the issues on the agenda.

As a result of the renewal of the Board and the new composition of the Committee with new members (May 13, 2011), the first meeting was held by outgoing members and subsequent meetings were carried out by the newly appointed members.

In particular, during 2011, the Related Party Transactions Committee, with ad hoc opinions, supported the Board in verifying the "Procedure for Related Party Transactions" adopted by Terna and the statutory amendments on matters submitted to the Shareholders' Meeting of May 13, 2011, as well as the Departments of the Company charged with approving specific non relevant transactions. All the opinions were favorable.

Terna has also identified specific terms for approving significant transactions carried out by the Company, also through subsidiaries (Article 1.C.1 lett. f) of the Governance Code) and for recognizing and managing situations in which a Director holds his own interest or an interest of third parties regarding a transaction that he should evaluate (Article 9.C.2 of the Governance Code), in compliance with the rules of the Governance Code, according to a specific internal procedure adopted as of 2007 and subsequently updated. For this purpose:

- significant transactions subject to the procedure are identified as: a) transactions that have as their object, amount and terms/time frames of implementation an impact on safeguarding the company assets or the completeness and correctness of Terna's information also of accounting information and that as such create an obligation for Terna to make available to the public an informative document in compliance with provisions by supervisory authorities of financial markets; b) financial transactions whose value exceeds 50 million euros with the exception for transactions included in the budget and in approved financial plans as well as those regarding dispatching activity and all related services;
- significant transactions are subject to prior approval or analysis (in the case of transactions falling under the field of activity of Terna's directly or indirectly controlled companies) of Terna's Board of Directors that may rely on the assistance of one or more independent experts that should express their opinion on the economic conditions and/or the executive terms of the transactions, with the exception for the powers assigned to the CEO for particularly urgent situations;

- the Board of Directors is duly informed on the executive terms of significant transactions, the time frames and economic conditions to implement such transactions, the evaluation process followed, the underlying interests and motivations and any possible risks for Terna and its subsidiaries linked to these transactions;
- the implementation of significant transactions, approved beforehand or subject to the evaluation by the Board of Directors is communicated to the Board of Directors and the Board of Statutory Auditors at least every three months.
- Directors who have an interest (including potential or indirect interests) in the transaction:
  - are required to inform the Board of Directors and Board of Statutory Auditors in due time of the existence of the interest, specifying its nature, terms, origin and scope;
  - are required to leave the Board meeting or refrain from voting at the time of resolving, unless the Board specifically authorizes participation in the related discussions and/or vote;
  - are required to inform the Board of their positions at the time of their appointment and regularly update the Board on them.
- Board resolutions passed in relation to intercompany transactions should be adequately justified and advantageous for the relevant company.

## Section XIII **Appointment of Statutory Auditors**

### Appointment and requirements of Auditors

The terms for appointing the members of the Board of Directors are ruled by article 26 of the Bylaws.
In compliance with the provisions of the Company's Bylaws, the Board of Statutory Auditors is comprised of three Standing Auditors and two Alternate Auditors, who are appointed by the Shareholders' Meeting for a period of three years and may be re-appointed at the end of their term.
All members of the Board of Statutory Auditors must meet the integrity and professionalism requirements as per the special legislation for Statutory Auditors of listed companies (Article 148, paragraph 4 of the Consolidated Law on Finance) now under Ministry for Justice Decree no. 162 of March 30, 2000, as integrated by appropriate Bylaws provisions (Article 26.1 of Bylaws).
Each Auditor may not be Standing Auditor of five or more companies that have issued securities and can hold other assignments of administration and control in share capital companies according to Book V, Title V, Chapters V, VI and VII of the Civil Code within the limits established by the Article 144terdecies of the Issuer Regulations implementing the provisions of art. 148bis of the Consolidated Law on Finance.
All the members of the Board of Statutory Auditors must also possess provided requirements of independence under Article 148, paragraph 3 of the Consolidated Law on Finance.
In implementing law provisions on the matter of privatizations and pursuant to Italian laws regarding listed companies, the entire Board of Statutory Auditors must be appointed using the voting list system, to ensure that the Board includes one Standing Auditor and one Alternate Auditor from minority lists.
On October 18, 2010, Terna's Board of Directors approved the amendments to the Bylaws necessary to adjust it to the novelties introduced by law provisions regarding shareholders' rights of listed companies aiming at favoring the participation of shareholders in the life of the Company (Directive 2007/36/CE and relative implementing Legislative Decree no. 27 dated January 27, 2010). Among other things, amendments involved Article 26.2 of the Bylaws regarding the appointment procedure for the Board of Statutory Auditors and the terms and modalities for depositing the lists.
Such amendments were applied for the first time on occasion of the annual Meeting held May 13, 2011, which, inter alia, also resolved the renewal of the expired company bodies.
On the basis of the novelties and according to the Bylaws, the deposit and publication of lists are ruled by the provisions for appointing the entire Board of Directors, in cases where this is compatible with the existing applicable law and the provisions of Article 26 of the Bylaws for the appointment of the Board of Statutory Auditors.
This system provides – in line with Article 4, paragraph 1bis, of Legislative Decree no. 332 of May 31, 1994 converted into Law no. 474/94 ("Privatization Law") and modified by Legislative Decree no. 27 of January 27, 2010, by art. 148 of the Consolidated Law on Finance and by the implementing rules for the abovementioned provisions included in articles 144ter and following of the Issuer Regulations, that the lists of candidates can be presented by shareholders that, alone or jointly with other shareholders, hold at least 1% of the share capital or a lower amount as envisaged by the law - of shares with voting rights in the meeting. For this purpose CONSOB, implementing the provisions of art. 148 of the Consolidated Law on Finance and articles 144 ter and following of the Issuer Regulations, has established - with Resolution no.17633 dated January 26, 2011 and for the year that ended on December 31, 2010 - the participation stake required for submitting candidate lists to be appointed in Terna's administration and control bodies at 1% of the share capital, taking into account the Company's capitalization, floating capital and owned assets and without prejudice to the lower stake included in the Bylaws.
The presentation and filing of lists must occur at least 25 days from the day established for the Meeting on first call.

