

Naturgás Energía Distribución, S.A.U.

Annual Accounts

31 December 2015

Directors' Report

2015

(With Independent Auditor's Report Thereon)

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

KPMG Auditores S.L.

Torre Iberdrola
Plaza Euskadi, 5
Planta 7ª
48009 Bilbao

Independent Auditor's Report on the Annual Accounts

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

To the Sole Shareholder of
Naturgas Energía Distribución S.A.U.

Report on the Annual Accounts

We have audited the accompanying annual accounts of Naturgas Energía Distribución S.A.U. (the “Company”), which comprise the balance sheet at 31 December 2015, the income statement, statement of changes in equity and statement of cash flows for the year then ended, and notes.

Directors' Responsibility for the Annual Accounts

The Directors are responsible for the preparation of the accompanying annual accounts in such a way that they give a true and fair view of the equity, financial position and financial performance of Naturgas Energía Distribución S.A.U. in accordance with the financial reporting framework applicable to the entity in Spain, specified in note 2 to the accompanying annual accounts, and for such internal control that they determine is necessary to enable the preparation of annual accounts that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these annual accounts based on our audit. We conducted our audit in accordance with prevailing legislation regulating the audit of accounts in Spain. This legislation requires that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the annual accounts are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the annual accounts. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the annual accounts, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the annual accounts 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. An audit also includes evaluating the appropriateness of accounting policies used and reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the annual accounts taken as a whole.

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

Opinion

In our opinion, the accompanying annual accounts give a true and fair view, in all material respects, of the equity and financial position of Naturgas Energía Distribución S.A.U. at 31 December 2015, its financial performance and its cash flows for the year then ended in accordance with the applicable financial reporting framework and, in particular, with the accounting principles and criteria set forth therein.

Report on Other Legal and Regulatory Requirements

The accompanying Directors' report for 2015 contains such explanations as the Directors consider relevant to the situation of the Company, its business performance and other matters, and is not an integral part of the annual accounts. We have verified that the accounting information contained therein is consistent with that disclosed in the annual accounts for 2015. Our work as auditors is limited to the verification of the Directors' report within the scope described in this paragraph and does not include a review of information other than that obtained from the accounting records of the Company.

KPMG Auditores, S.L.

(Signed on original in Spanish)

Estibaliz Bilbao Belda

28 April 2016

**NATURGAS ENERGÍA
DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)**

Annual Accounts
and Directors' Report

31 December 2015

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

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Balance Sheets

31 December 2015 and 2014

(Expressed in thousands of Euros)

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

Assets	Note	2015	2014
Intangible assets	Note 6	405,220	405,586
Patents, licences, trademarks and similar rights		38,271	38,271
Goodwill		366,674	366,674
Computer software		275	641
Property, plant and equipment	Note 7	492,404	524,468
Land and buildings		10,622	10,940
Technical installations, machinery, equipment, furniture and other items		476,623	506,986
Under construction and advances		5,159	6,542
Non-current investments in Group companies and associates	Note 10	342	354
Equity instruments	Note 10	329	329
Loans to companies		13	25
Non-current investments	Note 12	69,517	530
Equity instruments		-	2
Loans to third parties		69,000	-
Other financial assets		517	528
Deferred tax assets	Note 20	8,438	10,271
Total non-current assets		975,921	941,209
Non-current assets held for sale	Note 5	-	118,802
Inventories	Note 13	142	118
Goods for resale		72	72
Advances to suppliers		70	46
Trade and other receivables	Note 12	48,501	133,091
Trade receivables – current		8,132	3,615
Trade receivables from Group companies and associates – current	Note 22	33,767	92,110
Other receivables		6,452	37,185
Personnel		149	181
Public entities, other		1	-
Current investments in Group companies and associates		936,231	575,276
Other financial assets	Note 22	936,231	575,276
Current investments	Note 12	115	124
Other financial assets		115	124
Prepayments for current assets		148	168
Cash and cash equivalents		5	-
Cash		5	-
Total current assets		985,142	827,579
Total assets		1,961,063	1,768,788

The accompanying notes form an integral part of the annual accounts.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Balance Sheets

31 December 2015 and 2014

(Expressed in thousands of Euros)

