



# Audit Report on Madrileña Red de Gas, S.A.U.

(Together with the Financial Statements of  
Madrileña Red de Gas, S.A.U. for the year ended  
31 December 2019)



KPMG Auditores, S.L.  
Paseo de la Castellana 259 C  
28046 Madrid

## **Independent Auditor's Report in accordance with International Standards on Auditing**

To the Directors of Madrileña Red de Gas, S.A.U.

### **Opinion**

---

We have audited the financial statements of Madrileña Red de Gas, S.A.U. (the "Entity"), which comprise the balance sheet at 31 December 2019, and the income statement, statement of changes in equity and statement of cash flows for the year then ended, and the explanatory notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view, in all material respects, of the financial position of the Entity at 31 December 2019 and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards adopted by European Union (IFRS-EU).

### **Basis for Opinion**

---

We conducted our audit in accordance with International Standards on Auditing (ISA). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report.

We are independent of the Entity in accordance with the IESBA (International Ethics Standards Board for Accountants) Code of Ethics, and we have fulfilled our other ethical responsibilities in accordance with the IESBA Code of Ethics.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

### **Emphasis of Matter**

---

We draw attention to note 3.1.3 to the accompanying financial statements, which states that the comparative financial statements for the prior year differ from the financial statements for 2018 that were audited by other auditors, due to the recognition of the retrospective correction made as indicated in the aforementioned note to the financial statements. Our opinion is not modified in respect of this matter. On 27 March 2019 other auditors issued their unqualified audit report on the aforementioned financial statements for 2018.



## **Other Matter**

---

As mentioned in note 3.1.1 to the accompanying financial statements, these financial statements have not been prepared to meet legal requirements. They have been prepared voluntarily to present the financial position and performance of the Company in accordance with International Financial Reporting Standards adopted by European Union and have been audited applying International Standards on Auditing. Under no circumstances may this report be considered an auditor's report in the terms provided in legislation regulating the audit of accounts in Spain.

In compliance with legal the regulations in Spain, Madrileña Red de Gas, S.A.U. has formulated its annual accounts in accordance with the applicable financial statements auditing standards in Spain, on December 31, 2019 on which we gave our separate audit opinion on May 5, 2020.

## **Other Information**

---

The Directors are responsible for the other information. The other information comprises the directors' report but does not include the financial statements or our auditor's report thereon.

Our opinion on the financial statements does not cover other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If, based on the work that we have performed, we conclude that there is a material misstatement of this other information, then we are required to report that fact. We have nothing to report in this regard.

## **Directors' Responsibilities for the Financial Statements**

---

The Directors are responsible for the preparation of the accompanying financial statements in such a way that they give a true and fair view in accordance with International Financial Reporting Standards, and for such internal control as the Directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the Directors are responsible for assessing the Entity's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Directors either intend to liquidate the Entity or to cease operations, or has no realistic alternative but to do so.

## **Auditor's Responsibilities for the Audit of the Financial Statements**

---

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion.



Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISA will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISA, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Directors.
- Conclude on the appropriateness of the Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves a true and fair view.

We communicate with those charged with governance of Madrileña Red de Gas, S.A.U. regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

KPMG Auditores, S.L.  
Inscrito en el R.O.A.C nº S0702

Eduardo González Fernández  
Inscrito en el R.O.A.C nº 20.435

5 de mayo de 2020



## **MADRILEÑA RED DE GAS, S.A.U.**

Financial statements prepared under IFRS-EU corresponding to the year ended on  
December 31<sup>st</sup> 2019



**MADRILEÑA RED DE GAS, S.A.U.**

**BALANCE SHEET AS AT DECEMBER 31<sup>st</sup> 2019**  
**(Expressed in thousand of euros)**

<b>ASSETS</b>	<b>Note</b>	<b>31/12/2019</b>	<b>31/12/2018 Restated *</b>	<b>01/01/2018 Restated *</b>
<b>NON-CURRENT ASSETS</b>		<b>1,240,484</b>	<b>1,202,026</b>	<b>1,219,420</b>
Intangible assets	7	808,349	806,621	803,853
Property, plant and equipment	8	354,862	368,619	383,015
Non-current investments in group companies	9	54,734	-	-
Financial assets	9	1,006	1,854	5,273
Deferred tax assets	17	21,533	24,932	27,279
<b>CURRENT ASSETS</b>		<b>145,723</b>	<b>118,857</b>	<b>678,874</b>
Inventories	11	2,570	2,651	3,508
Trade and other receivables	9,10	39,137	52,490	58,580
Deferred expenses		590	674	761
Cash and cash equivalents	12	103,426	63,042	616,025
<b>TOTAL ASSETS</b>		<b>1,386,207</b>	<b>1,320,883</b>	<b>1,898,294</b>
<b>EQUITY AND LIABILITIES</b>	<b>Note</b>	<b>31/12/2019</b>	<b>31/12/2018 Restated *</b>	<b>01/01/2018 Restated *</b>
<b>EQUITY</b>		<b>298,085</b>	<b>233,274</b>	<b>304,800</b>
Capital	13	1,048	1,048	1,048
Share premium	13	100,354	100,354	222,954
Reserves	13	131,722	80,867	64,298
Profit/(loss) for the year		64,961	51,005	16,500
<b>NON-CURRENT LIABILITIES</b>		<b>1,041,445</b>	<b>1,028,529</b>	<b>1,017,442</b>
Provisions	16	4,761	5,276	5,737
Other non-current liabilities	9,14	1,849	1,656	1,841
Payables to related parties	9,14,20	943,839	942,640	941,481
Deferred income	15	30,892	28,720	28,016
Deferred tax liabilities	17	60,104	50,237	40,367
<b>CURRENT LIABILITIES</b>		<b>46,677</b>	<b>59,080</b>	<b>576,052</b>
Provisions	16	1,705	2,336	2,854
Financial liabilities	9,14	454	84	4,460
Payables to related parties	9,14,20	12,003	12,007	517,587
Trade and other payables	9,14	32,515	44,653	51,151
<b>TOTAL EQUITY AND LIABILITIES</b>		<b>1,386,207</b>	<b>1,320,883</b>	<b>1,898,294</b>

Notes 1 to 24 set out in the attached report form an integral part of these financial statements. The Company initially applied IFRS 16 as at 1 January 2019, using the modified retrospective approach. Under this approach, comparative information is not restated.

(\*) The 2018 comparative information has been restated to reflect the correction of errors.

**MADRILEÑA RED DE GAS, S.A.U.****INCOME STATEMENT CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019****(Expressed in thousand of euros)**

<b>CONTINUING OPERATIONS</b>	<b>Note</b>	<b>31/12/2019</b>	<b>31/12/2018 Restated *</b>
Revenues	18	184,146	186,278
Raw materials and consumables	18	(10,294)	(16,074)
Self-constructed assets		1,060	904
Other income	15	2,184	2,076
Staff costs	18	(11,955)	(11,668)
Other operating expenses	18	(20,614)	(21,936)
Amortisation and depreciation	7,8	(29,111)	(28,222)
Impairment and gains/(losses) on disposal of fixed assets		(4)	-
Other results	18	(1,704)	(746)
<b>OPERATING PROFIT</b>		<b>113,708</b>	<b>110,612</b>
Financial income	18	1,773	33
Financial costs	18	(29,120)	(42,896)
<b>NET FINANCIAL EXPENSE</b>		<b>(27,347)</b>	<b>(42,863)</b>
<b>PROFIT BEFORE INCOME TAX</b>		<b>86,361</b>	<b>67,749</b>
Income tax	17	(21,400)	(16,744)
<b>PROFIT FOR THE PERIOD</b>		<b>64,961</b>	<b>51,005</b>

Notes 1 to 24 set out in the attached report form an integral part of these financial statements. The Company initially applied IFRS 16 as at 1 January 2019, using the modified retrospective approach. Under this approach, comparative information is not restated.

(\*) The 2018 comparative information has been restated to reflect the correction of errors.

**MADRILEÑA RED DE GAS, S.A.U.**

**STATEMENT OF CHANGES IN EQUITY CORRESPONDING TO THE YEAR ENDED  
ON DECEMBER 31<sup>st</sup> 2019  
(Expressed in thousand of euros)**

**A) STATEMENT OF COMPREHENSIVE INCOME**

	<u>Note</u>	<u>31/12/2019</u>	<u>31/12/2018</u>
Profit for the period		<u>64,961</u>	<u>51,005</u>
<i>Items that will not be reclassified to profit or loss:</i>			
On actuarial gains and losses and other adjustments (net of tax)	16	(150)	69
Other comprehensive income for the period, net of tax		<u>(150)</u>	<u>69</u>
Total comprehensive income for the period		<u>64,811</u>	<u>51,074</u>

Notes 1 to 24 set out in the attached report form an integral part of these financial statements.



**MADRILEÑA RED DE GAS, S.A.U.**

**STATEMENT OF CHANGES IN EQUITY CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019**  
(Expressed in thousand of euros)

**B) TOTAL STATEMENT OF CHANGES IN EQUITY**

	Capital (Note 13)	Share premium (Note 13)	Reserves (Note 13)	Profit/(loss) for the period (Note 13)	Total
<b>BALANCE AT 31 DECEMBER 2017</b>	<b>1,048</b>	<b>222,954</b>	<b>64,298</b>	<b>16,500</b>	<b>304,800</b>
Profit for the period	-	-	69	51,005	51,074
Operations with shareholders or owners	-	-	-	-	-
Dividends	-	(122,600)	-	-	(122,600)
Other changes in equity	-	-	16,500	(16,500)	-
<b>BALANCE AT 31 DECEMBER 2018</b>	<b>1,048</b>	<b>100,354</b>	<b>80,867</b>	<b>51,005</b>	<b>233,274</b>
Profit for the period	-	-	(150)	64,961	64,811
Operations with shareholders or owners	-	-	-	-	-
Dividends	-	-	-	-	-
Other changes in equity	-	-	51,005	(51,005)	-
<b>BALANCE AT 31 DECEMBER 2019</b>	<b>1,048</b>	<b>100,354</b>	<b>131,722</b>	<b>64,961</b>	<b>298,085</b>

Notes 1 to 24 set out in the attached report form an integral part of these financial statements.

# MADRILEÑA RED DE GAS, S.A.U.

## CASH FLOW STATEMENT CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

A) CASH FLOW FROM OPERATING ACTIVITIES	Notes	31/12/2019	31/12/2018 Restated *
1. Profit/(loss) for the period before income tax		86,361	67,749
2. Adjustments for:		54,887	69,949
Amortisation and depreciation (+)	7,8	29,111	28,222
Change in provisions (+/-)		596	-
Impairment adjustments (+/-)		17	940
Release of grants (-)	15	(2,184)	(2,076)
Financial income (-)		(1,773)	(33)
Financial expenses (+)	18	29,120	42,896
3. Changes in working capital		(1,766)	(111)
Inventories (+/-)		81	746
Trade and other receivables (+/-)	10	13,421	5,061
Other current assets (+/-)		84	87
Creditors and other payables (+/-)	14	(13,321)	(4,333)
Other non-current liabilities (+/-)		(2,031)	(1,672)
4. Other cash flow from operating activities		(34,878)	(53,197)
Interest paid (-)	14	(27,928)	(47,356)
Interest received (+)		-	33
Income tax (paid)/received (+/-)	17	(6,950)	(5,874)
Other amounts paid (received) (-/+)		-	-
A) Cash flow from operating activities (+/-1+/-2+/-3+/-4)		104,604	84,390
B) CASH FLOW FROM INVESTING ACTIVITIES		(66,087)	(16,330)
6. Amounts paid on investments (-)		(53,000)	-
group and associate companies		(3,557)	(3,963)
Intangible assets	7	(9,530)	(12,367)
Property, plant and equipment	8	848	4,609
7. Amounts collected from divestments (+)		802	3,418
Other financial assets		46	1,191
Fixed assets		(65,239)	(11,721)
B) Cash flow from investing activities (7-6)			
C) CASH FLOW FROM FINANCING ACTIVITIES		1,399	1,323
9. Amounts collected from grants		1,399	1,323
Grants	14	(380)	(500,000)
10. Collections and payments financial liability instruments		-	(500,000)
Debts with group companies and associates (+).		(380)	-
Other financial liabilities IFRS payments 16 (-)		-	(126,975)
11. Dividend payments		1,019	(625,652)
C) Cash flow from financing activities			
NET INCREASE/(DECREASE) IN CASH OR CASH EQUIVALENTS		40,384	(552,983)
Cash and cash equivalents at the beginning of the period		63,042	616,025
Cash and cash equivalents at the end of the period		103,426	63,042

Notes 1 to 24 set out in the attached report form an integral part of these financial statements. The Company initially applied IFRS 16 at 1 January 2019, using the modified retrospective approach. Under this approach, comparative information is not restated.

(\*) The 2018 comparative information has been restated to reflect the correction of errors.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

#### **1. General information**

Madrileña Red de Gas, S.A.U. (hereinafter, the Company) is a Spanish public limited liability company, that was incorporated on July 3<sup>rd</sup>, 2009 under the registered name of GEM Servicios Comunes 2, S.L. The Company subsequently changed its registered name to Madrileña Servicios Comunes, S.L.U. on February 15<sup>th</sup>, 2010, and then to its current name as a result of the merger through absorption with Madrileña Red de Gas, S.A.U. on June 30<sup>th</sup>, 2011.

Its current registered and tax address is in "Centro Empresarial Arco", calle Virgilio nº 2-B Edificio 1, 28223 Pozuelo de Alarcón (Madrid).

Madrileña Red de Gas, S.A.U. is the company resulting from the merger through absorption of Madrileña Red de Gas, S.A.U. (as the merging company) and Madrileña Red de Gas II, S.A.U. (as the merged company) carried out on December 17<sup>th</sup>, 2013.

The merged company was incorporated on September 13<sup>th</sup>, 2010, resulting from the merger through absorption of Nueva Madrileña de Gas, S.A.U. (as the merging Company) and Madrileña Red de Gas II, S.A.U. (as the merged company) carried out on May 31<sup>st</sup>, 2012. Under this transaction the merging company Nueva Madrileña de Gas, S.A.U. changed its corporate form and its name to Madrileña Red de Gas II, S.A.U.

On May 7<sup>th</sup> 2015, the Company Elisandra Spain V, S.L.U. acquired the 100% of the Company's shares of MSIP Violin BV, and became part of the Group, whose ultimate parent company is Elisandra Spain IV, S.L (sole shareholder of Elisandra Spain V, S.L.U.), whose shareholders turn are Realgaz, S.A.S (formerly called C41, S.A.S), Stichting Depositary PGGM Infrastructure Funds, JCSS Mike S.A.R.L and Lancashire County Pension Fund.

On July 25<sup>th</sup>, 2017, the General Meeting of Shareholders approved the transfer of the shareholdings held by Lancashire County Pension Fund, representing 12.50% of the share capital of Elisandra Spain IV, S.L to LPPI Infrastructure Investment LP. By October 2017 Lancashire County Pension Fund had contributed its 12.5% stake in the company to the pooled investments vehicle, LPPI Infrastructure Investments LP, which is owned by it and the London Pension Fund Authority.

The Company forms part of the Elisandra Spain IV, S.L. Group, and its direct parent is Elisandra Spain V, S.L. On March 25<sup>th</sup> 2020 the directors of the Elisandra Spain IV, S.L. Group authorised the issue of the consolidated annual accounts for 2019, prepared under IFRS-EU (the 2018 accounts were authorised for issue on March 22<sup>nd</sup> 2019). The consolidated annual accounts will be filed at the Madrid Mercantile Registry.

The Company's corporate purpose is the distribution and secondary transmission of natural gas as well as the distribution and sale of piped liquefied petroleum gas (LPG). The activities included in its corporate purpose may be carried out in full or in part indirectly through the holding of shares or interests in companies having identical or analogous purposes in accordance with legislation on the hydrocarbon sector.

MADRILEÑA RED DE GAS, S.A.U.

**NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED  
ON DECEMBER 31<sup>st</sup> 2019  
(Expressed in thousand of euros)**

**2. Regulatory framework**

**Main characteristics of the Spanish gas sector**

The Spanish gas sector is regulated by Law 34/1998, of October 7<sup>th</sup> on the hydrocarbons sector, amended by Law 12/2007, of July 2<sup>nd</sup> Royal Decree-Law 13/2012 and Law 18/2015, of May 21<sup>st</sup> as well as Law 18/2014, of October 15<sup>th</sup> and by its enabling regulations, the most relevant being Royal Decree 1434/2002, of December 27<sup>th</sup> Royal Decree 949/2001, of August 3<sup>rd</sup> and Royal Decree 984/2015, of October 30<sup>th</sup>.

The Ministry of the Ecological Transition and Demographic Challenge, (previously Ministry of the Ecological Transition), is the competent organization responsible for the regulation of the gas and electricity industries, while the National Markets and Competition Commission (CNMC) is the regulatory authority in charge of maintaining and ensuring effective competition and transparent functioning of the Spanish energy industries. Prior to the publication of Law 3/2013 of June 4<sup>th</sup>, these functions were performed by the National Energy Commission (CNE), which was later integrated into the CNMC. The Ministries belonging to the Regional Governments also have competencies in legislative enactment and regulatory powers.

Royal Decree Law 1/2019, of 11 January, on urgent measures to bring the competencies of the National Commission on Markets and Competition into line with the requirements of Community Law with respect to Directives 2009/72/EC and 2009/73/EC of the European Parliament and of the Council, of 13 July 2009, on the common rules for the internal market in electricity and natural gas, amended Law 3/2013, of 4 June, on the creation of the National Commission on Markets and Competition; Law 34/1998, of 7 October, on the hydrocarbon sector; Law 24/2013, of 26 December, on the Electricity Sector; and Law 18/2014, of 15 October, approving urgent measures for growth, competition and efficiency.

With respect to the aspects subject to amendment, first of all, a mechanism is brought in to ensure consistency in the exercise of the competencies pertaining to the regulator with exclusive competence on the basis of the energy scheme that article 149.1.25.<sup>a</sup> of the Spanish Constitution attributes to Central Government, defining for such purposes a procedure which, in any event, guarantees the independence of the regulatory authority in approving legislative circulars, while foreseeing a prior reconciliation arrangement in order to attempt to deliver a mutually agreed solution in the event of discrepancy. In this way, the rule envisages that prior to the start of processing of the National Commission on Markets and Competition's legislative circulars, the Government, through an order of the Ministry of Ecological Transition, may establish the energy policy guidelines to be taken into account in the circular that is approved by the National Commission on Markets and the Competition. In such cases, and prior to the approval of the legislative circular, the Ministry of Ecological Transition may issue a report on the consistency of the proposal with such guidelines. In the event of discrepancies between the parties, a Cooperation Committee will be formed in order to seek an understanding between the both parties.

If there are no discrepancies or if there are, an understanding has been reached between the parties, the legislative circulars approved by the National Commission on Markets and the Competition will state that they are adopted «in accordance with the energy policy guidelines of the Ministry of Ecological Transition ». Otherwise, they will indicate that they are adopted «having heard the Ministry of Ecological Transition ».

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

Second, with respect to the remuneration of gas and electricity transport and distribution activities and of liquefied natural gas plants (except for underground natural gas storage facilities), the rule specifies that the National Commission on Markets and Competition will approve the methodology, the remuneration parameters, the asset regulatory base and the annual remuneration of the activity. In any event, the financial remuneration rate may not exceed the threshold established by Law for the regulatory period. For electricity and natural gas network access tolls, it is established that apart from the toll methodology, the regulatory authority will approve their structure and specific values, with the Ministry of Ecological Transition and Demographic Challenge being tasked with approving the structure of the charges, methodology and values.

Third, in relation to the terms of access and connection to the electricity and natural gas transport and distribution network, the National Commission on Markets and the Competition will be tasked with approving the methodology and conditions of access and connection that will comprise the economic criteria, and with assessing capacity, reasons for rejection, content of the requests, permits and contracts and the obligations of publicity and transparency regarding relevant access and connection information.

Fourth, the National Commission on Markets and Competition will be tasked with regulating the rules on the functioning of organised markets in terms of their regulated component in those aspects approval of which pertains to the national regulatory authority, in accordance with European Community law. In preparing the legislative circulars relating to the remuneration of regulated activities, network access tolls and access and connection terms and conditions and the rules on the functioning of organised markets, the National Commission on Markets and the Competition should take into account the energy policy guidelines that have been defined by the Ministry of Ecological Transition.

Fifth, the new regulation provides that the remuneration of the electricity system operator and gas system technical manager will be that established by the National Commission on Markets and the Competition, it clarifies the control function with respect to the transport network investment plans and re-defines the distribution of competencies under the disciplinary and inspection regime, in line with the function changes brought in.

Finally, it establishes a transitional regime for all the changes that are brought in, in order to ensure an orderly transfer of functions and that the legal certainty of the sector players is not affected.

On February 20<sup>th</sup> 2019, the National Markets and Competition Commission published the timetable for policy circulars that may affect the aspects of energy policy with a planned 2019 process.

The National Markets and Competition Commission approved in 2019 the following Circulars related to the gas sector:

- Circular 2/2019, of November 12<sup>th</sup>, laying down the natural gas balance standards.
- Circular 8/2019, of December 12<sup>th</sup>, establishing the methodology and conditions of access and allocation in the natural gas system.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

- Circular 9/2019, of December 12<sup>th</sup>, which determines the methodology of remuneration of regulated activities of transport and gas regasification

The Circular establishing the methodology for the calculation of transport tolls, local networks and natural gas regasification -CIR/DE/003/19) and the Circular establishing the methodology for determining the remuneration of natural gas distribution -CIR/DE/003/19- is currently in process, being foreseeable its approval during 2020.

Furthermore, the Technical Manager of the System, Enagás, S.A., is responsible for the appropriate functioning and coordination of the gas system. Law 12/2007 of July 2<sup>nd</sup> limits the shareholding in Enagás, S.A. to a maximum of 5% of its share capital, voting rights to 3% in general, and to 1% participants in gas activities, and in any event, the sum of the interest of the shareholders undertaking activities in the gas sector cannot exceed 40%.