Ownership of the minimum stake required to submit lists shall be determined by taking into account the shares that are registered in the name of the Shareholder(s) on the day in which the lists are filed with the Company.
In order to prove the legitimacy of presentation of the lists, entitled Shareholders must present and/or deliver the relative documentation even after the lists have been filed but within the time period set for the publication of the lists.
Pursuant to Article 144 sexies, paragraph 5, of the Issuer Regulations, in the event that on the date due for the submission of the lists for the Board of Auditors only one list has been filed, that is only lists submitted by members who are connected to each other pursuant to applicable law provisions, lists may be submitted up to the third day following said date; In this case, the thresholds set forth above shall be reduced by half.
Each Shareholder may present or assist in the presentation of one list only and each candidate may be on one list only or he will be considered ineligible The lists shall list candidates according to a progressive number and will be divided into two sections, one for the candidates to the office of Standing Auditor and the other for the candidates to the office of Alternate Auditor. The first one of the candidates of each section of the lists must be registered in the register of statutory auditors and must have exercised the activity of legal control of the accounts for a period of at least three years.
Pursuant to Article 148, paragraph 2 of the Consolidated Law on Finance, at least one standing member is appointed by the minority shareholders who, as required by art. 148, paragraph 2 of the Consolidated Law on Finance, are not connected, not even indirectly, with the shareholders who have submitted or voted the list winning for a number of votes.
In compliance with the Italian legislation for listed companies, the Bylaws (Article 26.2) attribute the chairmanship of the Board of Statutory Auditors to the Standing Auditor appointed by the minority list.
To ensure transparency in the procedure for the appointment of the Board of Statutory Auditors, also in line with the provisions of the Governance Code, lists are deposited, pursuant to Article 144 sexies, paragraph 3 of Issuer Regulations and also based on the provisions of Article 10.C.1 of the Governance Code, provided with:

a) information on the identity of the shareholders who have submitted the lists, indicating the total percentage of the shares held;
b) a declaration by shareholders other than those who hold, also as a group, a controlling interest or relative majority, indicating the absence of relationships as set forth in Article 144 quinquies of the “Issuer Regulations” with them. Moreover, Shareholders who submit a “minority list” are subject to the recommendations made by CONSOB Communication No. DEM/9017893 of February 26, 2009 indicated in such declaration;
c) an accurate description of the personal and professional characteristics of the candidates, accompanied - pursuant to Article 2400, last paragraph of the Civil Code - by a list of administration and control positions held within other companies as well as a statement by the candidates certifying possession of the requirements set by the law (including possession of independence requirements pursuant to Article 148, paragraph 3 of the Consolidated Law on Finance) and their acceptance of the candidacy.

Such documents are deposited at the registered office of the Company, and are published in the Company’s website according to the terms established by CONSOB, at least 21 days before the day of the Shareholders’ Meeting (Article 10.C.1 of the Governance Code).
For any replacement of the Statutory Auditors, the terms of Article 26.2 of the Bylaws will be applied. In case one of the Statutory Auditors is replaced, the Alternate Statutory Auditor first on the same list takes his place. If the Chairman of the Board of Statutory Auditors is replaced, this position will be taken by the Alternate Statutory Auditor taken from the same list.
For the appointment of the Statutory Auditors occurring outside the provisions for renewing the entire Board of Statutory Auditors, the Shareholders’ Meeting resolves based on the majority envisaged by the Law and without respecting the abovementioned procedure, but nonetheless so as to ensure a composition of the Board of Statutory Auditors in compliance with the requirements of integrity and professionalism established by the Law.

# Section XIV **Statutory Auditors**

## Composition of the Board of Statutory Auditors

The Board of Statutory Auditors currently in office, appointed by the ordinary Shareholders' Meeting of May 13, 2011, will be in office until the approval of the 2013 financial statements.
According to the resolution passed during the meeting on May 13, 2011, the Board of Statutory Auditors is formed by: Luca Aurelio Guarna (Chairman of the Board of Statutory Auditors appointed by the minority list submitted by shareholder Romano Minozzi and by his subsidiaries), Alberto Luigi Gusmeroli and Lorenzo Pozza (Standing Auditors appointed by the majority list submitted by Cassa Depositi e Prestiti S.p.A.).
Alternate Auditors were also appointed: Stefania Bettoni (included in the minority list submitted by the shareholder Romano Minozzi and by his subsidiaries), and Flavio Pizzini (included in the majority list submitted by Cassa Depositi e Prestiti S.p.A.).
The Auditors appointed represent both lists submitted for said meeting. Further information regarding the submitted lists of candidates and on the results of the voting is available on the Company's website at www.terna.it in the section "Investor Relations/Corporate Governance/Shareholders' Meetings/May 13, 2011". Following the statements made for the appointment, the vote count and after the voting, a standing member was appointed by the minority members that are not connected, not even indirectly, with the members who have submitted or voted the list that won for a number of votes.
From its appointment, the Board of Statutory Auditors is unchanged.
A summary of the professional background of the Standing auditors is provided below.

- **Luca Aurelio Guarna, 39 years old - Chairman of the Board of Statutory Auditors**
  [born in Milan on December 20, 1972]

He has a degree in Business Administration from the Luigi Bocconi University; he qualified for the title of Tax Consultant in 2000 and since 2002 he has been enrolled as Auditor.
He has carried out professional activity with prestigious legal and tax offices and since 2001 he has been a member of the administrative, tax and Corporate consulting Spadaccini office in Milan.
He is presently the Chairman of the Board of Statutory Auditors at Gemina S.p.A. and Standing Auditor in other companies such as: Aereoporti di Roma S.p.A., Delmi S.p.A. (company belonging to the A2A Group which is part of Edison S.p.A.'s holding chain), Eagle Pictures S.p.A. and Bieffe Medital S.p.A.
He has worked as a Professor for the Arthur Andersen network and for the Foundation of Tax Consultants in Milan.

- **Alberto Luigi Gusmeroli, 51 years old - Standing Auditor**
  [born in Varese on February 27, 1961]

He has a degree in Economics from the University of Pavia, School of Economics, with a focus on company finance and credit, enrolled as a tax consultant in the Auditors Register.
He is Chairman of the Board of Auditors of the publishing house Editoriale Nord soc. Coop since 1997 and of Comecor coop a.r.l. since 1990, as well as member of the Board of Auditors of Bancoposta Fondi S.p.A. Sgr (Poste Italiane Group) since 2002 and of Enel Green Power Strambino Solar s.r.l.. He is also a member of the Board of Società Italiana per Azioni per il Traforo del Monte Bianco. Since 2000 he has also been member of the Board of Fondazione Salina, and since 2005 of the Centro Studi sulle Lingue Parlate Locali ed i Dialetti. He is a member of the Commission for study on local bodies of the National Council of Tax Consultants in Rome and general partner of the auditing company Fiduciaria Di Revisione Sas. He was a member of the Board of the Hotel company 3S from 2000 to 2006, Chairman of the Board of Auditors of Frigorcoop from 1992 to 2000 and Auditor in Enel Energia S.p.A. from 2005 to 2007. In the municipalized company Aspem S.p.A. in Varese he was first Board member with powers, from 1998 to 2002, and then member of the Board of Auditors from 2003 to 2009. He has held many positions as consultant, including in Aero Club d'Italia, and he was an auditor in various local bodies as well as Member of the Inspection Committee of the Regional Council of the Region of Lombardy.

- **Lorenzo Pozza, 45 years old - Standing Auditor**
  [born in Milan on October 11, 1966]

He has a degree in Business Administration from the Luigi Bocconi University, tax consultant and auditor.
Since 2001, he has been Associate Professor of Business Administration at the Luigi Bocconi University and Professor of Methodology and Quantitative Standards for Companies after having held various positions as a Professor in International Accounting and Accounting and Budget since 1991 at the same university, and since 1992 at the Corporate Management School (SDA), and since 1996 at the University of Italian Switzerland.
He holds the position of Director or Auditor in various different companies, listed and unlisted, in the industrial, financial, real estate and insurance sectors, among which: Telecom Italia S.p.A., Gas Plus S.p.A., Bracco Imaging S.p.A., Leonardo & Co S.p.A. and Merloni Invest S.p.A.
He also carries out professional activity since 1990 and has been a founding member of the Partners S.p.A. consulting firm.