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

<i>Equity and Liabilities</i>	<i>Note</i>	<i>2015</i>	<i>2014</i>
Capital and reserves	Note 14	1,625,320	1,480,448
Capital			
Registered capital		100,000	100,000
Share premium		869,075	869,075
Reserves			
Legal and statutory reserves		118,272	118,272
Other reserves		330,798	312,229
Profit for the year		207,175	80,872
Grants, donations and bequests received	Note 15	37,770	39,015
Total equity		1,663,090	1,519,463
Non-current provisions		269	503
Other provisions	Note 16	269	503
Non-current payables	Note 18	1,737	1,743
Other financial liabilities		1,737	1,743
Deferred tax liabilities	Note 20	200,895	200,758
Total non-current liabilities		202,901	203,004
Liabilities associated with non-current assets held for sale	Note 5	-	2,251
Current payables	Note 18	3,846	2,953
Other financial liabilities		3,846	2,953
Group companies and associates, current		1	52
Trade and other payables	Note 18	91,225	41,065
Current payables to suppliers		-	104
Suppliers, Group companies and associates, current	Note 22	-	6,031
Other payables		84,483	29,501
Personnel (salaries payable)		2,832	1,621
Public entities, other	Note 20	3,910	3,808
Total current liabilities		95,072	46,321
Total equity and liabilities		1,961,063	1,768,788

The accompanying notes form an integral part of the annual accounts.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Income Statements
for the years ended
31 December 2015 and 2014

(Expressed in thousands of Euros)

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

	<i>Note</i>	2015	2014
Revenues	Note 23	202,815	207,274
Sales		173,834	177,447
Services rendered		28,981	29,827
Self-constructed assets	Note 7	5,247	4,920
Supplies	Note 23	(3,365)	(4,424)
Merchandise used		(160)	(450)
Raw materials and consumables used		(12)	(15)
Subcontracted work	Note 23	(3,193)	(3,959)
Other operating income		2,164	3,074
Non-trading and other operating income		1,979	2,996
Operating grants taken to income		185	78
Personnel expenses	Note 23	(14,936)	(13,917)
Salaries and wages		(11,999)	(10,892)
Employee benefits expense		(2,937)	(3,025)
Other operating expenses		(34,973)	(35,833)
External services		(30,585)	(32,065)
Taxes		(4,277)	(3,598)
Losses, impairment and changes in trade provisions	Notes 12 and 16	(56)	(87)
Other operating expenses		(55)	(83)
Amortisation and depreciation	Notes 6 and 7	(50,918)	(55,840)
Non-financial and other capital grants	Note 15	3,287	3,349
Provision surpluses		281	253
Impairment and gains/(losses) on disposal of fixed assets	Note 23	125,403	(32)
Gains/(losses) on disposal and other		125,403	(32)
Other income/(expenses)	Note 23	-	(7)
Results from operating activities		235,005	108,817
Finance income		1,899	3,674
Dividends			
Group companies and associates		126	150
Marketable securities and other financial instruments			
Group companies and associates	Note 11	1,640	3,496
Other	Note 11	133	28
Finance costs	Note 17	(72)	(99)
Other		(72)	(99)
Net finance income		1,827	3,575
Profit before income tax		236,832	112,392
Income tax	Note 20	(29,657)	(31,520)
Profit for the year		207,175	80,872

The accompanying notes form an integral part of the annual accounts.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Statements of Changes in Equity
for the years ended
31 December 2015 and 2014

A) Statements of Recognised Income and Expense
for the years ended
31 December 2015 and 2014

(Expressed in thousands of Euros)

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

	<i>Note</i>	<i>2015</i>	<i>2014</i>
Profit for the year		207,175	80,872
Income and expense recognised directly in equity			
Grants, donations and bequests		1,763	2,478
Transfers to liabilities associated with non-current assets held for sale		(16)	(2,251)
Tax effect		(489)	(63)
Total income and expense recognised directly in equity	Note 15	1,258	164
Amounts transferred to the income statement			
Grants, donations and bequests		(3,299)	(3,364)
Tax effect		796	814
Total amounts transferred to the income statement	Note 15	(2,503)	(2,550)
Total recognised income and expense		205,930	78,486