In general, the Spanish gas sector has the following main characteristics:

- It is an industry in which regulated and unregulated activities coexist. The regulated activities consist of transport, regasification, storage and distribution of natural gas. The non-regulated activities comprise production, supply and retailing of natural gas.
- The natural gas sector is entirely dependent on foreign supplies of natural gas, which represent almost 99.9% of the natural gas supply in Spain.
- Under EU legislation (Directives 2003/55/CE of June 26<sup>th</sup>, and 2009/73/UE of July 13<sup>th</sup>), the supply of natural gas in Spain is totally de-regulated, and all Spanish consumers can freely choose their natural gas provider as of January 1<sup>st</sup> 2003. The deregulation procedure for the industry has been reinforced substantially by the disappearance as of July 1<sup>st</sup> 2008 of the bundled tariff of distribution companies and the subsequent right of consumers to participate in the deregulated market (although as indicated further below a tariff of last resort has been maintained for consumers of lower consumption).

#### Regulation of natural gas activities in Spain

The natural gas activities are divided into: regulated activities: transport, storage, regasification and natural gas distribution; and non-regulated activities: production, supply and commercialization of natural gas.

#### **2.1 Regulated activities**

Regulated activities are characterized by:

- *Need for prior government authorization:* The undertaking of regulated activities requires prior regulated administrative authorization. In order to obtain this authorization, the applicant must demonstrate its legal, technical and economic capacity to exercise this activity. This authorization creates a legal monopoly for the regulated activity in a predetermined territory.



## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

- *Remuneration established by legislation:* The general directives that set the remuneration for these activities are governed by Law 18/2014 of October 15<sup>th</sup> and Royal Decree 949/2001 of August 3<sup>rd</sup> while the specific remuneration to be received is updated annually by ministerial order.

Thus, the remuneration framework incentivises the further development of the network infrastructure while allowing companies to recover investments made in the network and the operating costs incurred in undertaking regulated activities.

The regulatory framework for the natural gas industry in Spain has a procedure for settlement compensation amongst companies in the sector for net billing of gas acquisition and other costs, so that each company receives the appropriate remuneration for their regulated activities.

- *Subjection to specific obligations:* The carrying out of regulated activities is subject to specific obligations to ensure the development of competition in retailing. The two main obligations in this sense consist of permitting access by third parties to the transport and distribution pipelines (including regasification and storage) and the obligation to keep the regulated and non-regulated activities separate.

Circular 8/2019 of December 12<sup>th</sup>, the National Markets and Competition Commission, which establishes the methodology and conditions of access and capacity allocation in the natural gas system, regulates access by third parties to the network, which is managed by a single telematic platform, as well as the rights and obligations of each person involved in the system, develops the procurement of capacity services individually or aggregated and homogenizes the procedures of procurement at all facilities in the system and establishes, by default, the allocation of capacity through market mechanisms, modifying the procurement regime capacity established previously in the Royal Decree 948/2015, of October 30<sup>th</sup>, as well as in the regime established in 2001 by Royal Decree 949/2001, of August 3<sup>rd</sup>. The owners of the transport and distribution pipelines have the right to receive tolls and levies in consideration for this access, which are updated annually under ministerial order.

The legislation establishes the duty of functional separation, which means not only accounting separation, in order to avoid cross-subsidization and increase the transparency of the calculation of rates, tolls and levies, and legal separation, through separate companies, but also the requirement of independent operation of the regulated subsidiary company with regard to the other companies in the group.

#### 2.1.1 Transport

The transport activity includes regasification, storage and transport of gas through the high pressure gas pipeline network:

- *Regasification:* Natural gas is imported to Spain through a pipeline network (in gas form) and by gas tankers (in liquid form, hereinafter, liquefied natural gas). The regasification is the activity that involves the conversion of liquefied natural gas, stored in cryogenic tanks generally at regasification plants, into a gaseous state, which is then pumped into the national gas pipeline network.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

- *Transport:* once the natural gas is imported or produced and, if necessary, regasified, it is injected in gas form into the high pressure gas pipeline transport network. The transport network crosses most regions in Spain and transports the natural gas to the major consumers, such as electricity plants and industrial customers and local distributors.

The transport network is owned primarily by Enagás, S.A., although other companies own a small proportion of it.

- *Storage:* facilities consist mainly of underground tanks, which are necessary to ensure a constant supply of natural gas that is not affected by seasonal changes and other demand peaks. These facilities also serve to fulfil the obligation established by Royal Decree 1766/2007 of December 28<sup>th</sup> to maintain minimum security reserves. Current legislation also allows for unregulated underground storage facilities with third-party access, negotiated and previously authorised by the Spanish Government, although no such facilities currently exist.

The Royal Decree-Law 13/2014, of October 3<sup>rd</sup>, introduced a number of urgent measures in relation to the gas sector and ownership of nuclear plants.

This Royal Decree-Law formally accepted the relinquishment of the Castor natural gas storage plant and the termination of the concession to operate the plant held by Escal UGS, S.L. Additionally, the ongoing administration and maintenance of the facility was assigned to Enagás, S.A., with the related costs remunerated by the gas system. Finally, the amount of Euros 1,351 million was paid to Escal UGS, S.L., based on the net value of the investment in the facility. This sum was paid by Enagás, S.A. in exchange for a claim against the gas system whereby the amount is to be recovered over the following 30 years.

In accordance with the Judgement of the Constitution Court of 21 December 2017, that declares articles 4 to 6 and article 2.2, additional provision one and transitional provision one of that Royal Decree Law, null and void, Ministerial Order TEC/1367/2018, of 20 December, does not include these collection rights of Enagás for 2019.

During the calendar year 2019, the liquidations of regulated activities in relation to Castor underground storage were reviewed ex officio, where the Company has received an amount of Euros 14,551 thousand for this concept.

The Ministry Order ETU/1283/2017, of December 22<sup>nd</sup>, has established the remuneration for the companies owning transport assets for the year 2018.

The Ministry Order TEC/1367/2018, of December 20<sup>th</sup> has established the remuneration for the companies owning transport assets for the year 2019.

Resolution of December 18<sup>th</sup> 2019 of the National Markets and Competition Commission has established the remuneration of companies engaged in the regulated activities of liquefied natural gas, transport and distribution plants for the calendar year 2020.



## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

#### *2.1.2 Distribution*

Natural gas is transported from the high pressure transport pipeline network to the final consumer through the medium and lower pressure transport pipeline network owned by distribution companies.

According to Royal Decree-Law 5/2005, of March 11<sup>th</sup>, distribution businesses operate under a system of administrative authorisations that provides a distributor the right to exclusive operation within a given distribution zone. Additionally, Law 12/2007, of July 2<sup>nd</sup>, gives the distributor within a given zone the preference to obtain authorisations for adjoining zones.

Until July 1<sup>st</sup>, 2008, distributors also had the obligation to act as supplier of any consumer that accepted the regulated tariff. From July 1<sup>st</sup>, 2008 onwards, the distributor's activity is restricted to the expansion and management of distribution networks, with separate supply companies being responsible for the supply of gas to the end consumer, as discussed in section 2.2.2.

Royal Decree-Law 13/2012, of March 30<sup>th</sup>, transposes into Spanish law EU directives concerning common rules for internal gas and electricity markets, and electronic communications, as well as introducing measures to correct the deviations resulting from the imbalance between revenues and costs of the electricity and gas sector. In relation to the gas sector, measures introduced to correct the imbalance include the suspension of administrative authorisation of pipelines, except for those that are subject to international commitments, suspension of authorization of new regasification plants, as well as delays to remuneration of underground storage facilities.

Royal Decree-Law 8/2014, of July 4<sup>th</sup>, which was later transcribed into Law 18/2014, of October 17<sup>th</sup>, introduced measures for growth, competitiveness and efficiency. The key aspects of this Law as applied to the natural gas sector are described below:

- The principle of the gas system's economic and financial sustainability is established, whereby any regulation relating to the sector that entails an increase in costs for the gas system or a reduction in revenue must also bring an equivalent reduction in other cost items or an equivalent increase in revenue to ensure a balance in the system.
- The principle of economic and financial sustainability means that the revenue generated from the use of the facilities must meet all system costs. Gas system revenue will be employed solely to remunerate the regulated activities performed to supply gas.
- Annual deficits between system costs and revenue may not exceed 10% of revenue payable for the period, or the cumulative outstanding deficit within the system may not exceed 15%. If this sum is exceeded, tolls will be automatically revised to cover the portion that exceeds said limit. The portion of the deficit which, without exceeding the limits, is not offset by the rise in tolls and charges, will be financed by the parties to the settlement system, in proportion to the remuneration applicable to them. Each party will be entitled to recover its deficit contributions over the following five years including interest costs calculated using prevalent market rates.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

- The remuneration methodologies for the natural gas sector will take into consideration the costs incurred by an efficient, well-managed company to perform the activity under the principle of realization whereby the activity must be performed at the lowest possible cost to the system.
- Regulatory periods spanning six years have been established for the remuneration of regulated activities, allowing for possible adjustments every three years to the system's remuneration parameters (including unit reference values for customers and sales, operating and maintenance costs, etc.) in the event of significant changes to revenue and costs of the system. The first regulatory period will end on December 31<sup>st</sup> 2020.
- The remuneration system for transmission, regasification and storage facilities is based on homogenous principles including the use of the net asset value of an operator as the basis for calculating investment remuneration, inclusion of variable remuneration based on gas transported, re-gasified or stored by asset type and elimination of all automatic review procedures for values and parameters based on price indices.
- With respect to new secondary transmission facilities, remuneration is included in the remuneration methodology for distribution facilities, linking remuneration to customers' growth and to new demand generated.
- With regard to distribution facilities, remuneration is calculated for each distribution company and all its facilities based on the number of customers connected and the volume of gas supplied. However, automatic reviews are eliminated based on the Consumer Price Index and Industrial Price Index, and the parametric remuneration formula is established to distinguish remuneration categories between supplies at pressures equal to or below 4 bars, between consumers with an annual consumption of less than 50 MWh and consumers with a higher consumption, so as to guarantee the adequacy of system revenue at all consumption levels, taking into account the toll revenues in each case. The remuneration established in the Order IET/2446/2013, of December 27<sup>th</sup> is maintained, for the period from January 1<sup>st</sup> of 2014 to when the Royal Decree-Law 8/2014 came into force.
- In order to incentivise network expansion to non-gasified zones and bring remuneration into line with actual costs incurred by companies, different unit values are used depending on whether or not customers and consumption are in recently-gasified municipalities.
- With respect to the gas system's accumulated deficit as on December 31<sup>st</sup> 2014, which is supported by the subjects of the liquidation system, has been recognised, in the final liquidation applicable to the year 2014. This deficit will be financed by facility owners over a 15-year period; annual payments will be included as a system cost including interest costs calculated using prevalent market rates. On December 1<sup>st</sup>, 2017, the Company subscribed a loan agreement with a banking entity for the nominal amount pending collection (Note 10).

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

- A new system cost is introduced corresponding to the remuneration of natural gas assigned to the tariff marked under the Algeria contract, supplied through the Maghreb pipeline, as a result of the Award issued by the Paris International Court of Arbitration on August 9<sup>th</sup> 2010. The amount to be collected is up to Euros 164 million, and will be paid from the year 2015 during five years, including interest costs calculated using prevalent market rates.

Order ETU/1283/2017, of December 22<sup>nd</sup>, established the remuneration for the regulated activities of the gas sector for 2018. Specifically, the initial remuneration recognised by Madrileña Red de Gas for the year 2018 was an amount to 142,817 thousand euros for the period between January 1<sup>st</sup> and December 31<sup>st</sup> of 2018. The Order included an adjustment of the remuneration for 2016 and 2017 for an amount of Euros 2,432 thousand of higher income without assuming a significant impact on the income statement.

Order TEC/1367/2018 of December 20<sup>th</sup> has established the remuneration for the regulated activities of the gas sector for 2019. Specifically the initial remuneration recognized by Madrileña Red de Gas for the year 2019 is 142,299 thousand euros for the period between January 1<sup>st</sup> and December 31<sup>st</sup> of 2019. The order includes an adjustment of the remuneration for 2017 and 2018 for an amount of Euros 1,700 thousand of higher income without assuming a significant impact on the income statement

Resolution of December 18<sup>th</sup> 2019 of the National Markets and Competition Commission has established the remuneration of companies engaged in the regulated activities of liquefied natural gas, transport and distribution plants for the calendar year 2020. In particular, the provisional remuneration granted for Madrileña Red de Gas S.A.U. for the year 2020 amounts to Euros 147,093 thousand.

Order TEC/1259/2019 of December 20<sup>th</sup>, includes an adjustment of the remuneration for 2018 for an amount of Euros 6,637 thousand of higher income.

During the year ended on June 30<sup>th</sup> 2017, the Company received the final liquidation of the regulated activities of the gas sector corresponding to the years 2014 and 2015, and its impact on the income statement was immaterial. The gas sector deficit of 2014, which includes the accumulated deficit in previous years, was Euros 1,025 million (of which Euros 47.4 million correspond to Madrileña Red de Gas, S.A.U.), which would be recoverable by the facility owners over a period of 15 years, from November 25<sup>th</sup> 2016 until November 24<sup>th</sup> 2031, including interest costs calculated using prevalent market rates. For the interest rate, in order ETU/1977/2016 a provisional interest rate of 1.104% was proposed by the CNMC and this interest has been defined like definitive in the order TEC/1367/2018. On December 1<sup>st</sup> 2017, the Company agreed the assignment of the account receivable derived from the gas deficit for the year 2014.

In 2015, the deficit was Euros 27 million (of which Euros 1.3 million corresponds to Madrileña Red de Gas, S.A.U.), which will be recoverable by facility owners over a period of five years (from November 25<sup>th</sup> 2016 until November 25<sup>th</sup> 2021), including interest costs, which were yet to be established. However, in order ETU/1977/2016, the CNMC proposed a provisional interest rate of 0.836%, this interest has been defined like definitive in the order TEC/1367/2018, that considers the new collection right holders as parties to the clearing system due to the rights assigned.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

During year 2017, the Company has received the final settlement of the regulated activities of the gas sector for 2016 without significant impacts on the profit and loss account. For 2016, the deficit figure has been closed at Euros 90.01 million (of which Euros 4.6 million corresponds to Madrileña Red de Gas, SAU), which will be recoverable by the regulated subjects in five annuities at an interest rate in conditions equivalent to the market that is also not fixed yet, however, Order ETU/1283/2017 has proposed a provisional interest rate with the value of 0.503% as proposed by the CNMC, which has been defined as definitive interest rate of 0.716% by the Order TEC/1367/2018. On October 10th 2018, the Company has agreed to securitize the account receivable derived from the gas deficit for the years 2015 and 2016 (Note 9).

During the year ended on December 31<sup>th</sup> 2018, the company has received the final settlement of the regulated activities of the gas sector for 2017 without significant impacts on the profit and loss account. For 2017 the deficit figure has been closed at Euros 24.8 million euros (of which Euros 1.2 million corresponds to Madrileña Red de Gas SAU) which will be recoverable by the regulated subjects in five annuities at an interest rate in conditions equivalent to the market that is also not fixed yet, however Order TEC/1367/2018 has established a definitive interest rate with the value of 0.923%.

During the year ended December 31<sup>st</sup> 2019 the Company received the liquidation of the activities regulated by the gas sector for the calendar year 2018 without significant impacts on the profit and loss account. For the calendar year 2018, the surplus was closed at Euros 30.8 million (of which Euros 1.6 million corresponds to Madrileña Red de Gas S.A.U). Article 61.3 of Law 18/2014 of October 15<sup>th</sup> found that, if the annual gap in recognized income and remuneration resulted in a positive amount, it shall be allocated to settle the outstanding annuities of previous years, applying first to the temporary mismatch between revenue and costs and then to the cumulative deficit of the gas system as of 2014 December 31<sup>st</sup>. Subsequently, Order TEC/1367/2018 of December 20<sup>th</sup> determined that, in the event of several mismatches with outstanding balances, those with a higher interest rate will be repaid first. The final interest rates applicable to the various collection fees of the gas sector were established in that Order. On 2019 November 28<sup>th</sup>, the Regulatory Oversight Chamber of the National Markets and Competition Commission approved the final liquidation of the calendar year 2018, determining the existence of a surplus of 30,879 thousands euros, which, according to the above, will be used for the early and complete amortization of the temporary mismatches between income and costs for the years 2017 and 2015, as they bear higher interest rates, namely 0.923% and 0.836% respectively. The remaining amount is intended to partially amortize the 2016 mismatch, which bears an interest rate of 0.716%. For the calculation of the amounts to be depreciated corresponding to each collection right, the updated outstanding amounts obtained in that final settlement for the calendar year 2018 have been taken into account, as a result of the decisions of the National Markets and Competition Commission of 2019 July 5<sup>th</sup> on ex officio review procedures for final settlements of regulated natural gas activities relating to underground storage 'Castor'.

Other Ministerial Orders of interest are:

On April 9<sup>th</sup> 2019, Order TEC/406/2019 of April 5<sup>th</sup> establishing energy policy guidelines was issued to the CNMC, which sets out the recommendations of the Ministry for Energy Transition in relation to the Circulars planned for 2019.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

In addition, Order TEC/1259/2019, of December 20<sup>th</sup>, establishing the remuneration of basic underground storage activity and the tolls and royalties associated with third-party access to gas facilities by 2020.

#### **2.2 Unregulated activities**

##### *2.2.1. Supplies*

Taking into account the small volume of natural gas production in Spain, this section focuses on the international supply of natural gas.

The supply of natural gas in Spain is carried out mostly by gas operators through long-term contracts with gas producers. This supply, although being an unregulated activity, is subject to two types of limitations, the purpose of which is to ensure diversification of supply and the introduction of competition into the market: 1) no country can supply more than 60% of gas imported into Spain; and 2) since January 1<sup>st</sup> 2003 no business person or group can contribute, as a whole, natural gas for consumption in Spain that is greater than 70% of total national consumption, excluding self-consumption.

##### *2.2.2. Commercialization*

As of July 1<sup>st</sup> 2008, under Law 12/2007, of July 2<sup>nd</sup>, and its enabling regulations, most importantly Royal Decree 1068/2007, of July 27, and Order 2309/2007, of July 30<sup>th</sup>, natural gas is supplied exclusively by gas supply companies, with supply under regulated tariffs (previously performed by distribution companies) been eliminated. Additionally, consumers connected at a pressure of less than 4 bar that did not exceed a certain consumption threshold (3 GWh, although this has been progressively reduced to the current 50 MWh/year) were entitled to be supplied at a maximum price called the last resort tariff (TUR). The calculation of the TUR is performed pursuant to legislation, and includes the cost of raw materials, access tolls, retailing costs and supply security costs.

In order to ensure that consumers do not have practical problems in changing their supply company, Law 12/2007, of July 2<sup>nd</sup>, ordered the creation of the Supplier Change Bureau, «Oficina de Cambios de Suministrador, S.A. (OCSUM)», which is owned by the major gas and electricity operators. As of July 2014, these functions were taken over by the CNMC.

Ministry of Industry, Energy and Tourism (MINETUR) issued Order ITC/1506/2010, of June 8<sup>th</sup>, establishing that a review of the TUR for natural gas be carried out under the ruling of the General Directorate of Energy Policy and Mines (DGPEM). The fixed and variable terms of the tariffs will be reviewed when there is a modification on the fixed and variables terms of the tolls and levies for access to the system or in the waste coefficients in force. The variable term will be reviewed quarterly, from the 1<sup>st</sup> day of the months of January, April, July and October of each year, provided that the cost of raw materials varies upward or downward by more than 2%.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

Law 15/2012, of December 27<sup>th</sup>, on fiscal measures for energy sustainability included a number of changes affecting the natural gas sector including modifications to the tax on hydrocarbons, establishing a positive rate for natural gas employed as fuel in stationary motors, as well as for natural gas used for purposes other than as fuel (consumption). However, a reduced rate was established for natural gas employed for professional purposes once this was not used in generation or cogeneration of electricity.

With regards to energy efficiency, Royal Decree-Law 8/2014, of July 4<sup>th</sup>, subsequently approved as Law 18/2014, of October 15<sup>th</sup>, stipulates the following:

- The national energy efficiency obligations system is created, whereby gas and electricity supply companies, oil product wholesalers and liquefied petroleum gas (LPG) wholesalers will be allocated an annual energy-saving quota (saving obligations). Aggregate saving obligations will be equal to the target allocated to Spain in EU Directive 2012/27/EU.
- The National Energy Efficiency Fund (FNEE) is created, to allow the implementation of economic and financial support mechanisms, technical assistance, training and information, or other measures to enhance energy efficiency in different sectors, which are necessary to achieve the Energy Efficiency Directive's objectives.
- The financial equivalence of the saving obligations will be determined based on the average cost of the support mechanisms, incentives and measures required to mobilize the investments necessary to fulfil the annual savings target, through actions by the FNEE, based on the findings of the technical analysis by the Institute for Energy Diversification and Saving.
- The Government is also authorized to establish and develop a final energy saving accreditation system, by issuing Energy Saving Certificates (ESC). Once launched, this will allow companies to progressively fulfil their saving obligations by directly promoting energy efficiency enhancement actions that fulfil the necessary guarantees.

Annually by Ministerial Order it established the obligations of contribution to the FNEE for each of the obligors.

Law 8/2015, of May 21<sup>st</sup> modifies Law 34/1998, of October 7<sup>th</sup>, of the Hydrocarbons Sector, introducing certain tax and non-tax measures in relation to the exploration, research and exploitation of hydrocarbons. This reform for sees the creation of an organised natural gas market organising activity across the Iberian Peninsula, facilitating the entry of new marketers and increasing competition, as well as establishing a new single operator of this market, responsible for managing the gas hub.

Royal Decree 984/2015, of October 30<sup>th</sup>, regulates the organised gas market and third-party access to natural gas system installations, while Resolution of December 4<sup>th</sup> 2015, issued by the Secretary of State for Energy (SEE), approved the market rules, membership contract and the resolutions of the organised gas market. The organised gas market, managed by MIBGAS, began operations in December 2015.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

The SEE Resolution of June 6<sup>th</sup> 2016 approved various provisions concerning the organised gas market, including the number of market makers, the acquisition of cushion gas for Yela and the acquisition of heel gas and base gas.

The SEE Resolution of August 2<sup>nd</sup> 2016 approved the rules for the management of guarantees in the gas system. This Resolution lays down a standardised model for the provision of guarantees and determines the amount and duration of guarantees for mismatches in the virtual handover point and of guarantees required for contracting capacity, defines the valid instruments for concluding guarantees and, finally, establishes the protocol for communication with the Guarantee Manager and the action protocol in the event of non-compliance.

In addition, the SEE Resolution of August 2<sup>nd</sup> 2016 approved the framework contract for access to the facilities of the Spanish gas system. The purpose of the framework contract is for users (supply companies or direct customers in the market) to contract services for accessing the gas system facilities, excluding the contracting of handover point access services, to or from a gas pipeline connection with Europe.