He is the author of three books on budget and company evaluation as well as of numerous other publications, and has also written articles and essays on this subject for national and international magazines.

During the appointment and taking account of the information provided by the individuals involved, the Board of Directors, based on the envisaged terms, has confirmed and verified the existence of the requirements of integrity, professionalism and independence of the members of the Board of Statutory Auditors appointed by the Shareholders' Meeting held on May 13, 2011.
In the attached table 2, information is included regarding the composition of the Board of Statutory Auditors as of March 20, 2012.
No Standing Auditor holds five assignments in other Italian companies issuing stocks listed in the Italian regulated markets or in other countries of the European Union and in companies issuing financial instruments available to the public in significant amounts pursuant to Article 116 of the Consolidated Law on Finance as defined by Article 2 bis of the Issuer Regulations.
The total number of assignments as Director or Auditor in other companies according to Book V, Title V, Chapters V (S.p.A.), VI (S.A.p.A.) and VII (S.r.l.) of the Civil Code, relevant according to Article 148 bis of the Consolidated Law on Finance, is indicated in the attached table 2. The total number of assignments according to Article 144 quinquiesdecies of the abovementioned Issuer Regulations based on CONSOB resolution no. 17326 dated Mary 13, 2010, is published by CONSOB and is available on its website (www.consob.it). In this regard, it should be remembered that following the amendments to articles 144 terdecies and 144 quaterdecies of the Issuer Regulations as per the CONSOB resolution no. 18079 of January 20, 2012 (published in the Official Journal on February 7, 2012), the limits on the total number of assignments and the consequent obligation to notify CONSOB are not applicable to standing members of the control body who hold the position of standing member of the control body "in one issuer only".
During 2011, the Board of Statutory Auditors held ten meetings which lasted on average approximately one hour and fifty minutes each, with the regular participation of the Standing Auditors.
As a result of the renewal of the Board of Auditors (May 13, 2011), the first five meetings were carried out by the outgoing members and subsequent meetings were carried out by the newly appointed members.
In 2012, all the preliminary meetings are scheduled for reviewing the economic-financial data on the part of the Board of Directors. During the year in progress up to the date of approval of this Report, the Board of Statutory Auditors held 3 meetings.
The Board of Statutory Auditors of February 23, 2012 - on the basis of the criteria set out for evaluating the independence of its own members consistently with the criteria indicated in the Governance Code adopted by the Directors, the same criteria which the new Board of Statutory Auditors also has decided to make reference to, and on the basis of the information provided by each single member – certified that all Standing Auditors met the independence requirement.
Terna's Board of Statutory Auditors, already from March 16, 2007, decided to voluntarily adapt to a system of transparency analogous to that of the Directors in case of operations in which they bear an interest for themselves or third parties (Article 10.C.4 of the Governance Code). This orientation was also confirmed by the new Board of Statutory Auditors in the meeting held on February 23, 2011.
During 2011, the Board of Statutory Auditors carried out the activities that are typical to auditing as envisaged by the national regulations regarding (i) the observance of the Law and of the founding deed, including the respect of principles of proper administration in carrying out Corporate activities, (ii) the adequacy of the organizational structure, of the internal auditing system and of the Company's administrative-accounting system. It has also verified the implementation of the provisions pursuant to Article 114, paragraph 2 of the Consolidated Law on Finance relative to communication obligations. The Board of Statutory Auditors also monitored the independence of the auditing company verifying both the respect of the provisions applicable on the matter, and the nature and entity of the services different from the accounting and auditing provided to Terna and to its subsidiaries by KPMG S.p.A. and the bodies belonging to its network, as well as Pricewaterhouse&Coopers S.p.A., the auditing firm appointed to replace KPMG S.p.A., whose mandated term had expired, and bodies belonging to the network of the latter (Article 10.C.5 of the Governance Code). With respect to the appointment of the auditing firm Pricewaterhouse&Coopers S.p.A., the Board submitted the required proposal to the Shareholders' Meeting.
The Board of Statutory Auditors verified the proper application of criteria and of procedures adopted by the Board of Directors for evaluating the independence of its members and also analyzed the implementation of the regulations pursuant to Legislative Decree no. 231/01 and of the Regulations for the Executive in Charge of the preparation of financial documents pursuant to Law no. 262/05.
In carrying out its activity, the Board of Statutory Auditors was coordinated with the internal Audit Department and with the Internal Control Committee according to the terms included in the previous "Section XI: Internal Control System" (art. 10.C.6 and 10.C.7 of the Governance Code), with the Vigilance Body pursuant to Legislative Decree no. 231/01, with the Executive in Charge pursuant to Law no. 262/05, as well as with the Boards of Statutory Auditors of subsidiaries and with the auditing company.

## Section XV **Investor Relations**

Since its listing on the stock exchange, the Company has believed that is both in its best interest and a duty to the market establishing a constant dialogue, based on the mutual understanding or roles, with all of shareholders and institutional investors: this dialogue is to be carried out in compliance with both the procedure for the disclosure of documents and information outside the Company and the principles included in the "Guide for market disclosures" and in recent regulatory measures and regulations on market disclosure.
To this regard, and also considering the Company's size, it was decided that this dialogue should be facilitated by the creation of specific Company structures.
Accordingly, the Company has set up an (i) Investor Relations Department, which is currently identified as staff of the CEO and has the task of keeping contacts with institutional investors under the responsibility of Mrs. Elisabetta Colacchia (Viale Egidio Galbani, 70 – 00156 Rome – tel. 06 8313 8145 – fax 06 8313 9312 – e-mail: investor.relations@terna.it and (ii) a department for relations with general shareholders within the Corporate Secretary and Legal Affairs Department under the direction of Attorney Filomena Passeggio (Viale Egidio Galbani, 70 - 00156 Rome - tel. 06 8313 8136 – fax 06 8313 8218 – e-mail: azionisti.retail@terna.it) – (articles 11.C.1 and 11.C.2 of the Governance Code).
Furthermore, the Company has further encouraged dialogue with investors by creating a specific section in its website (www.terna.it), where they can find both financial information (financial statements, half year and quarterly reports and presentations to the financial community) and updated information and documents of interest to general shareholders (press releases, the Company structure, the Bylaws and regulations for Shareholders' Meetings, Corporate Governance information and documents, the Code of Ethics and the Organizational and Management Model pursuant to Legislative Decree no. 231/2001, distributed dividends, etc.) (Article 11.C.1 of the Governance Code).