The accompanying notes form an integral part of the annual accounts.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Statements of Changes in Equity
for the years ended
31 December 2015 and 2014

B) Statement of Total Changes in Equity for the year ended
31 December 2015

(Expressed in thousands of Euros)

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

	Registered capital	Share premium	Reserves	Prior years'	Profit for the year	Grants, dona	Total
Balance at 31 December 2014 and 1 January 2015	100,000	869,075	430,501	-	80,872	39,015	1,519,463
Recognised income and expense	-	-	-	-	207,175	(1,245)	205,930
Transactions with shareholders or owners							
Distribution of profit for 2014							
Dividends	-	-	-	(62,303)	-	-	(62,303)
Distribution of profit for the year	-	-	-	80,872	(80,872)	-	-
Other changes in equity	-	-	18,569	(18,569)	-	-	-
Balance at 31 December 2015	100,000	869,075	449,070	-	207,175	37,770	1,663,090

The accompanying notes form an integral part of the annual accounts.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Statements of Changes in Equity
for the years ended
31 December 2015 and 2014

B) Statement of Total Changes in Equity for the year ended
31 December 2014

(Expressed in thousands of Euros)

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

	Registered capital	Share premium	Reserves	Prior years'	Profit for the year	Grants, dona	Total
Balance at 31 December 2013 and 1 January 2014	100,000	869,075	411,933	-	74,478	41,401	1,496,887
Recognised income and expense	-	-	-	-	80,872	(2,386)	78,486
Transactions with shareholders or owners							
Distribution of profit for 2013							
Dividends	-	-	-	(55,910)	-	-	(55,910)
Distribution of profit for the year	-	-	-	74,478	(74,478)	-	-
Other changes in equity	-	-	18,568	(18,568)	-	-	-
Balance at 31 December 2014	100,000	869,075	430,501	-	80,872	39,015	1,519,463

The accompanying notes form an integral part of the annual accounts.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Statements of Cash Flows
for the years ended
31 December 2015 and 2014

(Expressed in thousands of Euros)

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

	2015	2014
Cash flows from operating activities		
Profit for the year before tax	236,832	112,392
Adjustments for:		
Amortisation and depreciation	50,918	55,840
Impairment	51	87
Change in provisions	(281)	(253)
Grants recognised in the income statement	(3,287)	(3,349)
Proceeds from disposals of fixed assets	(125,403)	32
Finance income	(1,899)	(3,678)
Finance costs	72	99
Change in fair value of financial instruments	1,190	-
Other income and expenses	(5,247)	(4,915)
Changes in operating assets and liabilities		
Inventories	(24)	223
Trade and other receivables	15,592	(55,018)
Other current assets	20	12
Trade and other payables	41,643	(8,692)
Provisions	(6)	(607)
Other non-current assets and liabilities	(3)	(4)
Other cash flows from operating activities		
Interest paid	(72)	(62)
Dividends received	126	150
Interest received	1,773	2,422
Income tax paid	(18,235)	(13,626)
Cash flows from operating activities	193,760	81,053
Cash flows from investing activities		
Payments for investments		
Intangible assets	(52)	(31)
Property, plant and equipment	(12,362)	(12,616)
Other financial assets	(361,006)	(14,653)
Proceeds from sale of investments		
Group companies and associates	12	12
Property, plant and equipment	240,712	163
Other financial assets	20	91
Cash flows used in investing activities	(132,676)	(27,034)
Cash flows from financing activities		
Proceeds from and payments for equity instruments		
Issue of equity instruments	2	-
Grants, donations and bequests received	1,228	1,992
Proceeds from and payments for financial liability instruments		
Issue		
Other	3	54
Redemption and repayment of		
Other payables	(9)	(155)
Dividends and interest on other equity instruments paid		
Dividends	(62,303)	(55,910)
Cash flows used in financing activities	(61,079)	(54,019)
Net increase in cash and cash equivalents	5	-
Cash and cash equivalents at year end	5	-

The accompanying notes form an integral part of the annual accounts.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

31 December 2015

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

(1) Nature and Activities of the Company, Regulatory Framework and Composition of the Group

Naturgas Energía Distribución, S.A.U. (hereinafter the Company) was set up as a corporation (*sociedad anónima*) under the name of Naturcorp Redes, S.A.U. on 31 December 2003 and adopted its current name in 2005. Its registered office is located in Bilbao (Vizcaya).