#### Regulation of Liquefied Petroleum Gas (LPG)

The supply of piped LPG is regulated by Law 34/1998, of October 7<sup>th</sup>, of the Hydrocarbons sector.

The (MINETAD) (currently called Ministry of the Ecological Transition and Demographic Challenge) establishes the selling rates for piped LPG for end consumers and the assignment prices of LPG at which it is purchased by piped LPG distributors, including specific rates and the methodology for automatically calculating and updating them. These selling rates are the maximum rate chargeable and apply to consumers in the whole of Spain, without prejudice to their specialties.

### **3. Basis for presentation**

The most significant accounting policies and measurement criteria applied in the preparation of the Company's financial statements are described below. Such accounting policies have been applied consistently for all the periods presented, unless otherwise stated.

#### **3.1.1 Transition to International Financial Reporting Standards adopted by the European Union (IFRS-EU)**

The accompanying financial statements are prepared in accordance with the International Financial Reporting Standards (IFRS) and the International Financial Reporting Interpretation Committee (IFRIC) adopted by the European Union (all together, IFRS-EU), in line with the European Parliament Regulation and Council Regulation 1606/2002 and subsequent amendments, being these the first consolidated financial statement prepared under IFRS-EU.

**MADRILEÑA RED DE GAS, S.A.U.**

**NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED  
ON DECEMBER 31<sup>st</sup> 2019  
(Expressed in thousand of euros)**

The following financial statements have been prepared on a voluntary basis to show the equity and profit/loss from the operations according to IFRS-EU, with the objective of comparing with other entities of the sector and to show the Company's financial magnitudes in accordance to an accounting framework that is globally recognized. The date of transition to IFRS-EU was set as July 1<sup>st</sup> 2015.

For statutory purposes, and in order to comply with the legal obligations of corporate information, the Company has presented separately its annual accounts corresponding to the year ended on December 31<sup>st</sup> 2019 in accordance with the current mercantile legislation stated in the Code of Commerce reformed in accordance with Law 16/2007, of July 4<sup>th</sup> on reforming and adapting Spanish corporate accounting legislation for its international harmonization based on European legislation; RD 1514/2007, of November 20<sup>th</sup> (modified by RD 1159/2010, of September 17<sup>th</sup>), by which the General Chart of Accounts is approved; and RD 602/2016, of December 2<sup>nd</sup>.

The General Chart of Accounts (PGC) differs in certain aspects from IFRS-EU. At the time of preparation of these financial statements, the Management has adjusted certain accounting and valuation principles applied to the annual accounts prepared under PGC in order to obtain the conversion into IFRS-EU.

The reconciliation of the conversion effect from General Chart of Accounts to IFRS-EU in the Company's equity and profit/loss for the year is shown in the Note 4.

These financial statements have been prepared under the historical cost convention.

The preparation of financial statements under IFRS-EU requires the Company to use certain estimates and judgements in relation to the future that are continuously assessed and are based on historical experience and other factors, including expectations of future events deemed reasonable under the circumstances. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are outlined in Note 6.



## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### 3.1.2 New IFRS-EU standards, amendments and IFRIC interpretations issued

##### *Mandatory standards, amendments and interpretations for all years beginning on or after 1 January 2019*

In 2019, the following standards and amendments were adopted for the first time:

Effective since:	New requirements or modifications
1 January 2019	<p>New standards and interpretations</p> <ul style="list-style-type: none"><li>• IFRS 16 Leases</li><li>• IFRIC 23 Uncertainties over Income Tax Treatments</li></ul> <p>Amendments</p> <ul style="list-style-type: none"><li>• Non-current Investments in Associates and Joint Ventures (amendments to IAS 28)</li><li>• Prepayment Features with Negative Compensation (amendments to IFRS 9)</li><li>• Amendment, curtailment or settlement of defined benefit plans (amendment to IAS 19)</li><li>• Annual Improvements to IFRS Standards, cycle 2015-2017 - various standards.</li></ul>

Below is a description of the different standards and interpretations issued:

#### **IFRS 16 Leases**

IFRS 16 "Leases" supersedes IAS 17, IFRIC 4, SIC-15 and SIC-27, and establishes the principles for accounting for leases under a single balance sheet model for all leases. IFRS 16 is effective for periods beginning on or after 1 January 2019 and has not been early adopted.

IFRS 16 requires lessees to recognise the underlying asset as a right-of-use asset against a lease liability in the balance sheet at the present value of the lease payments payable over the lease term. This asset is depreciated over the lease term and a finance cost is recognised for discounting the lease liability. Lessor accounting under this standard remains largely unchanged and the distinction between operating and finance leases is retained, to the extent to which the risks and rewards incidental to ownership are substantially transferred. In application of this standard, the Company has made the following estimates:

The standard has been applied to leases in which the underlying asset is higher than USD 5,000 (approximately Euros 4,500) and its estimated life exceeds twelve months.

On the date of first-time application, 1 January 2019, it was not re-assessed whether a contract is, or contains, a lease, and the standard has been applied to contracts which were previously identified as such.

The modified retrospective approach has been applied, whereby comparative figures for the prior year have not been restated, and the initial value of the asset is therefore the same as the lease liability at 1 January 2019 for all lease contracts.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

When measuring lease liabilities for leases that were classified as operating lease, the Company discounted lease payments using its incremental borrowing rate at 1 January 2019. The weighted-average rate is 3%.

The impact of the first-time application of IFRS-UE 16 at 1 January 2019 has been an increase in non-current assets of Euros 1,122 thousand corresponding to right-of-use assets under lease (see note 7), and an increase in non-current and current liabilities of Euros 742 thousand and Euros 380 thousand, respectively.

	01/01/2019
Operating lease commitments at 31 December 2018 as disclosed in the financial statements	219
Correction of errors	1,003
Discounted using the incremental borrowing rate at 1 January 2019	(62)
Finance lease liabilities recognised as at 31 December 2018	-
- Recognition exemption for leases of low- value assets	-
- Recognition exemption for leases with less than 12 months of lease term at transition	(38)
- Extension options reasonably certain to be exercised	-
Lease liabilities at 1 January 2019	1,122

The changes in Group accounting policies derived from the application of this standard are detailed in note 4.

#### IFRIC 23 Uncertainties over Income Tax Treatments

The interpretation introduces additional requisites to those of IAS 12 "Income Taxes", and specifies how to reflect the effects of uncertainty over income tax treatments. This interpretation clarifies how to apply the recognition and measurement requisites of IAS 12 when there is uncertainty over their accounting treatment. This interpretation became effective for annual accounting periods beginning on or after 1 January 2019 and has had no significant effects on the Financial Statements (see note 15).

The entry into force of the remaining standards has not had a significant impact on the Financial Statements.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### New requirements or amendments effective as of 1 January 2020.

The new standards approved whose application is not mandatory in 2019 and which become effective for annual accounting periods beginning on or after 1 January 2020 are as follows:

Effective since:	New requirements or modifications
1 January 2020	<ul style="list-style-type: none"><li>Amendments to References to the Conceptual Framework in IFRS Standards</li></ul>
1 January 2020	<ul style="list-style-type: none"><li>Definition of Materiality</li></ul>
Pending adoption by the EU	<ul style="list-style-type: none"><li>IFRS 17 Insurance Contracts</li></ul>
	<ul style="list-style-type: none"><li>Reform of the definition of materiality</li></ul>
	<ul style="list-style-type: none"><li>IBOR reform</li></ul>

The Company do not expect that the new standards have a significant effect.

#### 3.1.3 Comparison of information

The balance sheet, income statement, statement of changes in equity, statement of cash flows and the notes thereto for 2019 include comparative figures for 2018.

The figures for the year 2018 have been restated to register as property, plant and equipment and liabilities-deferred income, transfers of assets from customers that were not accounted for.

	Thousand euros		
	31/12/2017	Adjustments	01/01/2018 Restated figures
Property, plant and equipment	373,091	9,924	383,015
<b>TOTAL ASSETS</b>	<b>1,888,370</b>	<b>9,924</b>	<b>1,898,294</b>
Liabilities - Deferred income	18,092	9,924	28,016
<b>TOTAL NET EQUITY AND LIABILITIES</b>	<b>1,888,370</b>	<b>9,924</b>	<b>1,898,294</b>

	Thousand euros		
	31/12/2018	Adjustments	31/12/2018 Restated figures
Property, plant and equipment	358,522	10,945	369,467
<b>TOTAL ASSETS</b>	<b>1,309,938</b>	<b>10,945</b>	<b>1,320,883</b>
Liabilities - Deferred income	17,775	10,945	28,720
<b>TOTAL NET EQUITY AND LIABILITIES</b>	<b>1,309,938</b>	<b>10,945</b>	<b>1,320,883</b>
<b>INCOME STATEMENTS</b>			
Other income	1,641	435	2,076
Amortisation and depreciation	(27,787)	(435)	(28,222)

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

	Thousand euros		
	31/12/2018	Adjustments	31/12/2018 Restated figures
Amortisation and depreciation	27,787	435	28,222
Release of grants	(1,641)	(435)	(2,076)
<b>Cash flow from operating activities</b>	<b>84,390</b>	<b>-</b>	<b>84,390</b>

Certain amounts for 2018 have been reclassified in these financial statements to make them comparable with those for the current year and facilitate comparison. The reclassification has been as follows:

	Thousand euros	
	Dr	Cr
Property, plant and equipment		(846)
Intangible assets - Commercial acquisition costs	846	
Self-constructed assets		(904)
Consumption of goods	904	

The Financial Statements of 2019 are not comparable with those of the 2018 period as a result of the application of IFRS 16 as of January 1, 2019 (see note 3.1.2).

### 3.2 Intangible assets

#### a) Goodwill

Goodwill represents the difference, at the acquisition date, between the cost of the business combination and the fair value of the net identifiable assets acquired in the transaction. Therefore, goodwill is only recognized when it has been acquired for the consideration and related to future financial benefits from assets which cannot be identified individually and recognized separately.

Goodwill is not amortized but it is tested for impairment annually, or more frequently if events or changes in circumstances indicate that it might be impaired, and is carried at cost less accumulated impairment losses.

Goodwill is allocated to CGU for the purpose of impairment testing. The allocation is made to those CGUs or Groups of CGUs that are expected to benefit from the business combination in which the goodwill arose.

Value adjustments for impairment recognized in goodwill are not reversed in subsequent years.

#### b) Administrative authorisations

For the installation and commissioning of the distribution network in a specific distribution area, an administrative authorisation must be obtained.



## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

In order to obtain the authorization, the relevant distribution company must prove its legal, technical and economic capacity.

- a) Legal capacity: pursuant to Royal Decree 197/2010 of February 26<sup>th</sup>, it is necessary to be a limited liability company with Spanish nationality ("sociedad anónima") or from another EU member state.
- b) Technical capacity: as set out in the RD 1434/2002 distribution companies are deemed to meet the required technical capacity levels.
- c) Economic and financial capacity: as set out in the RD 1434/2002 distribution companies are deemed to have enough economic and financial capacity.

Most of the Company's administrative authorizations were acquired from Gas Natural Fenosa Group (currently called Naturgy).

The expenses incurred to obtain them have been recognised under the heading "Administrative Authorisations" as a part of the intangible assets. The administrative authorisations have an indefinite useful life (due to the fact that they allow the distribution network to be operated indefinitely) and therefore are not amortized, although any possible impairment is reviewed annually, valued at acquisition cost less accumulated impairment losses.

#### c) Computer applications

Acquired computer software licences are capitalised on the basis of the costs incurred to acquire and bring to use the specific software. These costs are amortised over the assets' estimated useful life (4 years).

Costs associated with maintaining software programmes are recognised as an expense as incurred. Development costs that are directly attributable to the design and testing of identifiable and unique software products controlled by the Company are recognised as intangible assets when the following criteria are met:

- It is technically feasible to complete the software so that it will be available for use
- Management intends to complete the software and use or sell it
- There is an ability to use or sell the software
- It can be demonstrated how the software will generate probable future economic benefits
- Adequate technical, financial and other resources to complete the development and to use or sell the software are available, and
- The expenditure attributable to the software during its development can be reliably measured.

Expenses associated with software maintenance are recognised when incurred. Costs directly related to the production of identifiable and unique computer programs controlled by the Company and that will probably generate economic benefits exceeding costs beyond one year are recognised as intangible assets. Direct costs include the software development employee costs and an appropriate portion of relevant overheads.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### d) Commercial acquisition costs

The incremental costs incurred directly to obtain contracts with clients, which reflect the commissions paid to obtain energy supply contracts with said clients and which are expected to be recovered in the expected duration of the contract, are recorded as intangible assets. The commercial acquisition costs recognized as assets are systematically amortized in the consolidated Profit and Loss Account throughout the expected average life of the contracts with clients, which ranges from 25 and 30 years.

### 3.3 Property, plant and equipment

Property, plant and equipment is recognised at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably. The carrying amount of any component accounted for as a separate asset is derecognised when replaced. All other repairs and maintenance are charged to profit or loss during the reporting period in which they are incurred.

Depreciation of property, plant and equipment, is calculated systematically using the straight-line method over their estimated useful lives, taking into account the depreciation actually suffered by their operation and use.

	<u>Useful life</u>
Plants (distribution network)	20 - 25
Other plant and machinery	8 - 20
LPG Plants	25 - 30

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at the end of each reporting period.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 3.4).

Gains and losses on disposals are calculated based on the difference between net proceeds from selling the asset and their carrying amount. These are included in profit or loss.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

#### **3.4 Impairment of assets**

Goodwill and intangible assets that have an indefinite useful life are not subject to amortisation and are tested annually for impairment, or more frequently if events or changes in circumstances indicate that they might be impaired. Other assets are tested for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's fair value less costs of disposal and value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash-generating units). Non-financial assets other than goodwill that suffered an impairment are reviewed for possible reversal of the impairment at the end of each reporting period.

In this sense, for the impairment test analysis, the Company has included all assets in the CGU of gas distribution.

#### **3.5 Right-of-use assets and lease liabilities**

Until first-time application of IFRS 16, which came into effect as of 1 January 2019, the Company classified leases on the basis of whether the risks and rewards of ownership were substantially transferred, distinguishing between operating leases, wherein the lessor retained a significant portion of the risks and rewards of ownership of the leased asset, and finance leases, wherein the significant risks and rewards of ownership of the assets were transferred to the Company. Assets recognized as finance leases were presented in the financial statements based on the nature of the leased asset.

As a result of applying IFRS 16 as of 1 January 2019, the Company applies the following criteria:

##### **(i) Identifying a lease**

At inception of a contract, the Company assesses whether the contract contains a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The period of time that the Company uses an asset includes consecutive and non-consecutive periods of time. The Company only reassesses the terms and conditions when the contract is modified.

##### **(ii) Lessee accounting**

For a contract that contains a lease component and one or more additional lease or non-lease components, the Company allocates the consideration in the contract to each lease component on the basis of the relative stand-alone price of the lease component and the aggregate stand-alone price of the non-lease components.

Payments made by the Company that do not lead to the transfer of goods or services to it by the lessor, do not constitute a separate lease component, but form part of the total consideration under the contract.

**MADRILEÑA RED DE GAS, S.A.U.**

**NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED  
ON DECEMBER 31<sup>st</sup> 2019  
(Expressed in thousand of euros)**

At the commencement date, the Company recognises a right-of-use asset and a lease liability. The right-of-use asset comprises the amount of the lease liability, any lease payments made at or before the commencement date, less any lease incentives received, the initial direct costs incurred and an estimate of any dismantling or restoration costs to be incurred, as indicated in the accounting policy for provisions.

The Company measures the lease liability at the present value of the lease payments that are not paid at the commencement date. The Company discounts the lease payments using the appropriate incremental interest rate, unless the interest rate implicit in the lease can be readily determined.

Unpaid lease payments comprise fixed payments, less any lease incentives receivable, variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date, amounts expected to be payable by the lessee under residual value guarantees, the exercise price of a purchase option if the lessee is reasonably certain to exercise that option and payments of penalties for terminating the lease, if the lease term reflects the lessee exercising an option to terminate the lease.

The Company measures the right-of-use assets at cost, less any accumulated depreciation and any accumulated impairment, adjusted for any remeasurement of the lease liability.

If the lease transfers ownership of the asset to the Company at the end of the lease term or if the right-of-use asset includes the price of the purchase option, the depreciation criteria indicated in the section on property, plant and equipment are applied from the commencement date to the end of the useful life of the asset. Otherwise, the Company depreciates the right-of-use asset from the commencement date to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term.

The Company applies the impairment criteria for non-current assets indicated in section 3.4 to determine whether the right-of-use asset is impaired.

The Company measures the lease liability by increasing the carrying amount to reflect the accrued finance cost, reducing the carrying amount to reflect the lease payments made and remeasuring the carrying amount to reflect any lease modifications or to reflect revised substance fixed lease payments.

The Company recognises variable lease payments not included in the initial measurement of the lease liability in profit or loss for the period in which the events that trigger their payment occur.

The Company recognises the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset, until this is reduced to zero and thereafter in profit or loss.

The Company remeasures the lease liability by discounting the lease payments using a revised discount rate if either there is a change in the lease term or there is a change in the assessment of an option to purchase the underlying asset.



## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

The Company remeasures the lease liability if there is a change in the amounts expected to be payable under a residual value guarantee or there is a change in an index or a rate used to determine the payments, including a change to reflect changes in market rental rates following a market rent review.

The Company recognises a lease modification as a separate lease if the modification increases the scope of the lease by adding rights to use one or more assets and the consideration for the lease increases by an amount commensurate with the stand-alone price for the increase in scope and any appropriate adjustments to that stand-alone price to reflect the circumstances of the particular contract.

If the modification does not result in a separate lease, at the effective date of the lease modification, the Company allocates the consideration in the modified contract as indicated above, determines again the lease term and remeasures the lease liability by discounting the revised lease payments using a revised discount rate. The Company decreases the carrying amount of the right-of-use asset to reflect the partial or full termination of the lease for lease modifications that decrease the scope of the lease, recognising the gain or loss in profit or loss. The Company adjusts the carrying amount of the right-of-use asset for all other lease modifications.

#### **(iii) Lessor accounting**

For a contract that contains a lease component and one or more additional lease or non-lease components, the Company allocates the consideration in the contract as indicated in the accounting policy for revenue from contracts with customers.

The Company classifies contracts as finance leases when substantially all the risks and rewards incidental to ownership of the leased asset are transferred to the lessee at the start of the lease. All other leases are classified as operating leases.

#### **☐ Finance leases**

The Company recognises a receivable for an amount equal to the present value of the lease payments plus the unguaranteed residual value, discounted at the contractual interest rate implicit in the lease (net investment in the lease). Initial direct costs are included in the initial measurement of the finance lease receivable and reduce the amount of income recognised over the lease term. Finance income is taken to the income statement using the effective interest method.

At the commencement of the lease, the Company recognises as lease receivables the amounts not yet collected relating to fixed payments, less any lease incentives payable, variable lease payments that depend on an index or a rate, measured using the index or rate as at the commencement date, any residual value guarantees provided to the lessor by the lessee, a party related to the lessee or a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee, the exercise price of any purchase option if the lessee is reasonably certain to exercise that option and payments of penalties for terminating the lease, if the lease term reflects the lessee exercising an option to terminate the lease.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

The Company recognises a finance lease modification as a separate lease if the modification increases the scope of the lease by adding one or more rights of use and the consideration for the lease increases by an amount commensurate with the stand-alone price for the increase in scope and any appropriate adjustments to that stand-alone price to reflect the circumstances of the particular contract.

If the modification to a finance lease is not accounted for as a separate lease and if the lease would have been classified as an operating lease had the modification been in effect at the inception date, the Company accounts for the lease modification as a new lease from the effective date of the modification and measures the carrying amount of the underlying asset as the net investment in the lease immediately before the effective date of the lease modification. Otherwise, the Company applies the modification requirements indicated in the accounting policy for financial instruments.

The Company regularly reviews unguaranteed residual values. If there has been a reduction, the Company revises the income allocation over the lease term and recognises immediately any reduction in respect of amounts accrued in profit or loss.

#### ☐ Operating leases

The Company recognises operating lease income, net of incentives granted, as income on a straight-line basis over the lease term, unless another systematic basis is more representative of the pattern in which benefit from the use of the leased asset is diminished.

The initial direct costs of the lease are included in the carrying amount of the leased asset and recognised as an expense over the lease term on the same basis as the lease income.

The Company recognises variable lease payments as income when it is likely that they will be received, which is generally when the events that trigger their payment occur.

The Company recognises modifications to operating leases as a new lease from the effective date of the modification, considering any prepayment or deferred payment in respect of the original lease as part of the lease payments for the new lease.

#### ☐ (iv) Cash-flow statement

The Company has classified:

- Cash payments for the principal portion of lease payments as financing activities;
- Cash payments for the interest portion as operating activities consistent with the presentation of interest payments chosen by the Company.
- Short-term lease payments and payments for leases of low-value assets as operating activities.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### 3.6 Financial assets

##### (i) Classification

From January 1<sup>st</sup> 2018, the Company classifies its financial assets in the following measurement categories:

- those to be measured subsequently at fair value (either through Other Comprehensive Income (OCI) or through profit or loss), and
- those to be measured at amortised cost.

The classification depends on the entity's business model for managing the financial assets and the contractual terms of the cash flows. IFRS9 (4.1.4),(5.7.1).

For assets measured at fair value, gains and losses will either be recorded in profit or loss or OCI. For investments in equity instruments that are not held for trading, this will depend on whether the Company has made an irrevocable election at the time of initial recognition to account for the equity investment at fair value through other comprehensive income (FVOCI).

Financial assets shall not be reclassified after initial recognition unless the Company changes its business model for managing financial assets.

##### (ii) Recognition and derecognition

Regular way purchases and sales of financial assets are recognised on trade-date, the date on which the Company commits to purchase or sell the asset. Financial assets are derecognised when the rights to receive cash flows from the financial assets have expired or have been transferred and the Company has transferred substantially all the risks and rewards of ownership.

##### (iii) Measurement

At initial recognition, the Company measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVPL are expensed in profit or loss.