## Section XVI **Shareholders' Meetings**

The Governance Code establishes that the Shareholders' Meetings should be considered as special occasions to initiate fruitful dialogue between shareholders and the Board of Directors (despite the wide-ranging diversification of the communications methods used by listed companies with their shareholders, institutional investors and the market). This was carefully evaluated and fully approved by the Company, which believed it necessary to adopt specific measures to adequately improve the meetings, in addition to guaranteeing the participation of its Directors (Article 11.C.4 of the Governance Code).
Also on the basis of special legislation enacted as expected in relation to listed companies, Terna introduced into its Bylaws a specific regulation aimed at facilitating the gathering of voting proxies for shareholders who are employees of the Company and its subsidiaries, so as to involve them in the decision-making process at the Shareholders' Meetings.
Pursuant to Article 11.1 of the Bylaws, every shareholder that has the right to attend the Shareholders' Meeting can be represented according to the Law, through a proxy.
In order to facilitate the notification of proxies to the Company, with resolution of October 18, 2010, Terna's Board of Directors approved the amendments to the Bylaws necessary for adjusting the Company Bylaws to the novelties introduced by law provisions regarding shareholders' rights of listed companies aiming at favoring the participation of shareholders in the life of the Company (Directive 2007/36/EC and relative implementing Legislative Decree no. 27 dated January 27, 2010) including notification of proxies by electronic means and, according to Article 125 bis of the Consolidated Law on Finance, mentioning such terms from time to time in the notice of call. On that occasion, the Board of Directors deemed appropriate to allow shareholders the possibility to grant proxies together with specific voting instructions to a Designated Company Representative according to Article 135 undecies of the Consolidated Law on Finance without exercising the so-called opt out possibility set by the Consolidated Law on Finance (Article 11.C.3 of the Governance Code).
In order to facilitate the collection of proxies with the shareholders' employed with the Company and its subsidiaries associated with shareholders' associations that meet the requirements envisaged by the existing laws, according to the terms and modalities agreed upon each time with their legal representatives, these associations have made spaces available to be used for communication and for carrying out activities for collecting proxies.
The Bylaws, instead, does not envisage attendance to the Shareholders' Meeting through telecommunications means or through the expression of the right to vote by correspondence or by electronic means.
With regard to the right to attend a Shareholders' Meeting, the Bylaws (Article 10.1) – as modified by the Board of Directors on October 18, 2010 implementing the abovementioned Legislative Decree no. 27 dated January 27, 2010 - envisages that attendance in the Shareholders' Meeting is allowed only to those who have the right to participate in the Meeting and to exercise the voting right pursuant to law provisions in force.
On the basis of this provision and according to existing Article 83 sexies of the Consolidated Law on Finance, eligibility to

participate in the Meeting and exercising the voting right is certified by a notice to the Company, made by an intermediary, in compliance with own accounting books, in favor of the person entitled to voting right on the basis of evidence related to the close of the accounting day of the seventh open-market day prior to the date set for the Shareholders' Meeting in first call, the so-called "record date".
These provisions do not entail any obstacles to the subsequent negotiations of shares. The credit and debit registrations made on accounts subsequent to said term are not material for purposes of legitimizing the exercise of the right to vote in the Shareholders' Meeting. Therefore, those who appear as owners of the Company shares subsequent to said date will not be allowed to participate and vote in the Meeting.
The right for integration of the Agenda on the part of the shareholders', by virtue of the postponement of general nature pursuant to Article 30 of the Bylaws, is held by the shareholders that, also jointly, represent at least 1/40th of the share capital according to the direct provisions of the Law (Article 126 bis of the Consolidated Law on Finance). On the basis of this forecast, Shareholders may submit a written request within ten days as of the publication of the Meeting's notice of call, for the integration of the agenda with additional items, by depositing within the same time frame a report on the items to be discussed on which the proposal is made. The integration of the list of items to be discussed is allowed only for those topics on which the Shareholders' Meeting is authorized to resolve pursuant to the Law. These topics exclude those for which the Law itself envisages that a resolution is made on the proposal by the Directors or on the basis of one of their projects or of a report they have prepared. In case of an integration to the agenda, the modified list of subjects to be discussed during the Meeting must be published according to the same terms as for the notice of call, at least fifteen days prior to the day scheduled for the Meeting.
Starting March 3, 2004, with a special shareholders' resolution, the Company implemented a specific regulation aimed at ensuring the exact and functional running of Shareholders' Meetings, with detailed rules for the various sectors, in compliance with each shareholders' fundamental right to request clarifications on the various issues being discussed, express an opinion and submit proposals (Article 11.C.5 of the Governance Code). With the shareholders' resolution of May 13, 2011, the text of the adopted "Regulations for Terna S.p.A's Shareholders' Meetings" was adjusted to be in line with the provisions of Legislative Decree no. 27, dated January 27, 2010 with regard to the exercising of some rights of shareholders of listed companies. On that occasion, some further adjustments were made in order to better define the scope of some provisions of the Regulations in light of the acquired enforcement practice and to ensure smoother running of the Shareholders' Meetings. The main amendments made, which were illustrated in detail to the shareholders with an ad hoc report to the Shareholders' Meeting, regarded provisions concerning governing the right to participate and vote in a Shareholders' Meeting and provisions concerning the right to pose questions on the items on the agenda, also before the Shareholders' Meeting.
In particular, with regard to the right of each shareholder to take the floor regarding the items on the agenda, Article 6 of the Regulations envisages that those entitled to exercising the right to vote can ask for the floor only once regarding the topics being discussed, presenting observations, requesting information and formulating proposals. The request to have the floor can be submitted at the time the Shareholders' Meeting is held and – unless otherwise stated by the Chairman – until the Chairman himself has not declared the discussion on the topic closed. The terms for such request, for taking the floor and relative order, are established by the Chairman. Considering the topic and the importance of each item discussed, as well as of the number of those requesting the floor and possible questions posed by shareholders before the Shareholders' Meeting which were not answered by the Company, the Chairman predetermines the duration of the reports and the responses – usually not to exceed ten minutes for reports and five minutes for the responses – in order to guarantee that the Shareholders' Meeting can end its activity in a single session. The Chairman and, by his invitation, all those who assist him, respond to the speakers at the conclusion of all the reports, or after each report, taking into consideration also possible questions posed by shareholders before the Shareholders' Meeting which were not answered by the Company. Those that have requested the floor may reply briefly.
Although said Regulation is not included in the Bylaws, it is approved by ordinary meetings under the specific power given to the shareholders by the Bylaws (Article 11.2). The contents of the Regulation have been aligned to the most sophisticated models prepared by trade associations (Assonime and ABI), for listed companies. The "Regulations for Terna S.p.A.'s Shareholders Meetings" can be found in the Company's website under the section: "Investor Relations/Corporate Governance".
The Board of Directors reports to the Shareholders' Meeting on the activities carried out and planned during the financial statements approval and regarding the report on management and provides the shareholders with adequate information in a timely manner, so that they may pass resolutions with full knowledge of the facts (Article 11.C.4 of the Governance Code).
The Shareholders' Meeting is chaired by the Chairman of the Board of Directors, or, in case of his absence or impossibility, by the Deputy Chairman, if appointed, or, in the absence of both, by another person designated by the Board of Directors; should all the above conditions not apply, the Shareholders' Meeting appoints its own Chairman (Article 12.1 of the Bylaws).
The Chairman of the Shareholders' Meeting is assisted by a secretary, even if not a shareholder, designated by those present upon the request of the Chairman, and can appoint one or more vote counters (Article 12.2 of the Bylaws and Article 4 of the Regulations for Terna S.p.A's Shareholders' Meetings). The assistance of the secretary, according to the terms envisaged by the Law, is not necessary if the Chairman waives said assistance or when the minutes of the Shareholders' Meeting are prepared by a notary public, even outside cases in which it is mandatory by law (Article 4 of