According to article 2 of its articles of association, the Company's statutory activity comprises:

- Natural gas transmission activities which, pursuant to article 3 of Royal Decree 1434/2002 of 27 December 2002, encompass natural gas transmission through the network in order to supply distributors or, where applicable, end consumers, as well as to cover international exchanges; the regasification of natural gas for supply to the transmission network and the liquefaction of natural gas; the storage of natural gas for supply to the gas system and the tariff-based sale and purchase of natural gas for the market, complying with the procedures and/or obtaining the authorisations necessary in accordance with applicable legislation.
- Natural gas distribution activities which, pursuant to article 7 of Royal Decree 1434/2002 of 27 December 2002, encompass the transmission of natural gas, at the appropriate quality, from transmission networks to points of supply, and the tariff-based sale of natural gas to consumers.

As explained in note 11 the Company holds investments in subsidiaries and associates. Consequently, in accordance with prevailing legislation, the Company is the parent of a group of companies. In accordance with generally accepted accounting principles in Spain, consolidated annual accounts are to be prepared to give a true and fair view of the financial position of the Group, the results of operations and changes in its equity and cash flows. Details of investments in Group companies and associates are provided in Appendix II.

Nevertheless, the Company does not prepare consolidated annual accounts as the subgroup is part of the Spanish Naturgas Energía Grupo, S.A. group, as provided in section 2 of article 43 of the Spanish Code of Commerce.

The Company forms part of the Naturgas Group, the parent of which is Naturgas Energía Grupo, S.A., with registered offices in Bilbao (Vizcaya).

On 25 February 2016 the directors of Naturgas Energía Grupo, S.A. are expected to authorise the issue of the consolidated annual accounts for 2015, which will be filed at the Lisbon Mercantile Registry.

In prior years, the Company acquired net assets derived from mergers of different companies. Details of these operations are included in the notes to the annual accounts for the years in which they were carried out.

Details of the basic regulatory framework applicable to the Company are as follows:

Hydrocarbon Industry Law 34/1998 of 7 October 1998, amended by Law 12/2007 and by Royal Decree-Law 13/2012, introducing mechanisms to foster competition within the sector and defining a new natural gas market model. This law implements the main system definitions as regards the parties that participate therein and organises the gas system, distinguishing between regulated activities (regasification, transmission, storage and distribution) and unregulated activities (supply and other services). Lastly, this law defines the rights and obligations of the parties that operate in the natural gas market.

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

The aforementioned Hydrocarbon Industry Law 34/1998, which repealed all other conflicting laws, and subsequent implementing legislation set out, inter alia, the following principles:

a) Gradual liberalisation of the natural gas system:

This law provides for the liberalisation of gas supply activities, gradually enabling different types of customers to select their supplier. Since 1 January 2003, different types of customers have been able to freely select their supplier. The schedule for implementing the last resort supply commenced on 1 July 2008, leading to the elimination of the previous tariff-based supplies from distributors.

Royal Decree 949/2001 of 3 August 2001 regulates third-party access to gas facilities and sets out an integrated economic system for the natural gas sector. This Royal Decree also sets out the model for calculating natural gas tariffs and the payments and fees charged for third-party use of the gas network.

Following approval by the Delegate Commission on Economic Affairs, the Ministry of Industry, Tourism and Trade set the new prices for last resort tariffs and the tolls and charges for basic third-party access services. The entitlement of direct market consumers and suppliers to use the basic grid and transmission and distribution facilities was also established, and a single nationwide toll was set for the use of these networks. Ministry of Industry, Energy and Tourism Order IET/2445/2014, stipulating the tolls and charges for third-party access to gas facilities and the remuneration for regulated activities for 2015, was published on 26 December 2014.

Royal Decree 1434/2002 of 27 December 2002, implementing the Hydrocarbon Industry Law, regulates transmission, distribution, sale and supply activities and the authorisation procedures for gas facilities.