Financial assets with embedded derivatives are considered in their entirety when determining whether their cash flows are solely payment of principal and interest.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### *Debt instruments*

Subsequent measurement of debt instruments depends on the Company's business model for managing the asset and the cash flow characteristics of the asset. There are three measurement categories into which the Company classifies its debt instruments:

- Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortised cost. Interest income from these financial assets is included in finance income using the effective interest rate method. Any gain or loss arising on derecognition is recognised directly in profit or loss and presented in other gains/(losses) together with foreign exchange gains and losses. Impairment losses are presented as separate line item in the statement of profit or loss.
- FVOCI: Assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in the carrying amount are taken through OCI, except for the recognition of impairment gains or losses, interest income and foreign exchange gains and losses which are recognised in profit or loss. When the financial asset is derecognised, the cumulative gain or loss previously recognised in OCI is reclassified from equity to profit or loss and recognised in other gains/(losses). Interest income from these financial assets is included in finance income using the effective interest rate method. Foreign exchange gains and losses are presented in other gains/(losses) and impairment expenses are presented as separate line item in the statement of profit or loss.
- FVPL: Assets that do not meet the criteria for amortised cost or FVOCI are measured at FVPL. A gain or loss on a debt investment that is subsequently measured at FVPL is recognised in profit or loss and presented net within other gains/(losses) in the period in which it arises.

#### *(iv) Impairment*

From 1 January 2018, the Company assesses on a forward looking basis the expected credit losses associated with its debt instruments carried at amortized cost and FVOCI. The impairment methodology applied depends on whether there has been a significant increase in credit risk.

For trade receivables, the Company applies the simplified approach permitted by IFRS 9, which requires expected lifetime losses to be recognized from initial recognition of the receivables.

Until January 1<sup>st</sup> 2018, the basis of presentation was the following:

- a) Loans and receivables

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

Credits and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted on an active market and are not intended to be traded in the short-term. They are included in current assets, except for maturities longer than 12 months after the balance sheet date. These are classified as non-current assets.

These financial assets are initially recognized at fair value, including directly attributable transaction costs, and are subsequently measured at amortized cost. Accrued interest is recognized at the effective interest rate, which is the discount rate that brings the instrument's carrying amount into line with all estimated cash flows to maturity. Trade receivables falling due in less than one year are carried at face value at both initial recognition and subsequent measurement, provided that the effect of not discounting flows is not significant.

At the year-end, at least, the necessary value adjustments are made to account for impairment when there is objective evidence that all receivables will not be collected.

The amount of the impairment loss is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate prevailing at the date of initial recognition. Value adjustments, and reversals, where applicable, are recognized in the income statement.

#### **b) Cash and cash equivalents**

Cash and cash equivalents include cash at hand, time deposits with financial entities and other short-term investments noted for their great liquidity with an original maturity no longer than three months as from the acquisition date.

### **3.7 Financial liabilities**

#### **a) Trade and other payables**

This category includes trade and non-trade payables and financial debts. Borrowings are classified as current liabilities unless the Company has an unconditional right to defer settlement for at least 12 months as from the balance sheet date.

Payables are initially recognized at fair value, adjusted for directly attributable transaction costs, and subsequently measured at amortized cost using the effective interest method. The effective interest rate is the discount rate that brings the instrument's carrying amount into line with the expected future flow of payments to the maturity date of the liability.

Trade payables falling due in less than one year without a contractual interest rate are carried at their face value at both initial recognition and subsequent measurement, provided that the effect of not discounting flows is not significant.

In the event of the renegotiation of existing debts, the financial liability is not deemed to change significantly when the lender of the new loan is the same as the initial lender and the present value of cash flows, including net fees, is not more than 10% higher or lower than the present value of cash flows payable on the original liability, calculated using the same method.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

#### **3.8 Inventories**

Inventories are stated at the lower of cost and net realisable value. Costs are assigned to individual items of inventory on the basis of weighted average costs. Costs of purchased inventory are determined after deducting rebates and discounts. Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

#### **3.9 Equity**

Ordinary shares are classified as equity.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction, net of tax, from the proceeds.

When the Company purchases the company's equity instruments, the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the owners of the Company as treasury shares until the shares are cancelled or reissued. Where such ordinary shares are subsequently reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the owners.

The Company does not have any own shares.

Dividends on ordinary shares are recognized as a deduction from equity when they are approved.

#### **3.10 Grants and other liabilities**

Grants are recognised at their fair value where there is a reasonable assurance that the grant will be received and the Company will comply with all attached conditions. Government grants relating to costs are deferred and recognised in the profit or loss over the period necessary to match them with the costs that they are intended to compensate. Government grants relating to the purchase of property, plant and equipment are included in non-current liabilities as deferred income and are credited to profit or loss on a straight-line basis over the expected lives of the related assets.

The amounts recorded under the heading of "Grants" for charges for network displacements paid by third parties, assets transferred from third parties and for consideration of new connections are applied linearly to results systematically based on the useful life of the corresponding asset, thus compensating the expense for the provision of depreciation.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

Other liabilities also includes connection charges as monetary consideration for the installation works and operations required to serve new gas supply points or extend existing ones. These connection charges are recognized as income in proportion to the annual depreciation of the assets being financed (30 years), or over the period specified in the contract if this is shorter, or, where applicable, when the assets are disposed of or impaired.

#### 3.11 Employee benefits

##### a) Pension commitments

##### Defined contribution pension plans

Under a fixed contribution plan, the Company makes fixed contributions to a separate entity and has no legal, contractual or implicit obligation to make additional contributions if this separated entity does not have sufficient assets to meet the commitments assumed.

The Company has recognised external defined contribution retirement and insured benefit plans to cover death and disability contingencies, which are in line with current pension plan and fund legislation and which cover its commitments to current personnel affected. It recognises certain economic rights for past services that are fully paid and is obligated to make a contribution of a percentage of computable salary according to the type of group. There are also defined retirement contribution plans to compensate management loyalty.

The annual contributions to cover the commitments accrued to the Company in relation to the plans are charged to the profit and loss account each year.

The Company recognises a liability in respect of the contributions to be made when at the year-end there are accrued contributions not paid.

##### b) Other post-employment obligations

The Company provide post-employment benefits to some of their retirees. The entitlement to these benefits is usually conditional on the employee remaining in service up to retirement age.

The expected costs of these benefits are accrued over the working life of the employees and the liability recognised for these commitments is equivalent to the current value of the obligation at the balance sheet date. The obligation for other commitments is calculated annually by the Company using the projected credit method. The current value of the obligation is determined by discounting the estimated future cash flows at a technical interest rate based in a curve of rates that takes into account the commitments duration and taking as reference the market performance, at the balance sheet date, corresponding to the emission of high credit rating bonds and obligations.

The Company's policy for amortizing the actuarial gains and losses of post-employment commitments consists of the immediate recognition in equity when they arise. The actuarial gains and losses arise from changes in the actuarial assumptions or from differences between the assumptions and reality.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### c) Termination benefits

Termination benefits are payable when employment is terminated by the Company before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. The Company recognises termination benefits at the earlier of the following dates: (a) when the Company can no longer withdraw the offer of those benefits; and (b) when the entity recognises costs for a restructuring that is within the scope of IAS 37 and involves the payment of terminations benefits. In the case of an offer made to encourage voluntary redundancy, the termination benefits are measured based on the number of employees expected to accept the offer. Benefits falling due more than 12 months after the end of the reporting period are discounted to present value.

#### 3.12 Provisions

Provisions are recognized when the Company has a present legal or implicit obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated. Provisions are not recognised for future operating losses.

The Company has the obligation to dismantle certain facilities at the end of its useful life. For this purpose, the present value of the cost of carrying value of these tasks is recorded in property, plant and equipment. This estimate is reviewed annually so that the provision reflects the present value of future costs by increasing or decreasing the value of the asset. The change in the provision arising from its financial update is charged to the "Financial expenses" caption.

Where there are a number of similar obligations, the likelihood that an outflow will be required in settlement is determined by considering the class of obligations as a whole. A provision is recognised even if the likelihood of an outflow with respect to any one item included in the same class of obligations may be small.

Provisions are measured at the present value of management's best estimate of the expenditure required to settle the present obligation at the end of the reporting period. The discount rate used to determine the present value is a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The increase in the provision due to the passage of time is recognised as interest expense.

Provisions maturing in one year or less, with an immaterial financial effect, are not discounted.

Where a part of the outflow necessary to settle the obligation is expected to be reimbursed by a third party, the reimbursement is recognized as a separate asset, just in the case that the collection is guaranteed.

The possible obligations coming as a consequence of past events, where its realization is conditioned to whether happens or not one or more future events independently of the Company's will are considered as contingent liabilities. Such contingent liabilities are not part of the accounting books and does not present details in the notes. (Note 23).



## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

#### **3.13 Income tax**

The income tax expense or credit for the period is the tax payable on the current period's taxable income based on the applicable income tax rate for each jurisdiction adjusted by changes in deferred income tax assets and liabilities attributable to temporary differences and to unused tax losses.

The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the end of the reporting period. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is provided, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. However, deferred income tax liabilities are not recognized if they arise from the initial recognition of goodwill. Deferred income tax is neither accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit nor loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the end of the reporting period and are expected to apply when the related deferred income tax asset is realized or the deferred income tax liability is settled.

Deferred income tax assets are recognised only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority. Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Current and deferred tax is recognised in profit or loss, except to the extent that it relates to items recognised in other comprehensive income or directly in equity. In this case, the tax is also recognised in other comprehensive income or directly in equity, respectively.

#### **3.14 Revenue recognition**

Revenues derived from contracts with customers must be recognised based on compliance with performance obligations with customers. Revenue reflects the transfer of goods or services to customers at an amount that reflects the consideration to which Madrileña Red de Gas expects to be entitled in exchange for such goods or services. Five steps are established for the recognition of revenue: 1. Identify the customer's contract(s) 2. Identify the performance obligations 3. Determine the price of the transaction 4. Allocate the transaction price to the performance obligations 5. Recognise the revenue according to the fulfilment of each obligation.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

With the distribution activity the regulatory framework identifies the following tasks: to build, operate and maintain networks and facilities for the distribution of natural gas intended for situating the gas at the points of consumption.

This set of tasks constitutes a commitment to the customers and the tasks cannot be performed independently from each other; therefore they are considered to be a single performance obligation which is fulfilled, indefinitely, in accordance with the administrative authorization granted by the competent institution on the basis of which it carries out its business, generating the right to receive remuneration or revenue. In this respect, consumers of gas simultaneously receive and consume the benefits of the service at the same time as the Company provides it.

The rights for the users' registrations are recorded as income in the year when the supply is contracted.

Revenue from services provided are only recognised when the amount of the gains, the realization grade, the incurred and outstanding costs, may be reliably estimated and it is probable that the economic benefits derived from the service will be collected. These gains are recognised considering the percentage of completion method of the service provided at the balance sheet date. The method to measure the percentage of completion is the output method.

#### **Distribution activity**

Note 2 describe the basic features of the regulations applicable to the Company.

The regulatory framework for the natural gas industry in Spain regulates a payment procedure for the redistribution amongst companies in the sector of the net turnover obtained, so that each company receives the remuneration recognised for its regulated activities.

The remuneration of the gas distribution is calculated and registered as income on the basis of the update of prior year remuneration, average increase of consumers, and the volume of energy circulated, according to the Ministerial Order that determines it each year and is adjusted by real data.

The remuneration gains from the distribution activities of each year are fixed with ex-ante character. In the Ministerial Orders that are published every year, a preview remuneration is established for the following year based on the sales expectations and customer attraction for the following year. This originates that the remuneration amount is subject to change for up to two years, until the definite data on demand and new customer is available for the year analysed. Based on this, Order TEC/1259/2019 of December 20<sup>th</sup> has regularized the retribution for 2019 and 2018 and the Order EC/1367/2018 of December 22<sup>nd</sup> regularized the retribution for 2018 and 2017 according to the updated sales and customers' figures.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

In the case of the distribution activity, the regulatory review carried out by Law 18/2014 was based on carrying out a new assessment of the remuneration bases of the agents who, reducing the total amount by approximately 110 million euros, considering positively the growth realized since the last regulatory review (realized in the year 2002) and giving a special value to the domestic consumption, that is the one that allows to introduce more tolls to the system. These remuneration bases will be updated annually, taking into account the increase in consumption and number of consumers connected to each distributor, especially encouraging the gasification of new municipalities, which will bring the national gasification index, currently 29%, to the countries average which are considerably higher. In order to do so, this law established unitary compensation values for each client and unit of energy incorporated, which in principle will remain fixed for the entire regulatory period (which will end on December 31<sup>st</sup> 2020) and, which are those applied to the growth's forecasts that each distributor has for the subsequent year, determine their provisional annual remuneration.

These Remunerations to the Distribution Activity will be adjusted once the Ministry of Ecological Transition (currently called Ministry of Ecological Transition and Demographic Challenge) establishes the definitive amounts of said remuneration from the actual figures of average increase of consumers and increase of vehicular kWh. The Company believes that there will be no significant differences between the amounts recorded and the final settlements.

However, these differences, when they occur, will be charged as a change of estimate in the Income Statement.

The Ministerial Order of October 28<sup>th</sup> 2002 by which the settlement procedures are regulated, establishes that the deviations occurred by the application of settlement procedures between the definite settled net gains and the credited remunerations each year, will be taken into account in the calculation of tariffs, tolls and levies for the following two years.

The Royal Decree-Law 8/2014, of July 4<sup>th</sup> (Note 2.1.2) establishes the accumulated deficit recognition of the gas system at December 31<sup>st</sup> 2014. The parties of the settlement system, including the Company, shall be entitled to recover said deficit for a period of fifteen years, with annuities to be included as a cost of the system and in which an interest rate shall be recognized in conditions equivalent to those of the market. On the other hand, the temporary mismatches produced between the revenues and costs of the gas system will be financed by the individuals in the settlement system, including the Company, generating a right to its recovery during the following five years, recognizing a type of interest in market conditions. As a result, the financing of the gas system's deficit of revenues is recorded as a financial asset according to which, under this regulation, there is the right to receive its refund without being subject to future contingent factors.

The Company recognises revenue when the amount may be reliably estimated, or in other words, when it is likely that the future economic benefits will flow to the Company.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

#### Registration fees

The registration fees of a new supply consists of the operation to connect the gas receiving facility to the network of the distribution company, and the review and verification that these adapt to the regulatory technical and safety conditions. This operation usually takes place one sole time and the activities are inseparable, whereby this activity is considered as constituting a single performance obligation.

Registration fees are regulated by each Autonomous Region at a set price.

The Company recognises the revenue for the registration fees at the moment at which the connection is made and verified, since it is at that moment when the customer obtains the benefits of the service rendered and there is no future obligation associated with it.

#### Rental of Natural Gas and Liquefied Petroleum Gas (LPG) metering equipment

Metering equipment (meter) is installed in the facilities of the end-customer, therefore the service of renting the meter constitutes a performance obligation.

The payment for renting natural gas metering equipment is regulated by the regulatory framework of the sector, at a set price.

The Company recognises the revenue throughout the provision of the service, since the customer simultaneously receives and consumes the benefits of the service at the same time the Company provides it.

The method to be used to measure the percentage of completion is the output method, since the service rendered is similar throughout the period, and revenue is recognised on a straight-line basis over time.

#### Rental of Community Receiving Facilities (CRF)

The Company collects a rental payment for the community receiving facility from the owners association without any other type of consideration, therefore the CRF comprises a single performance obligation.

The payment for renting the community receiving facility is the price established in the contract signed with the owners association, which sets a fixed monthly price.

The Company recognises the revenue throughout the term of the contract, since the customer simultaneously receives and consumes the benefits of the service at the same time the Company provides it.

The method to be used to measure the percentage of completion is the output method, since the service rendered is similar throughout the period, and revenue is recognised on a straight-line basis over time.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

#### Inspections of individual receiving facilities (IRF)

The service consists of the inspection of the individual receiving facility (IRF), involving a one-time action, considered as a single performance obligation.

The authority to set inspection is transferred to the Autonomous Region and, therefore, the price may vary from one area to another.

The revenue is recognized at the moment of the inspection, since it is at that time when the customer obtains the benefits of the service rendered.

#### Sale of Liquefied Petroleum Gas (LPG)

The contracts for the sale of LPG identify two separate performance obligations, which are those corresponding to the supply of LPG and the rental of the meter since, as mentioned above, they comply with the definition for considerations as different from each other. For LPG, the Company supplies as well as distributes the product, and therefore there is a contractual relationship with the customer.

In the case of LPG consumption, the transaction price will be established applying the established official tariff, with a fixed portion (standard monthly rate) and a variable element associated with consumption (Euro cents per Kg.)

The Company recognises the revenue throughout the period of time in which the customer receives and consumes the benefits of the service rendered at the same time the services takes place. Therefore, the revenue deriving from this service will be measured by percentage of completion.

For the purpose of measuring this completion, the Company considers that the output method is the one that best reflects the completion of the rendering of the service, whereby the revenue is recognized as the service is rendered, by unit of LPG (Kg) consumed by the customer.

#### Contracting party connection charges

The connection charge of the contracting party consists of the financial consideration for connecting the community receiving facility to the network and the commissioning of the facility. This operation usually takes place at one sole time, whereby it is considered as a single performance obligation.

The connection charges are regulated by the regulatory framework of the sector, at a set price.

The revenue is recognized at the moment of connection of the community receiving facility and the commissioning of gas, since this is the time at which control of the services rendered is transferred to the customer.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

#### Applicant connection charges

The Company is authorized to receive a financial consideration for performing the set of installations and operations necessary to cover a new gas supply point or increase the capacity of one already in existence.

In this case, a contract is arranged with the customer to establish the characteristics of the installation to be built and the quantity to be received for each service. Furthermore, it is established that the asset built by virtue of the contract will be the property of the Company and a remuneration for building the connection is established. This consideration is a determined fixed quantity.

The Company recognises these connection charges as income in proportion to the annual depreciation of the assets being financed (20 years), or over the period specified in the contract if this is less or, where applicable, when their disposal or impairment occurs, since the customer simultaneously receives and consumes the benefits of the service at the same time the Company provides them. The method to be used to measure the percentage of completion is the output method, since the service rendered is similar throughout the period, and revenue is recognized on a straight-line basis over time.

#### Interest income

Interest income is recognised using the effective interest method.

### **3.15 Functional and presentation currency**

The Company's annual accounts are stated in euros, which is the functional and presentation currency of the Company.

### **3.16 Transactions with related parties**

In general, transactions between group companies are initially recognised at fair value. If applicable, where the agreed price differs from the fair value, the difference is recognised based on the economic reality of the transaction. Transactions are subsequently measured in accordance with applicable standards.

### **3.17 Environmental assets**

Expenses relating to the protection and restoration of the environment, are registered as an expense in the year in which they arise unless they are related to assets' investments where its purpose is the minimization of the environment's impact and the protection and restoration of the environment, in that case, it is registered as a greater value of the asset.

# MADRILEÑA RED DE GAS, S.A.U.

## NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

### 4. Reconciliation from Spanish GAAP (PGC) to IFRS-EU

The following reconciliation includes the reconciliation of the balance sheet between PGC and IFRS-EU (Note 4.1) as of December 31<sup>st</sup> 2019 and December 31<sup>st</sup> 2018, the reconciliation of the profit/loss for the year and the global profit/loss for the financial years ended on December 31<sup>st</sup> 2019 and December 31<sup>st</sup> 2018, the effect in the profit/loss statement for the year ended on December 31<sup>st</sup> 2019 and December 31<sup>st</sup> 2018 (Note 4.2 and Note 4.3 respectively), as well as the re-classifications included because of the transition to IFRS-EU (Note 4.4).

#### 4.1 Reconciliation of the balance sheet

The reconciliation of the balance sheet at December 31<sup>st</sup> 2019 is as follows:

	Thousand euros		
	December 31 <sup>st</sup> 2019		
	Local GAAP	Adjustments	IFRS-EU
<b>NON-CURRENT ASSETS</b>	<b>968,799</b>	<b>271,685</b>	<b>1,240,484</b>
Intangible assets and goodwill (b) (e)	527,646	280,703	808,349
Property, plant and equipment (c)	354,120	742	354,862
Non-current investments in group companies	54,734	-	54,734
Financial assets	1,006	-	1,006
Deferred tax assets	31,293	(9,760)	21,533
<b>CURRENT ASSETS</b>	<b>145,723</b>	<b>-</b>	<b>145,723</b>
Inventories	2,570	-	2,570
Trade and other receivables	39,137	-	39,137
Deferred expenses	590	-	590
Cash and cash equivalents	103,426	-	103,426
<b>TOTAL ASSETS</b>	<b>1,114,522</b>	<b>271,685</b>	<b>1,386,207</b>

	Thousand euros		
	December 31 <sup>st</sup> 2019		
	Local GAAP	Adjustments	IFRS-EU
<b>EQUITY</b>	<b>110,720</b>	<b>187,365</b>	<b>298,085</b>
Capital	1,048	-	1,048
Share premium	100,354	-	100,354
Reserves	15,280	116,442	131,722
Prior periods' losses	(33,240)	33,240	-
Profit/(loss) for the year	4,112	60,849	64,961
Grants, donations and legacies received (a)	23,166	(23,166)	-
<b>NON-CURRENT LIABILITIES</b>	<b>958,034</b>	<b>83,411</b>	<b>1,041,445</b>
Provisions	4,761	-	4,761
Other non-current liabilities (c)	1,479	370	1,849
Payables to related parties	943,839	-	943,839
Deferred income (a)	-	30,892	30,892
Deferred tax liabilities (a) (b)	7,955	52,149	60,104
<b>CURRENT LIABILITIES</b>	<b>45,768</b>	<b>909</b>	<b>46,677</b>
Provisions	1,705	-	1,705
Financial liabilities (c)	82	372	454
Payables to related parties	12,003	-	12,003
Trade and other payables	31,978	537	32,515
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>1,114,522</b>	<b>271,685</b>	<b>1,386,207</b>

# MADRILEÑA RED DE GAS, S.A.U.

## NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

The reconciliation of the balance sheet at December 31<sup>st</sup> 2018 was as follows:

	Thousand euros December 31 <sup>st</sup> 2018		
	Local GAAP	Adjustments	IFRS-EU
<b>NON-CURRENT ASSETS</b>	<b>1,002,450</b>	<b>199,576</b>	<b>1,202,026</b>
Intangible assets (b) (e)	607,045	199,576	806,621
Property, plant and equipment	368,619	-	368,619
Financial assets	1,854	-	1,854
Deferred tax assets	24,932	-	24,932
<b>CURRENT ASSETS</b>	<b>118,857</b>	<b>-</b>	<b>118,857</b>
Inventories	2,651	-	2,651
Trade and other receivables	52,490	-	52,490
Deferred expenses	674	-	674
Cash and cash equivalents	63,042	-	63,042
<b>TOTAL ASSETS</b>	<b>1,121,307</b>	<b>199,576</b>	<b>1,320,883</b>

	Thousand euros December 31 <sup>st</sup> 2018		
	Local GAAP	Adjustments	IFRS-EU
<b>EQUITY</b>	<b>105,127</b>	<b>128,147</b>	<b>233,274</b>
Capital	1,048	-	1,048
Share premium	100,354	-	100,354
Reserves	15,430	65,437	80,867
Prior periods' losses	(23,746)	23,746	-
Profit/(loss) for the year	(9,494)	60,499	51,005
Grants, donations and legacies received (a)	21,535	(21,535)	-
<b>NON-CURRENT LIABILITIES</b>	<b>957,311</b>	<b>71,218</b>	<b>1,028,529</b>
Provisions	5,276	-	5,276
Other non-current liabilities	1,656	-	1,656
Payables to related parties	942,640	-	942,640
Deferred income (a)	-	28,720	28,720
Deferred tax liabilities (a) (b)	7,739	42,498	50,237
<b>CURRENT LIABILITIES</b>	<b>58,869</b>	<b>211</b>	<b>59,080</b>
Provisions	2,336	-	2,336
Financial liabilities	84	-	84
Payables to related parties	12,007	-	12,007
Trade and other payables	44,442	211	44,653
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>1,121,307</b>	<b>199,576</b>	<b>1,320,883</b>

- (a) Under Local GAAP, grants are classified within the equity caption, whereas under IFRS-EU grants are classified as deferred income under the "Deferred income" caption on the balance sheet.
- (b) This adjustment reflects the effect of amortization of goodwill and intangible assets reversed in 2019, 2018 and 2017 (Note 4.2(a)).
- (c) The application of IFRS 16 is not applicable under Local GAAP.