the Regulations for Terna S.p.A's Shareholders' Meetings).
The Shareholders' Meeting, unless otherwise stated by the terms envisaged by Article 21.2 of the Bylaws, assigns to the Board of Directors, according to the terms established by the Law, the power to adopt certain resolutions that fall under the Shareholders' Meetings duties that can determine amendments to the Bylaws and resolves on all the topics as established by the Law or the Bylaws (Article 13.1 of the Company Bylaws) according to the indications in the foregoing Section I under the heading: "Company Organization".
The resolutions adopted by the Shareholders' Meeting of significant impact on the Company, capable of amending the Bylaws indicated in Article 6.3 of the Company Bylaws are subject to the "special power" of veto by the Ministry of Economics and Finance as mentioned above in Section II "Information on Ownership Structure"' in paragraphs "Restrictions in share transfer and shares bearing special powers" and "Bylaws amendments".
Unless otherwise established by the Bylaws, the resolutions, both for ordinary and extraordinary Shareholders' Meetings, both on first, second or third call, or on single call, are passed with the majority required by the Law in each case (Article 13.2 of the Bylaws).
In particular, the Bylaws provide that: (i) for transactions with related parties that have not received a favorable opinion from the competent body, the Shareholders' Meeting resolves, in addition to the majority provided for by law, in the presence of unrelated shareholders, as defined by governing regulations, who represent at least 10% of the share capital with voting rights and with a favorable vote by the majority of said unrelated shareholders; (ii) for urgent transactions with related parties that have been submitted by the Directors for an advisory vote, the Shareholders' Meeting adopts resolutions with the majority provided for by law (Article 13.3 of the Bylaws).
During 2011 – with reference to the regulations for minority rights and compatibly with the Company's referenced regulations and rules mentioned above – no significant changes were made in market capitalization of the Company's shares or in the composition of its Corporate bodies for which the Board of Directors had to evaluate the opportunity of proposing to the Shareholders' Meeting any amendments of the Bylaws regarding the percentages established for exercising shares and of the prerogatives set for minority protection (Article 11.C.6 of the Governance Code).

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The hereby attached two tables summarize some of the most significant information included in the fourth, ninth and fourteenth sections of the document. An "Attachment 1" is also enclosed that includes the description of the "Principal characteristics of existing risk management and internal control systems with regard to the financial informative note" (pursuant to Article 123 bis, paragraph 2, letter b) of the Consolidated Law on Finance).

# Table 1

## COMPOSITION OF TERNA'S BOARD OF DIRECTORS AND OF THE COMMITTEES

| | | | BoD | | | | | | | | Int. Contr. Committee | | R.C. | | RPT Committee | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Position** | **Name (Last name and first name)** | **Appointed since** | **In office until** | **List** | **Exec.** | **Non exec.** | **Indep. based on Code** | **Indep. based on Cons. Law on Fin.** | **%** | **Other assignments** | **X** | **%** | **X** | **%** | **X** | **%** |
| Chairman (1) | Roth Luigi | 2 Nov. 2005 | Financial Statements at 31 Dec. 2013 | M | | • | | | 100% | 2 | - | - | - | - | - | - |
| CEO | Cattaneo Flavio | 2 Nov. 2005 | Financial Statements at 31 Dec. 2013 | M | • | | | | 100% | 1 | - | - | - | - | - | - |
| Director | Buscarini Fabio | 13 May 2011 | Financial Statements at 31 Dec. 2013 | m | | • | • | • | 57.14% | 3 | - | - | - | - | - | - |
| Director | Dal Pino Paolo | 28 Apr. 2008 | Financial Statements at 31 Dec. 2013 | M | | • | • | • | 100% | 0 | X | 100% | X | 100% | X | 100% |
| Director | Del Fante Matteo | 28 Apr. 2008 | Financial Statements at 31 Dec. 2013 | M | | • | | | 80% | 2 | X | 100% | - | - | - | - |
| Director (2) | Machì Salvatore | 16 Sept. 2004 | Financial Statements at 31 Dec. 2013 | m | | • | • | • | 100% | 1 | - | - | X | 100% | X | 100% |
| Director | Minozzi Romano | 13 May 2011 | Financial Statements at 31 Dec. 2013 | m | | • | • | • | 71.43% | 0 | - | - | X | 66.67% | X | 33.33% |
| Director | Francesco Pensato | 29 July 2011 | Financial Statements at 31 Dec. 2013 | M | | • | • | • | 100% | 1 | X | 100% | - | - | - | - |
| Director (3) | Polo Michele | 28 Apr. 2008 | Financial Statements at 31 Dec. 2013 | M | | • | • | • | 90% | 0 | X | 75% | - | - | - | - |
| **DIRECTORS WHO RESIGNED FROM THEIR POSITION DURING THE YEAR UNDER CONSIDERATION** | | | | | | | | | | | | | | | | |
| Director | Camporese Andrea | 13 May 2011 | 30 May 2011 | M | - | - | - | - | 100% | - | - | - | - | - | | - |
| Director | Cannarsa Cristiano | 28 Apr. 2008 | 13 May 2011 | M | | • | | | 100% | - | - | - | - | - | - | - |
| Director | Machetti Claudio | 21 March 2007 | 13 May 2011 | m | | • | | | 100% | - | - | - | - | - | - | - |
| Director | Rispoli Vittorio | 13 Jul. 2006 | 13 May 2011 | m | | • | • | • | 66.67% | - | - | - | X | 100% | - | - |

## LEGAL NUMBER NECESSARY FOR SUBMITTING THE LISTS DURING THE LAST APPOINTMENT:

## NUMBER OF MEETINGS HELD DURING THE YEAR UNDER CONSIDERATION

| BoD | ICC. | RC | AC. | EC | RPT Committee |
|---|---|---|---|---|---|
| 10 | 4 | 5 | - | - | 4 |

(1) Until May 13, 2011 also member of the Remuneration Committee. Participation % 100%.
(2) Until May 13, 2011 also member of the Internal Control Committee. Participation % 100%.
(3) Until May 13, 2011 also member of the Committee for Related Party Transactions. Participation % 100%.