# MADRILEÑA RED DE GAS, S.A.U.

## NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

### 4.2 Reconciliation of income statement at December 31<sup>st</sup> 2019 and 2018

The reconciliation of statement of profit or loss at December 31<sup>st</sup> 2019 is as follows:

	Thousand euros		
	December 31 <sup>st</sup> 2019		
	Local GAAP	Adjustments	IFRS-EU
<b>CONTINUING OPERATIONS</b>			
Revenues	184,146	-	184,146
Raw materials and consumables	(10,294)	-	(10,294)
Work carried out by the company for assets	1,060	-	1,060
Other income	2,184	-	2,184
Staff costs	(11,955)	-	(11,955)
Other operating expenses (c) (e)	(22,348)	1,734	(20,614)
Amortisation and depreciation (d)	(108,537)	79,426	(29,111)
Impairment and gains/(losses) on disposal of fixed assets	(4)	-	(4)
Other results	(1,704)	-	(1,704)
<b>OPERATING PROFIT</b>	<b>32,548</b>	<b>81,160</b>	<b>113,708</b>
Financial income	1,773	-	1,773
Financial costs (c)	(29,091)	(29)	(29,120)
<b>NET FINANCIAL INCOME/(EXPENSE)</b>	<b>(27,318)</b>	<b>(29)</b>	<b>(27,347)</b>
<b>PROFIT BEFORE INCOME TAX</b>	<b>5,230</b>	<b>81,131</b>	<b>86,361</b>
Income tax	(1,118)	(20,282)	(21,400)
<b>PROFIT FOR THE PERIOD</b>	<b>4,112</b>	<b>60,849</b>	<b>64,961</b>

The reconciliation of statement of profit or loss at December 31<sup>st</sup> 2018 is as follows:

	Thousand euros		
	December 31 <sup>st</sup> 2018		
	Local GAAP	Adjustments	IFRS-EU
<b>CONTINUING OPERATIONS</b>			
Revenues	186,278	-	186,278
Raw materials and consumables	(16,074)	-	(16,074)
Work carried out by the company for assets	904	-	904
Other income	2,076	-	2,076
Staff costs	(11,668)	-	(11,668)
Other operating expenses (e)	(22,878)	942	(21,936)
Amortisation and depreciation (d)	(107,945)	79,723	(28,222)
Other results	(746)	-	(746)
<b>OPERATING PROFIT</b>	<b>29,947</b>	<b>80,665</b>	<b>110,612</b>
Financial income	33	-	33
Financial costs	(42,896)	-	(42,896)
<b>NET FINANCIAL INCOME/(EXPENSE)</b>	<b>(42,863)</b>	<b>-</b>	<b>(42,863)</b>
<b>PROFIT BEFORE INCOME TAX</b>	<b>(12,916)</b>	<b>80,665</b>	<b>67,749</b>
Income tax	3,422	(20,166)	(16,744)
<b>PROFIT FOR THE PERIOD</b>	<b>(9,494)</b>	<b>60,499</b>	<b>51,005</b>

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

- (d) According to the RD 602/2016 December 2nd, under PGC the administrative concessions are considered as assets with definite useful lives, so the assets are being amortized. Additionally, the goodwill also must be amortized during its useful life, with no evidence proving the contrary, it is said to be 10 years and its recovery is straight-line. Because of the differences in the accounting policies regarding IFRS-EU such amortizations are reversed in the process to convert the financial statements into IFRS-EU, as well as the tax effect.
- (e) Commercial acquisition costs activated according to IFRS 15.

#### 4.3 Reconciliation of comprehensive income

The adjustments for the statement of comprehensive income of the year ended December 31<sup>st</sup> 2019 is as follows:

	Thousand euros December 31 <sup>st</sup> 2019		
	Local GAAP	Adjustments	IFRS-EU
Profit for the period	4,112	60,849	64,961
Items that will not be reclassified to profit or loss:			
Grants, donations and legacies received	4,359	(4,359)	-
On actuarial gains and losses and other adjustments (net of tax)	(150)	-	(150)
Income tax	(1,090)	1,090	-
Total income and expenses recognized in equity	3,119	(3,269)	(150)
Transfers to profit and loss			
Grants, donations and legacies received	(2,184)	2,184	-
Income tax	546	(546)	-
Total transfers to profit and loss	(1,638)	1,638	-
	5,593	59,218	64,811

The adjustments for the statement of comprehensive income of the year ended December 31<sup>st</sup> 2018 is as follows:

	Thousand euros December 31 <sup>st</sup> 2018		
	Local GAAP	Adjustments	IFRS-EU
Profit for the period	(9,494)	60,499	51,005
Items that will not be reclassified to profit or loss:			
Grants, donations and legacies received	2,781	(2,781)	-
On actuarial gains and losses and other adjustments (net of tax)	69	-	69
Income tax	(695)	695	-
Total income and expenses recognized in equity	2,155	(2,086)	69
Transfers to profit and loss			
Grants, donations and legacies received	(2,076)	2,076	-
Income tax	519	(519)	-
Total transfers to profit and loss	(1,557)	1,557	-
	(8,896)	59,970	51,074

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

#### **5. Financial Risk Management**

The Company's activities have no significant exposure to exchange rate risk and the fluctuation of interest rate. However, the Company is exposed to credit and liquidity risk.

The Company's Management focuses on maintaining a solid financial structure that optimises the cost of capital and the availability of financial resources to guarantee business continuity over the long term, in order to enhance value for shareholders while ensuring a solid credit profile. In this regard, the senior unsecured debt credit ratings assigned to the Company by Standard & Poor's and Fitch remain, respectively at BBB.

##### **5.1 Financial risk factors**

###### **Credit Risk**

In accordance with its corporate objects, the Company collects for the gas system the amounts relating to tolls to access the connection point network located in its distribution territory by invoicing to supply companies. On a monthly basis and within the settlement system framework coordinated by CNMC, a calculation is performed of the excess or shortfall in access tolls invoicing with respect to the remuneration recognised to the Company. If toll invoicing exceeds the remuneration recognized, the Company must settle such difference in favour of other gas system companies. Otherwise, the Company will receive from such companies the remaining balance to complete the remuneration recognized.

Regulations in this respect consider tolls invoiced to the supply companies to be collected for the purposes of the settlement system described above, and therefore in the event of non-payment by such counterparties, the Company is exposed to a credit risk with respect to part of its revenues.

The Company actively manages the above mentioned credit risk through a follow-up of outstanding receivable balances. Similarly, and taking into account (i) the reduced average collection period, less than 30 days, (ii) the regulatory supervisory framework in which gas system activities are performed and (iii) the mechanisms for suspending the contracts for Third-party Network Access in the event of non-payment of tolls to the Company (after a period of 60 days after a reliable request of the counterparty), exposure to the credit risk is considered to be limited.

###### **Interest rate risk**

During the current year, the Company has been exposed to several financial risks, mainly to interest rate risk.

The Company's interest rate risk results from long-term external borrowing and loans granted to the parent company at fixed rates. Therefore, a change in interest rates at the reporting date would not affect profit and loss.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### Liquidity and availability of funding risks

The Company maintains a liquidity policy that ensures compliance with the payment commitments acquired, diversifying the coverage of financing needs and debt maturities. Prudent liquidity risk management includes the maintenance of sufficient cash and realizable assets and the availability of funds for an adequate amount to cover the obligations.

On December 31<sup>st</sup> 2019, available liquidity amounts to Euros 303,426 thousand (December 31<sup>st</sup> 2018: Euros 263,042 thousand), taking into account cash and equivalents (Euros 103,426 thousand on December 31<sup>st</sup> 2019 and Euros 63,042 thousand on December 31<sup>st</sup> 2018) and unused equivalent credit lines (Euros 200,000 thousand on December 31<sup>st</sup> 2019 and Euros 200,000 thousand on December 31<sup>st</sup> 2018) (Note 14).

The Company's business and investment plans are mainly financed through cash generated from on-going operations and, occasionally, through revolving credit facilities.

It is the Company policy to match the debt's amortisation calendar to its capacity to generate cash flows to meet these maturities. In particular, the Company's Management attempts to ensure that the operations over the next 12 months are always fully financed without the need to substantially modify the conditions and structure of the Company's debt.

Management considers the Company has enough cash reserves to address the payments to realize the following 12 months.

The tables below analyse the Company's financial liabilities into relevant maturity groupings based on their contractual maturities for all non-derivative financial liabilities. The amounts disclosed in the table are the contractual undiscounted cash flows (in thousand of euros).

	31/12/2020	31/12/2021	31/12/2022	31/12/2023	Over 5 years	Total
<b>At December 31, 2019</b>						
Payables to related parties	27,558	27,558	29,358	302,468	750,630	1,137,572
Trade and other payables	27,265	-	-	-	-	27,265
Other accounts payable	454	204	204	204	867	1,933
<b>Total</b>	<b>55,277</b>	<b>27,762</b>	<b>29,562</b>	<b>302,672</b>	<b>751,497</b>	<b>1,166,770</b>
	31/12/2019	31/12/2020	31/12/2021	31/12/2022	Over 5 years	Total
<b>At December 31, 2018</b>						
Payables to related parties	28,284	28,284	28,284	30,084	1,052,114	1,167,050
Trade and other payables	40,075	-	-	-	-	40,075
Other accounts payable	84	204	204	204	1,044	1,740
<b>Total</b>	<b>68,443</b>	<b>28,488</b>	<b>28,488</b>	<b>30,288</b>	<b>1,053,158</b>	<b>1,208,865</b>

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### 5.2 Capital Risk management

The management of the Company's capital focuses on maintaining a solid financial structure that optimizes the cost of capital and the availability of financial resources to ensure the continuity of the business over the long term, in order to improve shareholder value while guaranteeing a solid credit profile.

The Company monitors its capital structure based on the net adjusted financial debt/EBITDA ratio. The Company considers as its adjusted net financial debt the nominal amounts of the non-current and current debt with related parties (Note 14) less cash and its equivalents. The Company defines EBITDA as profit before interest, taxes, depreciation and amortization, excluding other results, provision excess, indemnities (Note 18), banking and similar services and changes in provisions for commercial operations (Note 18).

	31/12/2019	31/12/2018
Operating Profit (loss)	113,708	110,612
Amortisation and depreciation	29,111	28,222
Banking services	223	238
Changes in provisions for commercial operations	17	829
Other results	1,704	746
Indemnities	1,312	1,123
Provision excess	-	111
Impairment and gains/(losses) on disposal of fixed assets	4	-
<b>EBITDA</b>	<b>146,079</b>	<b>141,881</b>
Other non-current liabilities	943,839	942,640
Payables to related parties	362	-
Financial liabilities	370	-
Payables to related parties	12,003	12,007
Non- current investment in group companies	(54,734)	-
Cash and cash equivalents	(103,426)	(63,042)
<b>Adjusted net financial debt</b>	<b>798,414</b>	<b>891,605</b>
<b>Adjusted net financial debt /EBITDA</b>	<b>5.47</b>	<b>6.28</b>

The Company initially applied IFRS 16 at 1 January 2019. In applying IFRS 16, in relation to the leases that were classified as operating leases, the Company recognises depreciation and interest costs, instead of operating lease expense. In relation to those leases, the Company recognised Euros 380 thousand of depreciation charges and Euros 29 thousand of additional interest costs from leases in 2019. The Company used the modified retrospective approach when initially applying IFRS 16. Under this approach comparative information is not restated.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

#### **6. Critical aspects of the valuation and estimation of uncertainty**

The preparation of the Financial Statements demands the use by the Company of certain estimations and judgments in relation with the future that are evaluated continuously and are based on the historical experience and other factors, including the expectations of future events that are considered reasonable under the circumstances.

The resulting accounting estimations, by definition, will rarely match the corresponding real results. The estimations and judgments that have a significant risk of proposing a material adjustment of the assets and liabilities' book value during the next financial year will be explained.

- Evaluation of the recoverability of intangible assets and goodwill to determine the existence of impairment losses.

The goodwill has an impairment test annually. The estimated recoverable amount has been determined from the discounted cash flows projected in the Company's business plan. Based on current knowledge, the Company considers that the changes envisaged in the key assumptions on which the determination of recoverable amounts does not imply that the net book value of the CGU exceeds the recoverable amounts. An analysis has been carried out whose sensitivity to reasonable changes in the key assumptions is estimated in each year without impairment on December 31<sup>st</sup> 2019 (see Note 7).

- Income taxes and recoverability of deferred tax assets

The calculation of the corporate income (expense) taxes requires the interpretation of fiscal regulations in force. The determination of expected outcomes regarding disputes and pending litigation requires the realization of significant estimates and judgments (Note 23). The Company assesses the recovery of deferred tax assets based on estimates of future taxable income and the ability to generate sufficient results during the periods in which such deferred taxes are deductible. Deferred tax liabilities are recorded in accordance with estimates made of net assets that in the future will not be tax deductible.

- Useful lives of tangible and intangible fixed assets

The accounting treatment of the investment in property, plant and equipment implies the preparation of estimates to determine the useful life of the same for the purposes of their amortisation as well as to determine the fair value at the acquisition date in the case of assets acquired in business combinations.

The determination of the useful lives requires estimates regarding the level of asset's utilization, as well as the expected technological evolution. Hypotheses regarding the level of utilization, technological framework and its future development implies a significant degree of judgment, to the extent that the timing and nature of future events are difficult to predict.

- Recognition of income and liquidation of regulated activities

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

The revenues derived from the remuneration established by the Ministry of the Ecological Transition and Demographic Challenge are recognized by the Company according to its publication in the relevant Ministerial Order. All other revenues are recognized when customer service has been performed. Historically, no material adjustments have been made to the amounts recorded as unbilled revenues and are not expected to be in the future.

- Estimation of right-of-use assets and lease liabilities (Note 3.5)

#### 7. Intangible assets

The breakdown and movement in the items included in this heading of the balance sheet is as follows:

	Thousand of euros					
	Goodwill	Administrative authorizations	Computer applications	Other intangible assets	Intangible assets in progress	Total
Book value at 31-12-2017	57,381	740,265	2,100	1,273	2,834	803,853
Additions	-	-	826	1,098	2,037	3,961
Depreciation charge	-	-	(932)	(261)	-	(1,193)
Cost	57,381	740,265	11,024	2,813	4,871	816,354
Accumulated amortisation	-	-	(9,030)	(703)	-	(9,733)
Book value at 31-12-2018	57,381	740,265	1,994	2,110	4,871	806,621
Additions	-	-	1,390	1,453	714	3,557
Other transfers	-	-	5,036	-	(5,036)	-
Depreciation charge	-	-	(1,628)	(201)	-	(1,829)
Cost	57,381	740,265	17,450	4,266	549	819,911
Accumulated amortisation	-	-	(10,658)	(904)	-	(11,562)
Book value at 31-12-2019	57,381	740,265	6,792	3,362	549	808,349

#### Commercial acquisition costs

At 31 December 2019 and 2018, Other intangible assets include incremental costs incurred directly to obtain contracts with clients and activated according to IFRS 15, for an amount of Euros 1,325 and 941, respectively.

The Goodwill comes from the merger through absorption between Madrileña Red de Gas, S.A.U. (merged company) and Madrileña Servicios Comunes, S.L.U. (merging company), on June 30<sup>th</sup> 2011 and the merger through absorption of Madrileña Red de Gas II, S.A.U. (merged company) and Nueva Madrileña de Gas, S.A.U. (merging company) on May 31<sup>st</sup>, 2012.

#### Impairment test for CGU containing goodwill

The core business of the Company is the gas distribution activity for which it receives an annual retribution granted by regulation. The recoverable amount for the CGU is determined on the basis of calculating its value in use.

These calculations are based on forecasted cash flows included in the business plan approved by the Board of Directors covering time period of 20 years included a terminal value.

The key assumptions to determine the value in use are as follow:

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

- Projection period: 20 years and remaining value
- Nominal growth rates: 0.5%, affecting only the residual value (0.5% in 2018)
- Discount rates after taxes: 5.02% (5,1% in 2018)

Apart from the discount rates, the most sensitive aspects that are included in the projections used and that are based on sector forecasts and historical experience are as follows:

- Revenue from remuneration.
- The amount and growth of the remuneration.
- Operational and maintenance costs.
- Investments.
- Conversion costs of the supply points of LPG to Gas.

Historically, the forecasted cash flows included in the business plan and the actual results have not significantly differed.

The estimated recoverable amount of the CGU exceeded its carrying. A decrease in the EBITDA of 1,5%, a decrease in the long term growth rate of 0.5%, or a rise in pre-tax discount rate by 1%, considering all changes in isolation, would not result in an impairment loss. Change required for carrying amount to equal recoverable amount is 8.74% Discount rate.

On December 31<sup>st</sup> 2019 and 2018, no goodwill or administrative authorizations impairment has been registered.

#### Additions

At December 31<sup>st</sup> 2019 and 2018, the most important additions are registered under the financial statement line "Computer applications" and licenses of computer applications in progress as consequences of the works being done for a algorithm's development that will allow the Company to optimize the lectures process and to reduce the percentage of losses in the distribution.

#### Other information

As of December 31<sup>st</sup> 2019, the Company has Euros 7,709 thousands of intangible assets fully amortised considering the accounting effects of mergers set out in Note 1 (December 31<sup>st</sup> 2018: Euros 6,828 thousands).

As of December 31<sup>st</sup> 2019 and 2018, the Company does not have any assets subject to reversion.

As of December 31<sup>st</sup> 2019 and 2018, the Company has no firm commitments to purchase intangible assets.



## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### 8. Property, plant and equipment

The breakdown and movement in the items included under this heading are as follows:

	Land and others	Technical installations	Transport equipment	Tooling	Furniture	Information processing equipment	Other fixed assets	Assets under construction	Total
Book value at 31-12-2017	144	358,214	503	255	121	201	784	12,869	373,091
Cost	144	586,625	719	565	227	855	1,065	12,869	603,069
Accumulated amortisation	-	(230,680)	(216)	(310)	(106)	(654)	(281)	-	(232,247)
Corrections of errors	-	12,193	-	-	-	-	-	-	12,193
Book value at 01-01-2018 restated	144	368,138	503	255	121	201	784	12,869	383,015
Additions	-	4,328	-	213	59	45	121	9,058	13,824
Disposals	-	-	(87)	-	-	-	-	(1,142)	(1,229)
Transfer	-	5,751	-	-	-	-	-	(5,751)	-
Depreciation charge	-	(26,610)	(111)	(65)	(25)	(157)	(61)	-	(27,029)
Depreciation disposals	-	-	38	-	-	-	-	-	38
Cost	144	608,897	632	778	286	900	1,186	15,034	627,857
Accumulated amortisation	-	(257,290)	(289)	(375)	(131)	(811)	(342)	-	(259,238)
Book value at 31-12-2018	144	351,607	343	403	155	89	844	15,034	368,619
Right-of-use assets IFRS 16	1,110	-	-	-	-	12	-	-	1,122
Additions	-	4,405	3	216	53	21	10	7,740	12,448
Disposals	-	-	(79)	-	-	-	-	(6)	(85)
Transfer	-	15,129	-	-	-	-	-	(15,129)	-
Depreciation charge	(380)	(26,571)	(99)	(92)	(29)	(46)	(65)	-	(27,282)
Depreciation disposals	-	-	40	-	-	-	-	-	40
Cost	1,254	628,431	556	994	339	933	1,196	7,639	641,342
Accumulated amortisation	(380)	(283,861)	(348)	(467)	(160)	(857)	(407)	-	(286,480)
Book value at 31-12-2019	874	344,570	208	527	179	76	789	7,639	354,862

Additions to property, plant and equipment in the fiscal year ended at December 31<sup>st</sup>, 2019 and December 31<sup>st</sup> 2018 relate mainly to investments in the natural gas pipeline network in the municipalities where the Company carries out its activity. At December 31<sup>st</sup> 2019 the Company provide services to 908,515 connection points (903,346 on December 31<sup>st</sup> 2018).

On June 9<sup>th</sup> 2016 a framework agreement was signed between Repsol Butano, S.A. and the Company for the purchase and transmission of LPG networks and installations for Euros 61 million, which consists in approximately 41 thousand points of supply, to the purpose of its progressive conversion to gas distribution assets, in accordance with the Company's layout. After the approval by the CNMC on July 21<sup>st</sup> 2016 the agreement for the transmission of LPG networks and installations were formalized. As of December 31<sup>st</sup> 2019, 17,734 LPG supply points converted to gas supply points. As of December 31<sup>st</sup> 2018, 16,448 LPG supply points have been converted to gas supply points.

As of December 31<sup>st</sup> 2019, property, plant and equipment includes fully amortized elements still in use considering the accounting effects of mergers set out in Note 1, amounting Euros 51,047 thousand (December 31<sup>st</sup> 2018: Euros 45,962 thousand).

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

It is the Company policy to take out insurance policies to cover risks relating to property, plant and equipment. The coverage provided by these policies is considered to be sufficient.

At December 31<sup>st</sup> 2019 and 2018, there is no commitments to purchase transport vehicles. There are investments to amplify and improves the network for an amount of 1,600 thousand euros (December 31<sup>st</sup> 2018: 1,600 thousand euros), and also for the construction of liquefied gas plants for an amount of 453 thousand euros (December 31<sup>st</sup> 2018: 453 thousand euros).

#### 8.1 Right-of-use assets and lease liabilities

The Company carries out its activity in offices leased from a third party. The lease contract is made up of fixed payments and a variable part referenced to the CPI and it has several renewal and cancellation options. The extension options held are exercisable only by the Company and not by the lessors. The Company assesses at lease commencement date whether it is reasonably certain to exercise the extension options. The Company reassesses whether it is reasonably certain to exercise the options if there is a significant event or significant changes in circumstances within its control. Additionally, the Company has long-term lease contracts for printers.

##### a) Right-of-use assets

	Plant	Printers	Total
Book value at 31-12-2018	-	-	-
Right-of-use on initial application of IFRS 16	1,110	12	1,122
Additions	-	-	-
Depreciation charge IFRS 16	(370)	(10)	(380)
Book value at 31-12-2019	740	2	742

##### b) Amounts recognized in profit and loss account

The detail of the amounts recorded in the income statement for the year 2019, related to the application of IFRS 16, is as follows:

	2019
Interest on lease liabilities	29
Amortisation	380
Total	409

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### c) Amounts recognized in statement of cash flows

The amount of payments made in 2019 related to leases is detailed below:

	2019
Lease payments	380
Interest paid on leases	29
Total	409

#### d) Future minimum lease payments

Committed future minimum lease payments are as follows:

	Thousand of Euros	
	31/12/2019	31/12/2018
Less than 1 year	39	219
Between 1 and 3 years	45	1,003
More than 3 years	9	-
Total	93	1,222

## 9. Financial instruments

The carrying value of each financial instrument category as set out in the accounting and measurement standard "Financial instruments" is as follows:

### 9.1 Analysis by category

#### a) Financial assets

	Thousand of Euros	
	Long-Term financial investments	
	At amortized cost	
	31/12/2019	31/12/2018
Loans to Group companies and associates	54,734	-
Other financial assets (Note 10)	1,006	1,854
Total	55,740	1,854
	Short-Term financial investments	
	At amortized cost	
	31/12/2019	31/12/2018
Trade and other receivables (Note 10) (*)	32,859	47,131
Cash and other equivalent liquid assets (Note 12)	103,426	63,042
Total	136,285	110,173

On June 19<sup>th</sup> 2019 the Company approved the extension of a loan to its direct parent, Elisandra Spain V, S.L., with a limit of Euros 1 billion, falling due in ten years, which accrues annual fixed interest of 6.04%. Euros 53 million was drawn down in 2019, which is repayable upon maturity.

# MADRILEÑA RED DE GAS, S.A.U.

## NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

### b) Financial liabilities

	Thousand of Euros			
	Long-term financial liabilities			
	Debts with credit institutions		Derivatives, Others	
	31/12/2019	31/12/2018	31/12/2019	31/12/2018
Trade and other payables (Note 14)	-	-	945,688	944,296
<b>Total</b>	<b>-</b>	<b>-</b>	<b>945,688</b>	<b>944,296</b>

	Thousand of Euros			
	Short-term financial liabilities			
	Debts with credit institutions		Derivatives, Others	
	31/12/2019	31/12/2018	31/12/2019	31/12/2018
Trade and other payables (Note 14)(*)	-	-	39,722	52,166
<b>Total</b>	<b>-</b>	<b>-</b>	<b>39,722</b>	<b>52,166</b>

(\*) Receivables and Liabilities with the Public Administrations have been excluded from the balance of loans and accounts receivable and loans and accounts payable.

### 9.2 Analysis by maturity date

On December 31<sup>st</sup> 2019 the long and short term debts with a determined or determinable maturity date, classified by the year in which they will mature, are as follows:

	2020	2021	2022	2023	Subsequent years	Total
Loans to group companies and associates	-	-	-	-	54,734	54,734
Gas system income deficit financing	3,600	-	-	-	-	3,600
Trade and other receivables	29,259	-	-	-	1,006	30,265
<b>Total</b>	<b>32,859</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>55,740</b>	<b>88,599</b>

  

	2020	2021	2022	2023	Subsequent years	Total
Trade payables to related parties	12,003	-	1,800	275,000	667,039	955,842
Trade and other payables	27,265	-	-	-	-	27,265
Other financial liabilities	454	574	204	204	867	2,303
<b>Total</b>	<b>39,722</b>	<b>574</b>	<b>2,004</b>	<b>275,204</b>	<b>667,906</b>	<b>985,410</b>

# MADRILEÑA RED DE GAS, S.A.U.

## NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

On December 31<sup>st</sup> 2018 the long-term debts with a determined or undetermined maturity date, classified by the year in which they will mature, are as follows:

	2019	2020	2021	2022	Subsequent years	Total
Gas system income deficit financing	19,248	234	234	234	257	20,207
Trade and other receivables	27,883	-	-	-	895	28,778
<b>Total</b>	<b>47,131</b>	<b>234</b>	<b>234</b>	<b>234</b>	<b>1,152</b>	<b>48,985</b>

  

	2019	2020	2021	2022	Subsequent years	Total
Trade payables to related parties	12,007	-	-	1,800	940,840	954,647
Trade and other payables	40,075	-	-	-	-	40,075
Other financial liabilities	84	204	204	204	1,044	1,740
<b>Total</b>	<b>52,166</b>	<b>204</b>	<b>204</b>	<b>2,004</b>	<b>941,884</b>	<b>996,462</b>

The fair value of the financial assets and liabilities is an amount of Euros 1,049,435 and 1,014,413 thousand at 31 December 2019 and 2018, respectively.

### 10. Trade and other receivables at amortized cost

The breakdown of this financial statement line as of December 31<sup>st</sup> 2019 and 2018 is as follows:

	Thousand of Euros	
	31/12/2019	31/12/2018
<b>Loans to Group companies and associates</b>		
Non-current investments in Group companies	54,734	-
	<b>54,734</b>	<b>-</b>
<b>Long-term financial investments</b>		
Gas system tariff deficit	-	959
Guarantee deposits	1,006	895
	<b>1,006</b>	<b>1,854</b>
<b>Short-term trade and other receivables</b>		
Trade receivables for sales and services	37,761	36,428
Provisions for bad debts	(8,659)	(8,642)
Debtors	3,600	19,248
Loans to employees	157	97
	<b>32,859</b>	<b>47,131</b>

### Gas system tariff deficit and sundry debtors

On December 31<sup>st</sup> 2019 and December 31<sup>st</sup> 2018, the item "Gas system tariff deficit" relates to mismatches between gas system revenues and costs accumulated by natural year 2017 being as follows:

	Thousand of Euros	
	31/12/2019	31/12/2018
<b>Long-term Gas System Deficit</b>		
Deficit generated in 2017	-	959
	<b>-</b>	<b>959</b>

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

These mismatches generates a recovery right, and in the next five years, plus interest at a market rate (once liquidity is obtained). The amount of this financing has been recognized in the financial statement line "Other non-current financial assets" the amount to be collected in the long term, and the amount of short term in "Debtors" based on the estimated recovery period through system settlements.

On October 10<sup>th</sup> 2018, the Company entered into an agreement with a banking entity to assign the nominal amount pending collection derived from the cumulative gas deficit for 2015 and 2016 and outstanding interest. By virtue of this agreement, the Company transferred the total credit recorded at that date for an amount of Euros 4,816 thousand. The Management of the Company, after analyzing the agreement, considers that all the risks related to this credit were substantially transferred and, consequently, the totally of the assigned credit was written off.

The breakdown of the financial statement line "Debtors" mainly collected between the deficit in 2017, 2018 and 2019, being as follows:

	Thousand Euros	
	31/12/2019	31/12/2018
<b>Sundry Debtors</b>		
Deficit / (Surplus) generated in 2017	46	240
Deficit / (Surplus) generated in 2018	-	19,030
Deficit / (Surplus) generated in 2019	3,584	-
Others debtors	(30)	(22)
	<b>3,600</b>	<b>19,248</b>

As of the date of preparation of these financial statements, the final assessments of the deficit of the year 2019 has not been received.

The Company registers in this financial statement line "Debtors" the deficit / (surplus), generated during the calendar year 2019, the amount of deficit accrued until the month of October.

#### Trade and rendering of services

As of December 31<sup>st</sup> 2019 and 2018, the amount included in the financial statement line "Trade receivables for sales and services" corresponds to the debtor balances by invoicing gas trading companies for the distribution activity in certain municipalities in the Autonomous Community of Madrid.

In general, the outstanding receivable toll invoices do not accrue interest, and the deadline for its payment by the supply companies is of 15 days after the invoice's emission date.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

According to the approved Resolution of July 17<sup>th</sup> 2015 by the "Dirección General de Política Energética y Minas", which establishes the valuation and liquidation of the amounts of measure differences on natural gas distribution networks from 2008 to 2012, and the communication of Enagás as of May 31<sup>st</sup> 2016 that published the amount of measure differences between distributors and trading during the period from July 1<sup>st</sup> 2008 to May 31<sup>st</sup> 2012 and during the period of 2014, corresponding to Madrileña Red de Gas, S.A.U. a net amount receivable of Euros 14,835 thousand, being the entire amount received as of totally in previous fiscal years. Similarly, the Company recognized a liability under "Suppliers" for the amount totally received (Euros 14,835 thousand on December 31<sup>st</sup> 2018) for the same concept.

According to the approved Resolution of April 23<sup>rd</sup>, 2018 by the "Dirección General de Política Energética y Minas" which establishes the valuation and liquidation of the amounts of measure differences on natural gas distribution networks from July 1<sup>st</sup>, 2012 to December 31<sup>st</sup>, 2013 was published the amount of measure differences between distribution and trading during the period of July 1<sup>st</sup>, 2012 and December 31<sup>st</sup>, 2013 corresponding to Madrileña Red de Gas S.A.U. a net amount payable of Euros 4,926 thousand being the entire amount paid as of totally in this fiscal year. On December 31<sup>st</sup> 2019 there are no amounts payable in this respect on the balance sheet.

On February 7<sup>th</sup> 2011 Gas Natural Fenosa (currently called Naturgy) signed with the Company a contract for the sale of distribution branch business in certain municipalities in Madrid, establishing the agreements to the assignments of the network division. On June 30<sup>th</sup>, 2011, an addendum was signed to this agreement, through which the pacts relating to the sectorization works contained in the aforementioned contract were established and new sectorization works were agreed. On December 31<sup>st</sup> 2018, the network division process has not yet been finalized, and until then, collections/payments for the measurement differences that are not assigned to the Company, although in October 2017, at the request of Naturgy discussions began related to the date from which the measurement differences would correspond to the Company, during 2019, a payment of Euros 7,877 thousand was made to Naturgy, and the Company has not recognised any additional amount in respect of such measurement differences on December 31<sup>st</sup> 2019.

The fair values of the loans and accounts receivable are the same as the net book values.

The movement in the insolvency provision for trade receivables are as follows:

	Thousand Euros	
	31/12/2019	31/12/2018
Opening balance	(8,642)	(7,813)
Charge to insolvency provision	(69)	(863)
Disposals	52	34
Closing balance	(8,659)	(8,642)

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### Long-term guarantees

The non-current guarantees do not have any specified maturity date.

#### 11. Inventory

As of December 31<sup>st</sup> 2019 and 2018 inventories correspond mainly to LPG and others materials of replacement distribution network.

As of December 31<sup>st</sup> 2019 there are no commitments to purchase or sell gas.

#### 12. Cash and cash equivalents

The breakdown of this financial statement line as of December 31<sup>st</sup> 2019 and 2018 is as follows:

	Thousand Euros	
	31/12/2019	31/12/2018
Cash and banks	103,426	63,042
	<u>103,426</u>	<u>63,042</u>

The treasury of the Company as of December 31<sup>st</sup> 2019 and 2018 is comprised mostly of checking accounts, with no availability limit and at market interest rate.

#### 13. Equity

The breakdown of this financial statement line as of December 31<sup>st</sup> 2019 and 2018 is as follows:

##### a) Share capital

	Thousand euros	
	31/12/2019	31/12/2018
Share capital	1,048	1,048
Total	<u>1,048</u>	<u>1,048</u>

On December 31<sup>st</sup> 2019 and 2018 the share capital was made up of 104,759 shares with a nominal value of Euros 10 each, fully subscribed by Elisandra V, S.L.U. (Note 1).

##### b) Share premium

On December 31<sup>st</sup> 2019 the share premium amounted to Euros 100,354 thousand (December 31<sup>st</sup>, 2018: Euros 100,354 thousand).

On July 21<sup>st</sup> 2015 the sole shareholder approved the distribution of a dividend charged to the issue premium reserve amounting to Euros 63,000 thousand, paid on July 29, 2015.



## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

In addition, on February 8<sup>th</sup> 2016 the sole shareholder approved another dividend charged to the share premium of Euros 25,000 thousand, whose disbursement occurred on March 1<sup>st</sup> 2016.

On October 20<sup>th</sup>, 2017 the sole shareholder approved the distribution of a dividend which was charged in the amounts of Euros 17,885 thousand to voluntary reserves, Euros 15,272 thousand to merger reserves and Euros 1,843 thousand to share premium reserves. As at December 31<sup>st</sup>, 2017, of this declared dividend, an amount totalling Euros 30,625 thousand has been disbursed with Euros 4,375 thousand (Note 14) whose disbursement occurred on this fiscal year.

On April 25<sup>th</sup>, 2018 the sole shareholder approved the distribution of a dividend which was charged in the amounts of Euros 116,000 thousand charged to the share premium that has been disbursement on 2018.

On November 28<sup>th</sup> 2018 the sole shareholder approved the distribution of dividend which was charged in the amounts of Euros 6,600 thousand charged to the share premium that has been disbursement on 2018.

On December 31<sup>st</sup> 2019 this reserve is freely available.

#### c) Reserves

	Thousand of Euros	
	31/12/2019	31/12/2018
<b>Legal and statutory:</b>		
- Legal reserve	210	210
<b>Other reserves:</b>		
- Voluntary reserves	116,442	65,437
- Merger reserves	-	-
- Goodwill reserves	15,734	15,734
- Actuarial reserves	(664)	(514)
<b>Total</b>	<b>131,722</b>	<b>80,867</b>

#### Voluntary reserves

On November 4<sup>th</sup> 2016 the Company's Sole Shareholder approved a dividend distribution with charge to voluntary reserves of Euros 94,800 thousand. Additionally, on October 20<sup>th</sup> 2017 the sole shareholder approved the distribution of a dividend which was charged in the amounts of Euros 17,885 thousand to voluntary reserves, Euros 15,272 thousand to merger reserves and Euros 1,843 thousand to share premium reserves. On December 31<sup>st</sup>, 2017, of this declared dividend, an amount totalling Euros 30,625 thousand was disbursed with Euros 4,375 thousand (Note 14) which has been disbursement during fiscal year 2018. The Company does not have limits for the dividends distribution others than the ones established in the article 273 of the Spanish Companies Act.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### Merger reserve

This is the result of the merger through absorption of Madrileña Servicios Comunes, S.L.U. and Madrileña Red de Gas, S.A.U. on June 30<sup>th</sup> 2011 in the amount of (Euros 5,861 thousand), and the merger through absorption between Madrileña Red de Gas, S.A.U. and Madrileña Red de Gas II, S.A.U. on September 24<sup>th</sup> 2013, in the amount of Euros 9,411 thousand. On October 20<sup>th</sup> 2017 the sole shareholder approved the distribution of a dividend which was charged in the amounts of Euros 17,885 thousand to voluntary reserves, Euros 15,272 thousand to merger reserves and Euros 1,843 thousand to share premium reserves. On December 31<sup>st</sup>, 2017, of this declared dividend, an amount totalling Euros 30,625 thousand has been disbursed with Euros 4,375 thousand, (Note 14) which has been disbursement during fiscal year 2018. On December 31<sup>st</sup> 2019 and 2018 the Company has not merger reserve.

#### Actuarial reserves

This corresponds to the actuarial profits and losses recorded directly against equity (Note 16.1).

#### Goodwill reserve

After the approval of the Royal Decree 602/2016 of December 2<sup>nd</sup>, in the years starting on January 1<sup>st</sup> 2016, the goodwill reserve will be re-classified to voluntary reserves and will be available starting on that date in the amount that exceeds the registered goodwill in the balance sheet's asset.

#### Proposed distribution of profit

The profit and reserves distribution proposal to be presented to the Sole Shareholders is as follows:

	Thousand of Euros	
	31/12/2019	31/12/2018
<b>Available for distribution</b>		
Profit for the year	64,961	51,005
<b>Application</b>		
To voluntary reserves	64,961	51,005
	64,961	51,005

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### 14. Financial liabilities, trade payables and other liabilities

The movement in this financial statement line is shown in the following table:

	Thousand Euros	
	31/12/2019	31/12/2018
<b>Long-term debts</b>		
Other financial liabilities-guarantees	1,849	1,656
Debts with group and associate companies (Note 20)	943,839	942,640
<b>Total</b>	<b>945,688</b>	<b>944,296</b>
<b>Short-term debt</b>		
Other financial liabilities	454	84
Trade Payables	11,318	21,769
Sundry payables	13,254	16,161
Accrued wages and salaries	2,693	2,145
Debts with group companies (Note 20)	12,003	12,007
	<b>39,722</b>	<b>52,166</b>
	<b>985,410</b>	<b>996,462</b>

#### Current and non-current payables to related parties:

The Company recorded under "Long-term payables to group companies and associates" the loans received during the fiscal year 2014 from the related company Madrileña Red de Gas Finance, BV (MRG Finance BV) and three new loans received during the fiscal years ended at June 30<sup>th</sup> 2016 and June 30<sup>th</sup> 2017 from the Sole Shareholder, Elisandra Spain V, S.L.U. through which it transferred to the Company the amounts obtained from the bond issues by MRG Finance, of which the Company is a guarantor:

- (i) Issue in September 2013 by MRG Finance BV, of bonds with a nominal amount of Euros 500,000 thousand and maturity in September 2018, under its EMTN programme secured by the Company. The amount of this issue was transferred to the Company under a financing agreement signed with MRG Finance BV. The bonds issued bear interest at a fixed rate of 3.799%, per year payable annually in September, and may be redeemed at maturity. On September 4<sup>th</sup> 2018 the Company amortized the loan who received by MRG Finance BV related to the emission repaid bond issue obligation for an amount of Euros 519,835 thousand (amount and interests).
- (ii) Issue in December 2013 by MRG Finance BV of bonds with a nominal amount of Euros 275,000 thousand maturing in December 2023, under its EMTN programme secured by the Company. The amount of this issue was transferred to the Company under a financing agreement signed with MRG Finance BV. The bonds issued bear interest at a fixed rate of 4.50% per year payable annually in December and may be redeemed at maturity.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

- (iii) Issue in March 2016 by MRG Finance BV of bonds with a nominal amount of Euros 75,000 thousand maturing in March 2031, under its EMTN programme secured by the Company. The amount of this issue was transferred to the Company under a financing agreement signed with Elisandra Spain V, S.L.U., Sole Shareholder of the Company, which it has signed a financing agreement with MRG Finance BV. The bonds issued bear interest at a fixed rate of 3.5% per year payable annually in March and may be redeemed at maturity.
- (iv) Issue in April 2017 by MRG Finance BV of bonds with a nominal amount of Euros 300,000 thousand maturing in April 2025, under its EMTN programme secured by the Company. The amount of this issue was transferred to the Company under a financing agreement signed with Elisandra Spain V, S.L.U., Sole Shareholder of the Company, which it has signed a financing agreement with MRG Finance BV. The bonds issued bear interest at a fixed rate of 1.375% per year payable annually in April and may be redeemed at maturity.
- (v) Issue in April 2017 by MRG Finance BV of bonds with a nominal amount of Euros 300,000 thousand maturing in April 2029, under its EMTN programme secured by the Company. The amount of this issue was transferred to the Company under a financing agreement signed with Elisandra Spain V, S.L.U., Sole Shareholder of the Company, which it has signed a financing agreement with MRG Finance BV. The bonds issued bear interest at a fixed rate of 2.25% per year payable annually in April and may be redeemed at maturity.

The main terms and conditions for these loans are as follows:

Notional amount of the loan	Start date	Maturity date	Term	Annual interest rate	Payment of interest	Repayment of principal
275,000	04.12.2013	04.12.2023	10 years	4.598%	Annual	04.12.2023
1,800	11.09.2013	11.09.2022	9 years	5.000%	Annual	11.09.2022
75,000	03.03.2016	03.03.2031	15 years	3.696%	Annual	03.03.2031
300,000	11.04.2017	11.04.2025	8 years	1.571%	Annual	11.04.2025
300,000	11.04.2017	11.04.2029	12 years	2.446%	Annual	11.04.2029
951,800						

#### Current payables to related parties

The Company recorded under "Short-term payables to group companies and associates" the outstanding interest payable on the loans mentioned in the previous section amounting to Euros 12,003 thousand (Euros 12,007 thousand on December 31<sup>st</sup>, 2018).

The financial expenses accrued on December 31<sup>st</sup>, 2019 amounts to Euros 28,752 thousand (Euros 42,520 thousand on December 31<sup>st</sup>, 2018).

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### Accounts payable and sundry payables

At December 31<sup>st</sup> 2019 and 2018 the Company has registered in the financial statement line "Accounts Payable" mainly the remaining balance to pay off the roadwork made on distribution network (Note 7). At the same time, on December 31<sup>st</sup> 2019 this mentioned financial statement line includes also an amount of Euros 1,308 thousand corresponding to a net amount payable due to the measuring differences, resulting from the amount payable explained in the Note 9 that corresponds to the other distribution companies (Euros 8,983 thousand on December 31<sup>st</sup>, 2018).

On the financial statement line "Sundry Payables" the Company includes, on December 31<sup>st</sup> 2019 and 2018 the provision resulting from the difference between the billing made on November and December, and the remuneration that truly corresponds to the settlements (Note 10).