Legend

**BoD:** Board of Directors.
**EC:** Executive Committee.
**AC:** Appointment Committee.
**RC:** Remuneration Committee.
**ICC:** Internal Control Committee.
**RPTC:** Related Party Transaction Committee established for approving the Procedure for Related Party Transactions as indicated by the "Regulations regarding related party transactions" issued by CONSOB with Resolution no. 17221 dated 12 March 2010, as subsequently modified by Resolution no. 17389 dated 23 June 2010 ("CONSOB Regulations for Related Parties").
**Position:** indicates whether is Chairman, Deputy Chairman, CEO, etc.
**List:** indicates M/m whether the Director was appointed from the majority list (M) or from the minority list (m).
**Exec.:** it is ticked if the Director can be qualified as an executive.
**Non exec.:** it is ticked if the Director can be qualified as a non executive.
**Indep.:** it is ticked if the Director can be qualified as independent according to the criteria of the Governance Code.
**Indep. Based on Cons. Law on Fin.:** it is ticked if the Director has the independence requirements as per art. 148, paragraph 3 of the Consolidated Law on Finance as indicated by art. 147-ter, paragraph 4 of the same Law.
**%:** indicates the attendance in percentage terms of Directors at the meetings of, respectively, the Board of Directors and of the Committees (in calculating this percentage the number of meetings was considered which the Director attended compared to the number of meetings of the Board or of the Committee that were held during the year under consideration or after his appointment).
**Other assignments:** indicates the total number stated of assignments as Directors or Auditors in other companies listed in regulated markets (also foreign markets), in financial, banking and insurance companies or in large companies, identified on the basis of criteria defined by the Board. In calculating the indicated assignments, those held in subsidiaries, either directly or indirectly controlled, namely Terna's subsidiaries, were not included. When more assignments are held within the same Group, also for a work relation with a company belonging to the Group itself, only the most important assignment is considered. For the list of assignments held by each Director, please see the brief professional resumes included in this Report.
**X:** "X" indicates that the Board Director belongs to the Committee.

# Table 2

## COMPOSITION OF THE BOARD OF STATUTORY AUDITORS

Collegio Sindacale

| Position | Members (Last name and first name) | Appointed since | In office until | List | Indep. Based on Code | % | Number other assignments | Number assignments in issuers |
|---|---|---|---|---|---|---|---|---|
| Chairman | Guarna Luca Aurelio | 28 Apr. 2008 | Financial Statements at 31 Dec. 2013 | m | • | 100% | 29 | 2 |
| Standing Auditor | Gusmeroli Alberto Luigi | 13 May 2011 | Financial Statements at 31 Dec. 2013 | M | • | 100% | 4 | 1 |
| Standing Auditor | Pozza Lorenzo | 28 Apr. 2008 | Financial Statements at 31 Dec. 2013 | M | • | 100% | 9 | 3 |
| Alternate Auditor | Bettoni Stefania | 28 Apr. 2008 | Financial Statements at 31 Dec. 2013 | m | - | - | - | - |
| Alternate Auditor | Pizzini Flavio | 13 May 2011 | Financial Statements at 31 Dec. 2013 | M | - | - | - | - |

## AUDITORS WHO RESIGNED FROM THE POSITION DURING THE YEAR UNDER CONSIDERATION

| | | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| Standing Auditor | Cosconati Marcello | 28 Apr. 2008 | 13 May 2011 | M | • | 100% | - | - |

## LEGAL NUMBER NECESSARY FOR SUBMITTING THE LISTS DURING THE LAST APPOINTMENT: 1%

## NUMBER OF MEETINGS HELD DURING THE YEAR UNDER CONSIDERATION: 10

Legend

**Carica:** Indicates whether is Chairman, Standing Auditor, Alternate Auditor.

**List:** Indicates M/m whether the Auditor was appointed from the majority list (M) or from the minority list (m).

**Indep. based on Code:** it indicates "•" if the Standing Auditor can be qualified as independent according to the criteria of the Code.

**%:** indicates the attendance in percentage terms of the Auditor at the meetings of the Board (in calculating this percentage the number of meetings was considered which the Auditor attended compared to the number of meetings of the Board that were held during the year under consideration or after his appointment).

**Number other assignments:** indicates the total number of other assignments as Director or Auditor in companies as per Book V, Title V, Chapters V (S.p.A.), VI (S.A.p.A.) and VII (S.r.l.) of the Civil Code that are important according to art. 148-bis of the Consolidated Law on Finance. The total list of the assignments, pursuant to art. 144-quinquiesdecies of the abovementioned Issuer Regulations based on CONSOB Resolution no. 17326 dated 13 May 2010 is published by CONSOB and is available on its website (www.consob.it).

**Number assignments in issuers:** indicates the total number of assignments in issuers, taking into account that, following the amendments to articles 144 terdecies and 144 quaterdecies of the Issuer Regulations made based on CONSOB Resolution no. 18079 dated 20 January, 2012, (published in the Official Journal dated 7 February, 2012), the limitations to the total number of assignments and the consequent information obligations to CONSOB shall not be applied for the standing members of the control body holding the position of standing members in the control body of "only one issuer". Art. 144 duodecies, paragraph 1, lett. d) of the Issuer Regulations defines as "issuers" the Italian companies with listed companies in regulated markets in Italy or in other EU countries and the companies issuing financial instruments publicly distributed in a significant way as established by art. 116 of the Consolidated Law on Finance ad as defined by art. 2 bis of the Issuer Regulations.

# Attachment 1

## Principal characteristics of existing risk management and internal control systems with regard to the financial informative note (pursuant to Article 123-bis, paragraph 2, letter b) of the Consolidated Law on Finance)

### Foreword

The Terna Group drafted the "262 Control Model" with the objective of defining operational modalities for assessing the "Internal Control System" hereinafter referred to as (ICS) that oversees the drafting of the financial statements in order to issue the certification required as per paragraphs 2 and 5 of Article 154-bis of the Consolidated Law on Finance.
The ICS that oversees the drafting of the financial statements is in line with the criteria envisaged in the Guidelines of the "Terna Group's Internal Control System" approved by the Board of Directors on December 21, 2006, in which the ICS is recognized as "the entirety of regulations, procedures and organizational structures that through an appropriate identification, measuring and managing process and monitoring of the principal risks, allow a proper Corporate management that is in line with the objects set by Terna".
The provisions of Law no. 262 (dated December 28, 2005 as subsequently modified by Legislative Decree no. 303 dated December 29, 2006) relative to the ICS that oversees the drafting of the financial statements have the principal objective of ensuring that the financial informative note provides a truthful and proper representation of the Company's shareholders' equity as well as its economic and financial position in compliance with the commonly accepted accounting principles.
On the basis of the provisions envisaged by Article 154-bis of the Consolidated Law on Finance, the ICS that oversees the drafting of the financial statements, actively involving all the Corporate departments, is focused on the reliability objectives pursued by establishing adequate "accounting administrative procedures" and by verifying their actual implementation.
Updating the field of activity (scoping) and processes to be analyzed must be carried out by the Executive in Charge (hereinafter referred to as "EIC") at least once a year in order to analyze the variations that have impacted the ICS and integrate/modify accordingly the administrative and accounting procedures.
This update must be appropriately substantiated in order to guarantee the traceability of activities.