#### Available credit lines

On December 31<sup>st</sup> 2019 and 2018 the Company has the following available credit lines of:

	Thousand of Euros	
	31/12/2019	31/12/2018
- Credit for general corporate purposes	200,000	200,000
	200,000	200,000

At December 31<sup>st</sup>, 2019 and 2018, the Company has not provided any credit lines.

#### Information on delays in payments to suppliers. Additional Provision 3 of "Duty to inform" of Law 15/2010, of July 5<sup>th</sup>.

The details of the required information regarding the average payment period to suppliers is as follows:

	31/12/2019 Days	31/12/2018 Days
Average payment period to suppliers (1)	61	66
Ratio paid transactions (2)	60	66
Ratio of outstanding payment transactions (3)	67	61

  

	Thousand of Euros	Thousand of Euros
Total payments made in the year	59,190	57,383
Total outstanding payments	4,830	5,112

(1) Calculation considering the amounts paid and payables at December 31, 2019 and 2018

(2) Average payment period in transactions paid during the year

(3) Average length of outstanding balance providers

# MADRILEÑA RED DE GAS, S.A.U.

## NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

Law 31/2014, of December 3<sup>rd</sup>, modified the law 15/2010 regarding the provision of information relating to a company's average payment period for suppliers. Subsequently, the ICAC Resolution of January 29<sup>th</sup> 2016 developed the methodology for the calculation of the average payment period to suppliers and the required disclosures in the notes to the financial statements. This resolution came into force on February 5<sup>th</sup> 2016 and applies to annual accounts from the year started on January 1<sup>st</sup> 2015.

### Reconciliation of movements of liabilities to cash flows arising from financing activities

	Liabilities		Share premium	Equity	Total
	Other loans and borrowings	Lease Liabilities		Reserves	
Restated balance at 1 January 2019	956,387	1,122	100,354	80,867	1,138,730
Proceeds from loans and borrowings	-	(380)	-	-	(380)
Total changes from financing cash flows	-	(380)	-	-	(380)
Changes arising from obtaining or losing control of subsidiaries or other businesses	-	-	-	-	-
The effect of changes in foreign exchange rates	-	-	-	-	-
Changes in fair value	-	-	-	-	-
Other changes	-	-	-	-	-
Liability-related	(176)	-	-	-	(176)
Interest expense	29,120	-	-	-	29,120
Interest paid	(27,928)	-	-	-	(27,928)
Total liability-related other changes	1,016	-	-	-	1,016
Total equity-related other changes	-	-	-	50,855	50,855
Balance at 31 December 2019	957,403	742	100,354	131,722	1,190,221

	Liabilities		Share premium	Equity	Total
	Other loans and borrowings	Lease Liabilities		Reserves	
Restated balance at 1 January 2018	1,465,369	-	222,954	64,298	1,752,621
Proceeds from loans and borrowings	(500,000)	-	-	-	(500,000)
Dividends paid	-	-	(126,975)	-	(126,975)
Total changes from financing cash flows	(500,000)	-	(126,975)	-	(626,975)
Changes arising from obtaining or losing control of subsidiaries or other businesses	-	-	-	-	-
The effect of changes in foreign exchange rates	-	-	-	-	-
Changes in fair value	-	-	-	-	-
Other changes	-	-	-	-	-
Liability-related	(4,522)	-	-	-	(4,522)
Interest expense	42,896	-	-	-	42,896
Interest paid	(47,356)	-	-	-	(47,356)
Total liability-related other changes	(8,982)	-	-	-	(8,982)
Total equity-related other changes	-	-	4,375	16,569	20,944
Balance at 31 December 2018	956,387	-	100,354	80,867	1,137,608

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### 15. Deferred income

The breakdown of the "Deferred income" includes collections for the distribution network. The movement in this category is shown in the following table:

	Thousand of Euros	
	31/12/2019	31/12/2018
Opening balance	28,720	28,015
Additions	4,357	2,781
Disposals	(2,185)	(2,076)
Closing balance	30,892	28,720

#### 16. Provisions

The breakdown of provisions is as follows:

	Thousand Euros	
	31/12/2019	31/12/2018
Provisions for personnel expenses	1,440	1,333
Other Provisions for personnel expenses	1,224	615
Decommissioning provisions	2,097	3,328
Non-current provisions	4,761	5,276

  

	Thousand Euros	
	31/12/2019	31/12/2018
Decommissioning provisions	1,705	2,336
Short-term provisions	1,705	2,336

##### 16.1 Employee benefit obligations

The total provisions amount on December 31<sup>st</sup> 2019 and 2018 corresponds to commitments for bonuses to the natural gas consumption and health insurance for current personal from Gas Natural Fenosa (currently Naturgy), during post-retirement period.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

The movement in the liability recorded in the balance sheet for actuarial obligations is as follows:

	Thousand Euros	
	31/12/2019	31/12/2018
Opening balance	1,333	1,476
Cost of service in financial year	54	48
Cost of interests	10	28
Actuarial gains and losses (recorded in equity)	150	(69)
Benefits paid	(12)	(10)
Disposals	(95)	(140)
Closing Balance	1,440	1,333

The actuarial assumptions used to value the gas credit commitments are as follows:

	31/12/2019	31/12/2018
Technical discount rate	0.69%	2.12%
Cost increase (annual)	1.50%	1.50%
Inflation rate (annual)	1.50%	1.50%
Mortality table	Table INE	Table INE

#### 16.2 Decommissioning provisions

After the acquisition of LPG assets, the Company's Management has evaluated the necessary costs for the LPG plants' dismantling that will not be utilized once the process of converting the LPG points finishes. In this sense and according to the best estimate the Company has made, it has been registered in the long-term an amount of Euros 2,097 thousand and in the short-term an amount of Euros 1,705 thousand (Euros 3,328 thousand in the long-term and Euros 2,336 thousand in the short-term at December 31<sup>st</sup> 2018, respectively).

#### 17. Tax situation

From July 1<sup>st</sup> 2015 the Company began to file consolidated tax returns as a subsidiary of Tax Group No. 474/15, parented by Elisandra Spain IV, S.L.

The Tax Consolidated Group No. 474/15 is formed by the parent Elisandra Spain IV, S.L. and the companies Elisandra Spain V, S.L.U, Aliara Energía, S.L.U. y Madrileña Red de Gas S.L.U.



**MADRILEÑA RED DE GAS, S.A.U.****NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED  
ON DECEMBER 31<sup>st</sup> 2019  
(Expressed in thousand of euros)**

Set out below is the reconciliation between net income and expense for the year ended at December 31<sup>st</sup> 2019 and corporate tax base:

Thousand of Euros						
	Income statement			Income and expenses recognized in equity		
	Additions	Disposals	Total	Additions	Disposals	Total
Profit (loss) for the year			64,961			(150)
Corporate income tax	21,400	-	21,400	-	-	-
Permanent differences	-	(6)	(6)	-	-	-
Temporary differences	3,413	(59,272)	(55,859)	-	-	-
Tax base			30,496			(150)

Set out below is the reconciliation between net income and expense for the year ended on December 31<sup>st</sup> 2018 and corporate tax base:

Thousand of Euros						
	Income statement			Income and expenses recognized in equity		
	Additions	Disposals	Total	Additions	Disposals	Total
Profit (loss) for the year			51,005			69
Corporate income tax	16,744	-	16,744	-	-	-
Permanent differences	-	58	58	-	-	-
Temporary differences	1,437	(43,673)	(42,236)	-	-	-
Tax base			25,571			69

On March 31<sup>st</sup> 2012 the Official State Gazette published Royal Decree-Law 12/2012 (March 30), which was subsequently amended by Royal Decree-Law 20/2012 (July 12), introducing several tax and administrative measures to reduce the public deficit. This Royal Decree-Law establishes a general limit to the deduction of financial expense. In general, the amount of net deductible financial expense in the tax period is reduced to 30% of operating profits for the year (applying certain corrections) and, in any event, financial expense not exceeding Euros 1 million are deductible. These limitations will apply to the tax periods commencing as from January 1<sup>st</sup> 2012.

Article 7 of Law 16/2012 (of December 27<sup>th</sup>), which adopts several tax measures to consolidate public finances and encourage economic activities, introduces a temporary limitation in 2013 and 2014 affecting tax deductible amortisation and only 70% of the amortisation recognised by companies that do not comply with the requirements of Article 108 of the Spanish Corporate Income Tax Act, which regulates the requirements for the small company classification, may be deducted.

**MADRILEÑA RED DE GAS, S.A.U.**

**NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED  
ON DECEMBER 31<sup>st</sup> 2019  
(Expressed in thousand of euros)**

On December 31<sup>st</sup> 2019 the disposals of temporary differences mainly include the reversal of Euros 2,030 thousand (December 31<sup>st</sup> 2018: Euros 2,949 thousand) due to the limitation on the amortization of PP&E, the tax depreciation of administrative authorisations in an amount of Euros 37,040 thousand (December 31<sup>st</sup> 2018: Euros 37,040 thousand), the tax amortisation of goodwill in an amount of Euros 2,869 thousand (December 31<sup>st</sup> 2018: Euros 2,869 thousand), and Euros 13,895 thousand due to non-deductible financial expenses (December 31<sup>st</sup> 2018: Euros 0). The additions of temporary differences include Euros 1,309 thousand (December 31, 2018: Euros 865 thousand) due to the personnel liabilities, and Euros 439 thousand (December 31<sup>st</sup> 2018: Euros 439 thousand) for the difference between tax and accounting amortisation, according to Royal Decree 3/93.

At December 31<sup>st</sup> 2019 the Company had made interim corporate income tax payments totalling Euros 5,442 thousand (December 31<sup>st</sup> 2018: Euros 5,483 thousand).

Corporate income tax expense is analysed below:

	Thousand of Euros	
	31/12/2019	31/12/2018
Current tax	(8,135)	(5,834)
Deferred tax	(13,265)	(10,910)
	<u>(21,400)</u>	<u>(16,744)</u>

The current corporate tax results from the application of the 25% to the tax base. At December 31<sup>st</sup>, 2019, it is also included tax differences adjustments from prior tax years by the amount of Euros 605 thousand (Euros 465 thousand at December 31<sup>st</sup> 2018 as an increasing expense) and adjustments for deductions for an amount of Euros 94 thousand as a decreasing expense (Euros 94 thousand as a decreasing expense at December 31<sup>st</sup> 2018).

# MADRILEÑA RED DE GAS, S.A.U.

## NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

### Deferred tax assets and liabilities

Movements during the year in deferred tax assets and liabilities, without taking into account the offset of balances, were as follows:

Deferred tax assets	Provisions	Financial expenses	Merger fixed asset	Asset amortisation	Insolvency provisions and others	Total
Balance at 31/12/2017	1,355	19,166	2,738	3,965	55	27,279
Charged/(credited) to profit or loss	(194)	-	(297)	(529)	(22)	(1,042)
Other	-	(1,305)	-	-	-	(1,305)
Balance at 31/12/2018	1,161	17,861	2,441	3,436	33	24,932
Charged/(credited) to profit or loss	281	(3,474)	(67)	(122)	(17)	(3,399)
Other	-	-	-	-	-	-
Balance at 31/12/2019	1,442	14,387	2,374	3,314	16	21,533

Deferred tax liabilities	Tax amortisation RD3/93	Tax amortisation Administrative concessions	Tax amortisation goodwill	Total
Balance at 31/12/2017	(446)	(37,874)	(2,047)	(40,367)
Charged/(credited) to profit or loss	110	(9,260)	(718)	(9,868)
Other	-	(2)	-	(2)
Balance at 31/12/2018	(336)	(47,136)	(2,765)	(50,237)
Charged/(credited) to profit or loss	110	(9,253)	(723)	(9,866)
Other	-	-	-	-
Balance at 31/12/2019	(226)	(56,389)	(3,488)	(60,103)

The deferred tax assets arising from tax loss carry forwards available to offset are recognised as it becomes likely that the Company will obtain future tax profits to offset them. At December 31<sup>st</sup> 2019 and 2018 the Company records no tax bases pending to offset.

Management has recognised deferred tax assets with a recovery period of ten years as profit is reasonably stable and, therefore, there is no doubt regarding their recoverability. At the date of the financial statements formulation, it is open the process of inspection for the last 4 years of the main taxes (VAT, Personal Income Tax and Corporate Tax).

The Company is under one process of inspection in relation to VAT and Corporate Tax to the financial years 2010 and 2011, and financial years 2012 and 2013 respectively, as well as the VAT for the years 2011 (July to December, both included), 2012 and 2013, which ended with the corresponding settlement agreements, which were challenged before the competent Economic-Administrative Court, currently pending resolution (Note 23).

In accordance with current legislation, tax returns cannot be deemed definitive until they are verified by the tax authorities or until they pass their statute of limitation. The Company has not yet submitted the declaration of corporate income tax for the year ended on December 31<sup>st</sup> 2019, although in its calculation are taken into consideration the various legislative provisions apply.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

As a result, among other things, of the different interpretations the fiscal legislation may have, as well as the results of the inspections that could happen in the verification years, it may arise additional liabilities with contingent character for the Company, that are not susceptible to objective quantification. The Company's Directors do not expect additional liabilities to arise as a consequence of the said resources nor the inspection of the outstanding fiscal years (Note 23).

The amount included under "Other receivables/payables to Public Administrations" breaks down as follows:

	Thousand euros	
	31/12/2019	31/12/2018
<b>Debit balances</b>		
VAT receivable	919	-
Tax receivable for other items (Note 23)	5,359	5,359
<b>Total debt balances</b>	<b>6,278</b>	<b>5,359</b>
<b>Credit balances</b>		
VAT payable	-	72
Current tax	2,090	907
Other payable for withholdings made	-	(1)
Other debts with Public Administrations	2,997	3,452
Social Security payables	163	148
<b>Total credit balances</b>	<b>5,250</b>	<b>4,578</b>

The amount included in "Other debts with Public Administrations" relates to the credit balances with Councils for public land occupancy tax.

## 18. Income and expense

### a) Revenue

	Thousand of Euros	
	31/12/2019	31/12/2018
<b>Revenue</b>		
Remuneration (Note 2)	149,590	146,958
Other non-regulated income	4,165	4,296
Other non-regulated income by indemnities	188	153
Other regulated income	18,262	16,526
Non regulated LPG income (Note 2)	43	59
LPG income (Note 2)	11,898	18,286
<b>Total</b>	<b>184,146</b>	<b>186,278</b>

The entirety of the Company's revenues relate to activities carried out in the Region of Madrid.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### Other regulated income

Other regulated income corresponds to services related to natural gas distribution activity, where its prices are determined in the regulation. These services include the renting of gas meters, periodic inspections and network services.

#### Other non-regulated income

Other non-regulated income is also for services relating to the natural gas distribution activity, where its prices are not regulated, such as services like the operations realized in the final user's home and other auxiliary services.

Timing of revenue recognition	Thousand of Euros	
	31/12/2019	31/12/2018
Services transferred at a point in time	160,152	155,172
Services transferred over time	23,994	31,106
Revenue from contracts with customers	184,146	186,278

#### b) Raw materials and consumables

The breakdown of the Raw materials and consumables caption at the end of the financial year is as follows:

Consumption of goods	Thousand of Euros	
	31/12/2019	31/12/2018
Other	(10,375)	(16,820)
Variation in inventories	81	857
Impairment of merchandise, raw materials and other supplies	-	(111)
<b>Total</b>	<b>(10,294)</b>	<b>(16,074)</b>

#### c) Personnel expenses

	Thousand of Euros	
	31/12/2019	31/12/2018
Wages, salaries and similar	(8,190)	(8,061)
Social charges:		
- Contributions and allocations for pensions	(78)	(89)
- Other social charges	(2,375)	(2,395)
Indemnities	(1,312)	(1,123)
<b>Total</b>	<b>(11,955)</b>	<b>(11,668)</b>

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

The number of employees by professional category and gender on December 31, 2019 by category is as follows:

	Male	Female
Senior Managements / Managers	13	8
Administrative	7	10
Business development	18	10
Operations	66	11
	<b>104</b>	<b>39</b>

The number of employees by professional category and gender at the end of the year ended on December 31<sup>th</sup> 2018 by category was as follows:

	Male	Female
Senior Managements / Managers	15	6
Administrative	7	8
Business development	22	9
Operations	70	13
	<b>114</b>	<b>36</b>

The average number of employees' professional category and gender of the Company in the fiscal year ended on December 31<sup>st</sup> 2019 is as follow:

	Male	Female
Senior Managements / Managers	14	8
Administrative	7	9
Business development	20	10
Operations	68	12
	<b>109</b>	<b>39</b>

The average number of employees by professional category and gender of the Company in the year ended on December 31<sup>th</sup> 2018 was as follow:

	Male	Female
Senior Managements / Managers	15	6
Administrative	8	8
Business development	23	9
Operations	76	11
	<b>122</b>	<b>34</b>

During the fiscal years ended on December 31<sup>st</sup> 2019 and 2018 no employees with a disability higher or equal to 33% have been hired.

**MADRILEÑA RED DE GAS, S.A.U.**

**NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED  
ON DECEMBER 31<sup>st</sup> 2019  
(Expressed in thousand of euros)**

**d) Other operating expenses**

	Thousand of Euros	
	31/12/2019	31/12/2018
<b>Operating expenses</b>		
Leases and royalties	(49)	(453)
Repairs and maintenance	(3,034)	(3,267)
Professional services	(1,204)	(1,299)
Insurance	(367)	(357)
Bank services and similar	(223)	(238)
Publicity	(15)	(22)
Supplies	(445)	(479)
Taxes	(4,113)	(4,130)
Losses, impairment and changes in provisions for commercial operations	(17)	(829)
Other operating expenses	52	28
Other expenses	(8,382)	(8,024)
Other services	(2,817)	(2,866)
<b>Total</b>	<b>(20,614)</b>	<b>(21,936)</b>

"Other expenses" line largely relates to expenses accruing in the financial year due to the reading of meters carried out by external parties, management services for the billing and charging and other items related to the overall operation of the Company.

**e) Other results**

	Thousand Euros	
	31/12/2019	31/12/2018
<b>Other results</b>		
Other non-recurring expenses	(1,704)	(746)
<b>Total</b>	<b>(1,704)</b>	<b>(746)</b>

On December 31<sup>st</sup> 2019 and 2018 the financial statement line "Other results" includes expenses for professional services received corporate projects of an exceptional nature and for a significant amount.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

#### f) Financial expenses

	Thousand of Euros	
	31/12/2019	31/12/2018
<b>Financial income:</b>		
Marketable securities and other financial instruments		
- Third parties	40	33
- Current loans to Group companies and associates	1,733	-
	<u>1,773</u>	<u>33</u>
<b>Financial expenses</b>		
Interest on debts with group companies (Note 14 and 20)	(28,752)	(42,520)
Interest on debts with third parties	(368)	(376)
	<u>(29,120)</u>	<u>(42,896)</u>
<b>Financial results</b>	<u>(27,347)</u>	<u>(42,863)</u>

#### 19. Remuneration of the Board of Directors and Management

In the years ended on December 31<sup>st</sup> 2019 and 2018 the members of the Board of Directors have not received remuneration in the form of salaries or other remunerations. In addition, they have not been granted loans or advances, rights relating to pensions or life insurance or others of a similar nature at the Company's expense.

The Company considers senior management staff understood "Senior Management ", not only those cases where there are employment contracts of senior management but also those people who exercise functions related to the general objectives of the Company, such as planning, management and control activities, performing its functions independently and with full responsibility, limited only by higher bodies that represent them.

The total remuneration accrued during the fiscal year ended on December 31<sup>st</sup>, 2019 by senior management amounts to Euros 2,707 thousands (Euros 2,677 thousand on December 31<sup>st</sup> 2018), of which Euros 2,601 thousand (Euros 2,570 thousand in December 31<sup>st</sup>, 2018) relates to total amount of remuneration, Euros 0 (Euros 5 thousand on 31<sup>st</sup>, December 2018) relates to indemnities, Euros 96 thousand (Euros 91 thousand on December 31<sup>st</sup>, 2018) corresponds to contributions to pension fund and Euros 10 thousand (Euros 11 thousand on December 31<sup>st</sup>, 2018) ) corresponds to the amount accrued in senior management life insurance. On December 31<sup>st</sup> 2019 and 2018 the Company did not granted any loans to senior management.

During the 2019 and 2018 financial years the Administrators have not received, nor have they granted advances or credits, no obligations have been assumed on their behalf as a guarantee and have civil liability insurance premiums been paid for damages caused by acts or omissions in the exercise of office by amount to Euros 19 thousand (Euros 19 thousand on December 31<sup>st</sup>, 2018).

On April 30th, 2018, the assignment of Mr. Guillaume D'Engremont and Mr. Jérôme Sousselier were revoked and on June 5th 2018 the new directors assigned are Mr. Maxime Nekoian and Mr. Pierre Alexandre Marie Benoist-d'Anthenay.



## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

On July 23rd, 2018 the assignment of Mr. Maxime Nekoian was revoked and the new director assigned is Mrs. Fanny Marie Colette Grillo.

On March 22nd, 2019, the assignment of Mr. Michael Andrew Bryan and Mrs. Rong Yan were revoked and the new directors assigned are Mr. Dong Dong and Mr. Andrew Wilkie.

#### Director's conflict of interest

As regards the duty to avoid conflicts of interest with the Company, during the year the Board of Directors fulfilled the obligations stipulated in Article 228 of the Spanish Companies Act. Both the Directors and their related parties avoided the conflict of interest scenarios envisaged in Article 229 of the Act, except for cases in which the necessary authorisation was obtained.

#### 20. Related-party transactions

Related parties are as follows:

- The Sole Shareholder of Madrileña Red de Gas, S.A.U., Elisandra V, S.L.U. and the ultimate parent company Elisandra IV, S.L., and its significant shareholders Realgaz, S.A.S, Stichting Depositary PGGM Infrastructure Funds, JCSS Mike S.A.R.L and LPPI Infrastructure Investments LP.
- Directors and executives of the company, and their immediate families. The term "director" means a member of the Board of Directors; "executive" means a member of the Senior Management of Madrileña Red de Gas, S.A.U.
- Companies of Madrileña Red de Gas, S.A.U., Elisandra Spain IV, S.L., Elisandra Spain V, S.L.U., Aliara Energía, S.L.U., and Madrileña Red de Gas Finance B.V.

#### a) Balances with related parties

	Thousand of Euros		
	Group companies	Other related parties	TOTAL
<b>31/12/2019</b>			
Current loans to Group companies and associates	54,734	-	54,734
Long-term debts with group and associate companies (Note 14)	(943,839)	-	(943,839)
Short-term debts with group and associate companies (Note 14)	(12,003)	-	(12,003)

**MADRILEÑA RED DE GAS, S.A.U.****NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED  
ON DECEMBER 31<sup>st</sup> 2019  
(Expressed in thousand of euros)**

	Thousand of Euros		
	Group companies	Other related parties	TOTAL
<b>31/12/2018</b>			
Long-term debts with group and associate companies (Note 14)	(942,640)	-	(942,640)
Short-term debts with group and associate companies (Note 14)	(12,007)	-	(12,007)

At the year ended on December 31<sup>st</sup> 2019 the Company recorded under "Long-term and short-term payables to group companies and associates" loans from the related company Madrileña Red de Gas Finance BV and its Sole Shareholder Elisandra Spain V, S.L.U. in the amount of Euros 955,842 thousand (Euros 954,647 thousand on December 31<sup>st</sup> 2018) where the loans conditions are described in the Note 14.

**b) Transactions with related parties**

	Thousand of Euros		
	Group companies	Other related parties	TOTAL
<b>31/12/2019</b>			
<u>INCOME</u>			
Office renting and other complementary services	35	-	35
Interest income	1,733	-	1,733
<u>EXPENSES</u>			
Interest expenses (Note 18)	(28,752)	-	(28,752)
Others	(126)	(175)	(301)

At 31 December 2018, the Company sold three natural gas fuelling stations to Group company Aliara Energía, S.A.U. The stations were built by a third party and sold for their carrying amount of Euros 1,136 thousand (Nota 6).

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

The remuneration accrued by senior management in 2019 is set out in Note 19.

31/12/2018	Thousand of Euros		
	Group companies	Other related parties	TOTAL
<u>INCOME</u>			
Services rendered	9	-	9
<u>EXPENSES</u>			
Interest expenses (Note 18)	(42,520)	-	(42,520)
Others	(129)	(175)	(304)

On December 31<sup>st</sup> 2019 Consilia Asesores S.L., which holds the presidency of the Board of Directors represented by Pedro Mielgo, has received 175 thousand euros (December 31<sup>st</sup> 2018: 175 thousand euros) for advising and consulting regarding the signed contract.

All the transactions realized between group companies were carried out at market price.

#### 21. Auditors' fees

The fees charged on December 31<sup>st</sup> 2019 financial year by KPMG Auditores, S.L. for auditing the annual accounts and other related limited reviews and audits works were Euros 26.5 thousand (December 31<sup>st</sup> 2018: Euros 71 thousand by PricewaterhouseCoopers Auditores, S.L). On December 31<sup>st</sup> 2019 and 2018 has not been earned by fees charged for other audit related services.

Similarly, the fees accruing at December 31<sup>st</sup> 2019 calendar year for other companies using the KPMG Auditores, S.L brand as a result of other services provided to the Company were Euros 0 (December 31<sup>st</sup> 2018: Euros 409 thousand using PricewaterhouseCoopers brand).

#### 22. Environmental information

The Company has not received any subsidies or income as a result of activities related to the environment. The Company has no assets related to the environment and has incurred expenses to comply with and adapt to current legislation and regulations, as well as to the maintenance of the environmental management.

## MADRILEÑA RED DE GAS, S.A.U.

### NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)

On August 27<sup>th</sup> 2004 Royal Decree Law 5/2004 was passed which governs the system of trading emission rights of greenhouse gases, with the purpose of assisting to comply with the obligations deriving from the Kyoto Convention and Protocol. Due to the nature of its activities the Company does not have allocations of CO2 emissions nor expenses deriving from the consumption of emission rights. The Management of the Company does not anticipate any type of penalty or contingency deriving from compliance with the requirements laid down in Act 1/2005.

#### **23. Other Commitments and contingencies**

##### Commitments

As of December 31<sup>st</sup> 2019 there is a total of Euros 38,982 thousand guaranteed (December 31<sup>st</sup> 2018: Euros 38,480 thousand) by different bank entities. Of the aforementioned total amount; Euros 5,338 thousand are guaranteed by different banks entities against local city councils for work carried out in the municipalities in which the Company operates; and Euros 33,644 thousand guaranteed by different banks entities against tax authorities for the open inspections of 2012-2013. The Company's Directors estimates that given the nature of the guarantees, it does not exist any risk that originates no preview liabilities.

##### Contingencies

As a result of the tax inspections which commenced in the year 2015 over the 2010 and 2011 tax, on February 17<sup>th</sup> 2016 the Company was notified of the settlement agreement for corporate income tax relating to 2010, which resulted in tax payable totalling Euros 5,488 thousand, paid by the Company on April 5<sup>th</sup> 2016, largely due to the inspector's approach to the deductibility of certain expenses, facts that have not arisen any sanction. Additionally, on February 29<sup>th</sup> 2016 the Company was notified about the corporate income tax settlement agreement for 2011 and as explained above, although it resulted in an adjustment to the accounting result which reduced the Company's losses by Euros 1,752 thousand, it resulted in zero tax payable. Both assessments were contested.

On March 15<sup>th</sup> 2016 the Company filed two economic-administrative claims against the Settlement Agreements to the Central Economic and Administrative Tribunal (TEAC), requesting its accumulation for both claims to be processed jointly and in a single procedure, where the TEAC has answer on October 5<sup>th</sup>, 2016 with a notification accepting the request, as well as the disclosure of both files with a period of one month to review and to formulate the corresponding allegations. At November 4<sup>th</sup>, 2016, the Company presented to the TEAC the allegations showing the two economic-administrative claims against the Settlement Agreements, which at the financial statements formulation date, have not received any answer.

In case that the claims do not succeed, the greater risk for the Company amount Euros 8,024 thousand in instalments, plus Euros 929 thousand as default interest up to the present date.

**MADRILEÑA RED DE GAS, S.A.U.**

**NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED  
ON DECEMBER 31<sup>st</sup> 2019  
(Expressed in thousand of euros)**

According to the legal advisor's opinion, at December 31<sup>st</sup> 2019, the Company's Directors consider that there are high probabilities of succeeding in the economic-administrative claims. As a result, at December 31<sup>st</sup> 2019, the Company's Management has considered not necessary to register any expense regarding the amount claimed and to maintain account receivable with the Public Administrations for the amount referred before (Euros 5,359 thousand) in the financial statement line "(Public Administration – other credits)", as well as in the previous calendar year.

Additionally, on March 15<sup>th</sup> 2016, April 22<sup>nd</sup> 2016 and May 25<sup>th</sup> 2016, the tax authorities informed the Company of the initiation of a corporate tax review for the fiscal years ended in 2012 and 2013, and a VAT review for the second semester of 2011, and for the years 2012 and 2013.

As a result of such inspections, on July 17<sup>th</sup> 2017 the tax authorities issued provisional assessments resulting in a proposal for tax payable of Euros 28,008 thousand in respect of corporate income tax plus late-payment interest of Euros 5,036 thousand, on the understanding that the expenses relating mainly to the tax amortization of the administrative concessions, increase in the value of assets and goodwill, among others, are not deductible in those years as they do not yet meet the requirements to be tax deductible. The assessments raised include no penalty in respect of the tax in question and Euros 122 thousand for VAT as a consequence of the inspection criteria on the deductibility of certain expenses plus late-payment interest of Euros 24 thousand. The Company signed both tax assessments in disagreement and has made allegations about those records.

On January 16<sup>th</sup>, 2018, the Company was notified of the definitive settlement agreement corresponding to the Value Added Tax, which confirms the content of the provisional assessments, in accordance with the previous paragraph, for an amount of Euros 122 thousand in instalments and Euros 26 thousand for late-payment interest and have been paid on 1<sup>st</sup> 2018, by the Company.

On March 8<sup>th</sup>, 2018, the Company has been notified of the definitive settlement agreement corresponding to the Corporate Income Tax, which confirms the content of the provisional assessments, in accordance with the previous paragraph, for an amount of Euros 28,022 thousand in instalments and Euros 5,622 thousand for late-payment interest.

On September 28<sup>th</sup> 2019, the Company has submitted to TEAC the statement of allegations of the economic-administrative claims brought against the Settlement Agreements relating to corporation tax for the fiscal years 2012 and 2013, on which no response has yet been received at the date of the formulation of these financial statements.

On December 4<sup>th</sup> 2019, the Company has submitted to the TEAR the statement of allegations of the economic-administrative claims brought against the Settlement Agreements relating to Value Added Tax in the fiscal years 2012 and 2013, on which no response has yet been received at the date of the formulation of these financial statements.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **NOTES TO THE FINANCIAL STATEMENTS CORRESPONDING TO THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2019 (Expressed in thousand of euros)**

In case of future allegations do not succeed, the greater impact for the Company for the two years that were reviewed (2012 and 2013) will be an expense of Euros 16,280 thousand as a greater corporate tax quota, and a default interest expense of Euros 7,560 thousand corresponding to corporate income tax until the date of notification of the settlement agreement and a lower deferred tax asset by Euros 5,219 thousand and a lower deferred tax liability of Euros 16,714 thousand, although the right to deduct the costs at issue corresponding to the tax amortization of administrative concessions, increased asset value and goodwill remains to the extent that the conditions referred to in the minutes having not opened inspections at the current date of years.

At the financial statements formulation date and for the next fiscal years, some of the circumstances questioned in the inspections would remain in force.

Having realised the allegations of the claims filed, and according to the Company's legal advisor's opinion, at the time the annual accounts were drafted, the Company considers that it has solid arguments to defend its position in relation the deductibility of such expenses, and as a result, at December 31<sup>st</sup> 2019, the Company's Management considers it reasonable to not recognise any expense or assets relating to the amounts claimed.

#### **24. Subsequent events**

On January 20<sup>th</sup> 2020 the taxation authorities notified the Company of the commencement of an inspection of income tax for the fiscal year ended in 2015. At the date on which the annual accounts were authorised for issue, Company management considered it reasonable not to record any expense in this regard.

On March 9<sup>th</sup>, 2020 the Company reduced the amount of the credit facility by Euros 125,000 thousand, and the amount available is Euros 75,000 thousand (note 5).

On March 18<sup>th</sup>, 2020 the assignment of Mr. Ruwantha Vidanaarachchi was revoked and the new director assigned is Mr. Qingtong Li.

On March 18<sup>th</sup>, 2020 Euros 103,000 thousand had been drawn down on the credit facility signed with its direct parent, Elisandra Spain V, S.L., which was approved by the Company in June 2019 (note 8.1).

The Company has performed a risk analysis of the crisis brought about by COVID-19 and with the information available at present no significant risk is foreseen that could compromise the Company's ability to continue as a going concern in the next 12 months.

There have been no other significant events subsequent to year-end and to the date of preparation of these consolidated financial statements that the Group considers could significantly affect them.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **DIRECTORS REPORT FOR THE YEAR ENDED ON 31 DECEMBER 2019 (Expressed in thousand of euros)**

#### **COMPANY'S ORIGIN**

In their resolution of 11 February 2009, the Spanish National Competition Authorities (Comisión Nacional de la Competencia, hereinafter CNC) stipulated that authorisation for the concentration resulting from the acquisition of Unión Fenosa by the Gas Natural Group (hereinafter Gas Natural) would be subject to compliance with certain divestment commitments undertaken by the latter.

These divestment commitments were described in an action plan approved by the CNC on 17<sup>th</sup> March 2009.

As a result of this divestment process, on April 30<sup>th</sup> 2010 MSIP Violín BV, acquired the natural gas distribution activity in certain municipalities of Madrid, split on March 30<sup>th</sup> 2010, from Gas Natural Distribución SDG S.A.. This acquisition was authorised by the NCC on 24<sup>th</sup> March 2010.

Subsequently, on January 24<sup>th</sup> 2011, the NCC amended the action plan requiring Gas Natural to carry out additional divestments. As a result of the above and of a new split, the natural gas distribution activity was contributed to Madrileña Red de gas II, S.A. in various municipalities of Madrid, and some of its districts. This line of activity was also being carried out by Gas Natural Distribución SDG S.A. This split was entered in the Barcelona Mercantile Registry on June 30<sup>th</sup> 2011.

On this date the Madrileña Red de Gas group acquired Madrileña Red de Gas II, S.A. This acquisition, which had been authorised by the NCC and by the National Energy Commission on 11<sup>th</sup> and 12<sup>th</sup> May 2011 respectively, was subject to authorisation by the Community of Madrid. This authorisation was given on May 31<sup>st</sup> 2011.

On May 7<sup>th</sup> 2015, MSIP Violín BV sold all its shares to Elisandra V Spain, S.L., controlled by the consortium formed by Ginkgo Tree Investment Ltd., PGGM Infrastructure Funds and EDF Invest with the subsequent inclusion of Lancashire County Pension Fund to the consortium, it has been set up the solely shareholder of the company at the closing date of the tax year.

On July 25<sup>th</sup>, 2017, The General Meeting of Shareholders approved the transfer of the shareholdings held by Lancashire County Pension Fund, representing 12.50% of the share capital of Elisandra Spain IV, S.L to LPPI Infrastructure Investment LP. By October 2017 Lancashire County Pension Fund had contributed its 12.5% stake in the company to the pooled investments vehicle, LPPI Infrastructure Investments LP, which is owned by it and the London Pension Fund Authority.

## MADRILEÑA RED DE GAS, S.A.U.

### DIRECTORS REPORT FOR THE YEAR ENDED ON 31 DECEMBER 2019

(Expressed in thousand of euros)

#### DEVELOPMENT OF THE BUSINESS

The Company obtained an EBITDA of 146.1 million euros during the year ended on December 31<sup>st</sup>, 2019.

Revenues in the period ended on December 31<sup>st</sup>, 2019 amounted to (1) Euros 186.3 million of which Euros 174.4 million relate to the gas natural business. The remaining Euros 11.9 million are derived through the supply of LPG. Within the natural gas business, 87% of revenues are derived from regulated remuneration relating to distribution activity, composed of the figures established through the Ministry of Industry, Tourism and Commerce Order, 1367/2019 published in Official Gazette No. 312 of December 20<sup>th</sup>, 2019, 11% of revenue relating to natural gas is derived from other regulated services with the remaining and 2% derived from other non-regulated services. In November 2016, the Company acquired, from Repsol, 505 LPG plants and related network assets comprising 41,054 supply points, in the territory of Madrid. This business contributed revenue of 11.9 million euros during the year 2019, with an EBITDA of 1.9 million euros before depreciation and amortisation.

	Natural Gas	LPG	Total	
Remuneration	149.6	-	149.6	
Other regulated income	18.2	11.9	30.1	
Other non-regulated income	4.4	-	4.4	
<b>Turnover figure</b>	<b>172.2</b>	<b>11.9</b>	<b>184.1</b>	(1)
<b>Operating result</b>	<b>144.2</b>	<b>1.9</b>	<b>146.1</b>	(2)
Operating result %	84%	16%	79%	

(1) The difference in turnover is due to the charging connection and extension rights (approx. 2.2 million euros).

(2) EBITDA is defined as operating income + fixed assets depreciation + other expenses + provision excess + changes in provisions for commercial operations + severance payments (Note 18.c) + bank services and similar (Note 18.d) + Impairment of merchandise, raw materials and other supplies+ Impairment and gains/(losses) on disposal of fixed assets.

The Company, at the year end, has administrative authorisations to perform distribution activities in 59 municipalities, including the city of Madrid, where it has authorisation for 5 districts. The total number of connection points to which the Company provides services is 908,515, of which 885,268 correspond to natural gas and 23,247 points of LPG (17,734 have been transferred to natural gas).

MRG considers financial strength as a key strategic pillar, and aims to maintain an investment grade rating as well as high ratio levels relating to solvency and liquidity. Increases in debt are accompanied by additional cash generation derived from the new investments. The company maintains a robust capital structure that is appropriate for the profile of a regulated business.



## **MADRILEÑA RED DE GAS, S.A.U.**

### **DIRECTORS REPORT FOR THE YEAR ENDED ON 31 DECEMBER 2019 (Expressed in thousand of euros)**

In this context, on April 11<sup>th</sup> 2017, the Company completed two new issuances under the existing EMTN program. The issuance was completed by Madrileña Red de Gas Finance BV, which then on lent the funds to MRG through an inter-company loan structure. Both issuances were for 300 million each with terms of 8 and 12 years. The programme is guaranteed by Madrileña Red de Gas and is listed on the Luxembourg stock exchange. The funds raised were primarily earmarked for the redemption of bonds totalling Euros 500 million, with maturity in September 2018, whilst the remainder will be used for different corporate purposes.

At the same time, the Company secured a contingent credit line (Revolving Credit Facility) with a group of four banks amount to 200 million euros over a 5-year term.

The net equity of Madrileña Red de Gas S.A.U. is €298.1million, the majority of which consists of freely-available reserves.

Share capital is currently represented by 104,759 ordinary registered shares with a par value of 10 euros each, fully paid in and with the same voting and economic rights.

## **BUSINESS OUTLOOK**

The company's strategy for the following years continues to focus on financing the growth of its current distribution network to municipalities adjacent to its existing territories which do not currently have natural gas supply, as well as gaining new connection points in its existing territories of operation.

As part of this strategy, the Company will continue to undertake the conversion of LPG supply points it owns to natural gas connection points

## **ENVIRONMENT**

The Company has not received environmental subsidies or income as a result of the activities relating to the environment. The Company has no assets nor has it incurred in expenses related to the environment. The company has incurred in some expenses in order to accomplish and adapt to the current legislation and regulation, thereby to the maintenance of the management environmental system.

## **STAFF**

There were 143 Company employees at the 2019 fiscal year end, of whom 18 are part-time retirees.

## **RESEARCH AND DEVELOPMENT**

The Company has carried out research and development processes during the year.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **DIRECTORS REPORT FOR THE YEAR ENDED ON 31 DECEMBER 2019**

**(Expressed in thousand of euros)**

#### **TREASURY SHARES**

The parent Company has not acquired treasury shares during the year.

#### **AVERAGE PAYMENT PERIOD TO SUPPLIERS**

The average payment period of suppliers is of 61 days (66 days in at December 31<sup>st</sup> 2018)

#### **SUBSEQUENT EVENTS**

On January 20<sup>th</sup> 2020 the taxation authorities notified the Company of the commencement of an inspection of income tax for the fiscal year ended in 2015. At the date on which the annual accounts were authorised for issue, Company management considered it reasonable not to record any expense in this regard.

On March 9<sup>th</sup>, 2020 the Company reduced the amount of the credit facility by Euros 125,000 thousand, and the amount available is Euros 75,000 thousand (note 5).

On March 18<sup>th</sup>, 2020 the assignment of Mr. Ruwantha Vidanaarachchi was revoked and the new director assigned is Mr. Qingtong Li.

On March 18<sup>th</sup>, 2020 Euros 103,000 thousand had been drawn down on the credit facility signed with its direct parent, Elisandra Spain V, S.L., which was approved by the Company in June 2019.

The Company has performed a risk analysis of the crisis brought about by COVID-19 and with the information available at present no significant risk is foreseen that could compromise the Company's ability to continue as a going concern in the next 12 months.

There have been no other significant events subsequent to year-end and to the date of preparation of these consolidated financial statements that the Group considers could significantly affect them.



## **USE OF FINANCIAL INSTRUMENTS**

The Company's activities have no significant exposure to exchange rate risk and the fluctuation of interest rate. However, the Company is exposed to credit and liquidity risk.

The Company's Management focuses on maintaining a solid financial structure that optimises the cost of capital and the availability of financial resources to guarantee business continuity over the long term, in order to enhance value for shareholders while ensuring a solid credit profile. In this regard, the senior unsecured debt credit ratings assigned to the Company by Standard & Poor's and Fitch remains, respectively at BBB.

### Credit risk

In accordance with its corporate objects, the Company collects for the gas system the amounts relating to tolls to access the connection point network located in its distribution territory by invoicing to supply companies. On a monthly basis and within the settlement system framework coordinated by CNMC, a calculation is performed of the excess or shortfall in access tolls invoicing with respect to the remuneration recognised to the Company. If toll invoicing exceeds the remuneration recognised, the Company must settle such difference in favour of other gas system companies. Otherwise, the Company will receive from such companies the remaining balance to complete the remuneration recognised.

Regulations in this respect consider tolls invoiced to the supply companies to be collected for the purposes of the settlement system described above, and therefore in the event of non-payment by such counterparties, the Company is exposed to a credit risk with respect to part of its revenues.

The Company actively manages the aforementioned credit risk through a follow-up of outstanding receivable balances. Similarly, and taking into account (i) the reduced average collection period, less than 30 days, (ii) the regulatory supervisory framework in which gas system activities are performed and (iii) the mechanisms for suspending the contracts for Third-party Network Access in the event of non-payment of tolls to the Company (after a period of 60 days after a reliable request of the counterparty), exposure to the credit risk is considered to be limited.

## **MADRILEÑA RED DE GAS, S.A.U.**

### **DIRECTORS REPORT FOR THE YEAR ENDED ON DECEMBER 31<sup>st</sup> 2018 (Expressed in thousand of euros)**

#### Interest rate risk

During the current year, the Company has been exposed to several financial risks, mainly to interest rate risk.

The Company's interest rate risk results from long-term borrowings.

Borrowings issued at fixed rates expose the Company to the fair value of its financial liabilities.

#### Liquidity and availability of funding risks

The Company maintains a liquidity policy that ensures compliance with the payment commitments acquired, diversifying the coverage of financing needs and debt maturities. Prudent liquidity risk management includes the maintenance of sufficient cash and realizable assets and the availability of funds for an adequate amount to cover the obligations.

On December 31<sup>st</sup>, 2019, available liquidity amounts to 303,426 thousand euros (December 31<sup>st</sup> 2018: 263,042 thousand euros), taking into account cash and equivalents (103,426 thousand euros on December 31<sup>st</sup> 2019 and 63,042 thousand euros on December 31<sup>st</sup> 2018) and unused equivalent credit lines (200,000 thousand euros on December 31<sup>st</sup> 2019 and 200,000 thousand euros on December 31<sup>st</sup> 2018 (Note 14).

The Company's business and investment plans are mainly financed through cash generated from on-going operations and, occasionally, through revolving credit facilities.

It is the Company policy to match the debt's amortisation calendar to its capacity to generate cash flows to meet these maturities. In particular, the Company's Management attempts to ensure that the operations over the next 12 months are always fully financed without the need to substantially modify the conditions and structure of the Company's debt.

Management considers the Company has enough cash reserves to address the payments to realize the following 12 months.