### Description of the principal characteristics of the existing risk management and internal control systems with respect to the financial informative note

**a) Phases of the existing risk management and internal control systems with respect to the financial informative note.**

The analysis approach of the ICS that oversees drafting the financial statements adopted by Terna is based on a twofold method of analysis:

#### Individual Company Analysis

Overall analysis (brief) of the individual companies of the Group with reference to 5 elements that form the CoSO report, specifically focusing on the adequacy of the financial informative note. This is mainly an analysis of the infrastructural components of the Internal Control System (the supervisory activities carried out by the Board of Directors, by the Internal Control Committee, by the Board of Statutory Auditors, as well as the Corporate policies and general group policies etc.) conducted in general terms but with a particular focus on the consequences of the quality of the economic and financial information.
The establishment, management and assessment of the ICS at the individual company level is to be carried out by those in charge of the various company departments (management) with regard to their respective duties, in line with the structure of the "individual company" being analyzed.
The objective of the individual company analysis is to identify any shortcomings in the general control of the individual company that would potentially render ineffective even the best structure of controls overseeing the processes.
The assessment is expressed with a "benchmarking" activity with respect to the reference procedures defined or referred to by official bodies or with the international best-practices adopted by companies similar to the Terna Group.
This method is applied by filling out a check list based on the five components of the control system (Control Environment, Risk Assessment, Control Activity, Information System and Communication Flows, Monitoring), developed in specific control objectives.
Controls are assessed on the basis of the following requirements, where applicable:
- Existence of the control tool (organizational structure, legal structure, process);
- Adequate communication regarding the existence of the control tool identified for all the bodies referred to;

- Understanding on the part of the company's employees of their role and responsibility in implementing the identified control tool;
- Appropriate and effective monitoring of the control tool;
- Management support in implementing the control tool;
- Application, or action undertaken by the management aimed at ensuring compliance with the implemented control tool.

### Individual Process Analysis

Analysis of relevant processes by establishing guidelines that define the principal risks on the financial informative note and relative controls aimed at mitigating them.
The individual process analysis allows assessing the action plan and operational level of the controls on Corporate processes and sub-processes on which the financial informative note is based.
The terms for carrying out this analysis are the establishment of administrative and accounting procedures for preparing the financial statement/consolidated financial statements/half-year report that include the execution of specific control activities aimed at preventing the occurrence of risks of significant errors in financial statements during the development of the processes. The process analysis and the subsequent establishment of administrative and accounting procedures requires the selection of "significant processes". For this purpose, it is necessary to carry out specific "scoping" in order to identify both the significant items in the financial statements/financial informative note as well as associate the significant information to the processes. The relevance of the financial informative note is assessed with reference to the possible consequence that its omission or misrepresentation could determine in decisions made by the individuals who are notified about the note through the financial statements. With regard to the above, quantity parameters are identified, that are normally defined in terms of percentages compared to income before taxes, as well as quality parameters capable of rendering an information relevant, even if the amount is lower than the level of relevance identified.
Identifying significant information is carried out through the combination of quantity parameters, linked to the level of significance defined for Terna and quality parameters linked to the specific risk for financial statements sections or informative notes. Identifying quality parameters consists in considering possible "factors" that render significant various calculations, even if these do not exceed the threshold of materiality, by themselves. Investors could demonstrate a certain interest in various calculations in the financial statements that represent an important performance indicator or an important indicator for the sector they belong to. The association of the information identified as being significant for the relative processes they are based on allows concentrating identification activities on those processes that can determine significant errors regarding the financial information. Each selected significant information/item in the financial statements must be associated with the processes that contribute to its elaboration, in order to determine the significant processes.
On the basis of quality and quantity parameters, after having defined the significant information and having selected the relevant processes, the EIC establishes the guidelines for "risk activities and controls" that represent administrative and accounting procedures and assesses their adequacy and actual implementation (assessment of their operational level).
For this purpose, the analysis of significant processes occurs through the following operational steps:

- defining and analyzing activities that form the processes ("mapping");
- identifying and assessing risks for each activity and their being associated with the control objectives;
- identifying and assessing existing controls;
- assessing the operational level of existing controls.

Analyzing activities that form the processes ("mapping") is aimed at clearly identifying the process that creates the data or the comment to be represented in the financial statements, from identifying the initial event that originates it up to its being included in the accounting prospects or in the notes. Mapping activities that form the processes are functional to the final objective of applying controls along the entire process of data creation or for the notes commenting the financial statements and should be capable of ensuring that the information having an administrative impact is collected, processed and sent correctly and in a timely fashion. For every process, for mapping purposes and the subsequent association of the risks and controls, the "key" elements must be identified that are useful in identifying existing risks and controls.
Verifying the effectiveness of the action plan and the actual operational level of the "key" controls is carried out through a testing activity that is conducted by a dedicated structure, using sampling techniques that are recognized by the international best practices. Control assessment, where deemed necessary, can involve identifying compensatory controls, corrective measures and improvement plans. The results of these activities are submitted to the evaluation of the Executive in Charge who in turn notifies the company executives.

**b) Roles and Departments involved.**

### The Executive in Charge

Is responsible for:

- annually updating the field of activity and the significant processes considering the factors of change/risk communicated by the Directors of Terna S.p.A. and by the management of the companies that are individually significant;

- establishing and updating adequate administrative and accounting procedures for drafting the financial statements and the consolidated financial statements;
- providing, with the collaboration of the Human Resource and Organization Department, to disseminate administrative and accounting procedures and action plans;
- supporting the Directors of Terna S.p.A. and the management of the companies that are individually significant in executing operational, control and reporting activities that are part of their specific duties.
- The EIC can rely on the assistance of qualified external companies with specialized professional staff for carrying out plan assessment activities and the assessment of the operational levels of controls over administrative and accounting procedures.

### The Internal Audit and Risk Management

Are responsible for:

- supporting the EIC in its activities for assessing the adequacy and actual application of administrative and accounting procedures for drafting the financial statements and the consolidated financial statements and the suitability and the proper operation of the Internal Control System and relative mechanisms for risk management;
- coordinating with the EIC in defining the Annual Audit Plan for administrative and accounting processes in order to take into account the results of the operational risk analysis carried out by the company departments;
- providing the EIC with a suitable information flow regarding the results of activities connected with the audit plan for administrative and accounting processes, with the modalities shared with the EIC;
- in case of involvement in specific testing activities, ensuring the necessary collaboration and changes in the audit plan and in defining priorities also, if necessary, with the assistance of the administrative body in charge.

### Terna S.p.A.'s Directors

Are responsible for:

- coordinating those in charge of individual controls in executing the controls they are responsible for;
- coordinating individual controls in establishing and implementing the Action Plans;
- supporting the activities carried out by the EIC and ensure access to all documents/information useful in carrying out his activities;
- preparing and forwarding in the time frames established by the reporting calendar the certifications regarding the control activities and their operational level.

### The management of the companies that are individually significant

Is responsible for:

- coordinating those in charge of individual controls in executing the controls they are responsible for;
- assessing, in collaboration with the EIC, the ICS of the company that is individually significant;
- preparing and forwarding, in the time frame established by the reporting calendar, the certifications regarding the ICS of the company that is individually significant.

To enable the EIC and the administrative bodies in charge to issue the certificates in compliance with Article 154-bis of the Consolidated Law on Finance introduced with Law no. 262/2005, it was necessary to define an internal system of "chain" certificates with the objective of ensuring the adequacy and actual implementation of administrative and accounting procedures drafted as part of the "262 Project", of preparing and disseminating the Plan for corrective measures, where necessary, and to update such procedures.

The certification, issued with the CONSOB form, is based on a complex evaluation process that includes:

- collecting internal "chain" certificates issued by the Directors of Terna S.p.A. and by the management of the companies that are individually significant. The existence of a periodic reporting flow allows carrying out the following:
- periodic assessment of the plan for existing controls and consequent updating of administrative and accounting procedures;
- assessment of the operational level of existing controls and the subsequent certification of the actual implementation of administrative and accounting procedures;
- assessment of the shortcomings (absence of control or failure to execute controls) that emerge with reference to their impact on the informative note on the financial statements;
- the assessment of the actual operational level of administrative and accounting procedures carried out by the EIC;
- the final assessment of the adequacy of administrative and accounting procedures by the CEO and the EIC. This activity is supported by the assessment of the plan for specific controls as well as by that for their operational level as mentioned above. It is therefore carried out overall with reference to the probability that following one or more significant shortcomings an error in the financial statements could occur and with reference to the risk that this error may have been significant.

Any significant shortcomings highlighted by the assessment process must be immediately notified jointly with the outcome of the compensatory controls carried out by the CEO and the EIC, to the Internal Control Committee, to the Vigilance Body and to Terna S.p.A.

# Glossary

**Connection**
Set of grid elements consisting of the transmission line and the stalls at the ends of the same, including the relative circuit sectioning devices. Classification of connections by voltage level is carried out with reference to the nominal voltage. The length of the connection is normally the length of the line constituting the actual link.

**Connection line**
Any power line that links the power distribution plant with the user's plant, or the power distribution plant with the connection station.

**Development**
Intervention within the electricity grid involving an adaptation or expansion of the transport, transformation, connection and interconnection capacity, an increase in operating flexibility of the grid or a disposal of grid elements.

**Dispatching**
Electricity cannot be stored. It is therefore necessary to continuously produce the quantity of energy requested by consumers and deliver it to the National Transmission Grid in such a way as to keep electricity supply and demand in equilibrium, thereby ensuring continuing and security in supplying this service. Management of these flows of electricity along the grid is known as "dispatching".

**Frequency**
Represents the number of oscillations per second, during which the value of an alternating quantity, such as voltage, varies from positive polarity to negative polarity. It is measured in Hertz (Hz).

**Generator**
Electrical machine that transforms a source of primary energy into electricity.

**Gigawatt (GW)**
Unit of measurement equal to one billion watts (1,000 megawatts).

**Grid management**
The set of activities and procedures that bring about operation and the operating plan, under every condition, of an electrical network. Said activities and procedures include the management of electricity flows, interconnection devices and the necessary auxiliary services, as well as the decisions for maintenance and development measures.

**Gross production of electricity**
Sum of the quantities of electrical energy produced, measured at the electrical generator terminals.

**High voltage**
Nominal voltage greater than 35 kV and less than or equal to 220 kV.

**High-voltage electricity line**
An electricity line is a system that connects two power stations, or a power station and an energy input or withdrawal point. The length of an electricity line (km/line) is expressed as the length of the circuits projection over the ground (geographical length).

**High-voltage power station**
A transfer power station is the part of the grid used both for dividing electricity among the grid's lines and for transferring electricity among grids with different voltages.

**Interconnection line**
High-voltage power line in alternating current (a.c.) or direct current (d.c.) which links two different electrical transmission or distribution grids or even two generation plants.

**Interconnection of electricity grids**
Connection between electricity grids required for the transfer of electricity.

**Interoperability of electricity grids**
Operating method for the completion of management, operation, maintenance and development activities for two or more interconnected grids, in order to ensure simultaneous and coordinated functioning of the same.

**kilowatt-hour (kWh)**
Unit of measurement that expresses the quantity of electricity equal to 1,000 watts provided or requested in one hour.

**kW**
Unit of measurement of power (1 kW=1000 J/sec).

**kWh**
Unit of measurement of energy.

**Maintenance**
Measures and intervention aimed at the maintenance or restoration of efficiency and proper functioning of electricity plants, taking into account any declines in performance.

**Maximum total transport capacity on interconnection with foreign countries**
Maximum transport capacity for importing along the lines of the interconnection grid with the electricity plants of neighbouring countries.

**Medium voltage**
Nominal voltage greater than 1 kV and less than or equal to 35 kV.
**Megavolt-ampere (MVA)**
Unit of measurement of the apparent electrical power.
**Megawatt (MW)**
Unit of measurement equal to one million watts.
**National Transmission Grid (NTG)**
National electricity transmission grid as defined by the Decree of the Ministry of Industry of 25 June 1999 and subsequent amendments and additions.
**Net production of electricity**
Sum of the quantities of electrical energy produced, measured at the outgoing points of the production plants.
**Operations planning**
Preparation of plans and schedules for operation of the electricity system.
**Peak power**
The highest value of electrical power supplied or absorbed at any point of the system during a specific time interval.
**Planning**
Definition of the usage plans, for a specific period of time, for the available means of production and transmission, in order to satisfy the energy requirements with respect to quality and continuity of service.
**Power station**
Part of a grid, concentrated and closed within a specific site, used to distribute electricity among the lines of a grid, transfer electricity among grids at different voltages and transform electricity into the lowest voltage for the user.
**Producer**
Natural or legal person that produces electricity, regardless of ownership of the generation plant.
**Production**
Generation of electrical energy, in any way.
**RAB (Regulatory Asset Base)**
Value of the net capital invested, as recognised by the Italian Authority for Electricity and Gas for transport and distribution companies for the purposes of determining the applicable tariffs.
**Requirement**
Demand for electrical energy to be satisfied by the national electricity system. It shows a variable trend throughout the day, month and year.
**Stall**
Set of power plants and accessory systems linked to a power line or transformer that links said elements to the grid with the busbars of a power station.
**Switch**
Sectioning and manoeuvring device able to carry and interrupt current under normal operating conditions, as well as during specific exceptional operating conditions, such as in the case of short circuits.
**Switching station**
Part of a grid consisting of the set of equipment used to distribute the electricity among the lines of a grid at the same level of voltage.
**Transformation station**
Part of a grid consisting of the set of equipment used to transfer electricity between grids with different voltages.
**Transformer**
Electrical machine used for the connection and transfer of energy between grids at different voltage levels.
**Transmission**
Electricity transport and transformation activities along the interconnected high- and very-high-voltage grid for the purposes of delivery to clients, distributors and recipients of self-produced energy.
**Transmission activity**
The activity of transporting and transformation electricity across the grid.
**Transmission line**
High- and very-high-voltage power line, overhead or cable, used for the transport of electricity from the production plants to the distribution systems or to users.
**Unified management of the grid**
Coordinated management of all portions of the Grid.
**Very-high voltage**
Nominal voltage over 220 kV.
**Volt**
Unit of measurement of voltage.
**Watt**
Unit of measurement of electric power.

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