With respect to distributors, Ministry of Economy Order ECO/301/2002 set out the remuneration for distribution activities for the first time, to be determined as of that date on the basis of an annual revision, taking into account increases in the points of supply, the volume of gas transmitted and price fluctuations. Publication of Royal Decree-Law 8/2014 and Law 18/2014 brought about changes to the remuneration model applicable to distributors from the second half of 2014 onwards, although the annual revision of remuneration will continue to be determined by reference to the variation in demand.

In addition to tolls and changes, the aforementioned Ministry of Economy Order IET/2445/2014 also sets the remuneration for regulated activities in 2015.

Similarly, Ministry of Economy Order ECO/2692/2002 of 28 October 2002 defines the settlement procedures for the payment obligations and rights to receivables necessary to remunerate natural gas regasification, transmission, storage and distribution activities and the pertinent specifically allocated payments and charges, and defines a system for reporting on natural gas billings and consumption.

b) Settlements of regulated activities - gas sector:

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Basically as a result of the entry into force of the Spanish Gas Industry Law 34/1998 and the corresponding implementing provisions, intercompany settlements have arisen since 2002. These settlements are performed by the Spanish National Markets and Competition Commission (which includes the defunct National Energy Commission) and give rise to receipts and payments between companies in the sector in order to redistribute the proceeds obtained from access tolls and charges so that each company receives the remuneration effectively allocated to it for regulated activities. Settlement functions, at present performed temporarily by the Commission, will be transferred when determined by the Ministry of Industry, Energy and Tourism in accordance with Law 3/2013 on the creation of the Spanish National Markets and Competition Commission.

c) Financing of the cumulative deficit at 31 December 2015:

Law 18/2014 defines the treatment to be given to the tariff deficit affecting the gas sector at the end of 2014, i.e. the financing of the negative imbalances between revenues and costs of the gas system for each year.

As such, the Law stipulates that the amount of the cumulative deficit at 31 December 2014 will be determined in the final settlement for 2014 (settlement 15), and that regulated parties will be entitled to recover the annual amounts of this cumulative deficit in the settlements for the next 15 years and accrue interest at market rates. The amount of the deficit recognised, the corresponding annual amount and the interest rate applied are subject to approval by Order of the Ministry of Industry, Energy and Tourism.

Based on Spanish National Markets and Competition Commission forecasts, the cumulative deficit at 31 December 2014 could amount to Euros 1,011 million. In such a scenario, an amount of Euros 70 million would be assigned to the Company, reimbursement of which would foreseeably commence as of November 2016.

The sector is not expected to generate a deficit for 2015.

d) Correct functioning of the system guaranteed through the following measures:

Enagás GTS, S.A.U. carries out system technical manager activities, for which it receives remuneration. As the entity responsible for the technical management of the basic grid and secondary transmission networks, Enagás GTS, S.A.U. must guarantee the continuity and security of supply of natural gas and the correct coordination between access points, storage facilities and transmission facilities under criteria of non-discrimination.

e) Unbundling of activities

Activities pertaining to the supply of natural gas by pipeline are conducted by transmission agents, distributors and suppliers. Regasification, strategic storage, transmission and distribution are regulated activities, whilst supply activities are carried out freely and the corresponding economic regime is determined on the basis of the terms and conditions agreed between the parties.

In this regard, trading companies that carry out any of the regulated activities described in the preceding paragraph should have this activity as their sole statutory activity and may not, therefore, carry out any supply activities. Similarly, companies engaged in the supply of natural gas should have this activity as their sole statutory activity and may not carry out any regulated activities.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Natural gas companies that conduct more than one of the regulated activities described above must maintain separate accounts for each of these activities in their internal accounting records, exactly as would be required if these activities were conducted by different companies. Furthermore, the Law defines a number of mandatory unbundling requirements applicable to companies that carry out regulatory activities and belong to a corporate group that also includes companies that carry out supply activities.

(2) Basis of Presentation

(a) True and fair view

The annual accounts for 2015 have been prepared based on the accounting records of Naturgas Energía Distribución, S.A.U. in accordance with prevailing legislation and the Spanish General Chart of Accounts to give a true and fair view of the equity and financial position at 31 December 2015 and results of operations, changes in equity, and cash flows for the year then ended.

The Directors consider that the annual accounts for 2015, authorised for issue on 24 February 2016, will be approved with no changes by the sole shareholder.

(b) Comparative information

The balance sheet, income statement, statement of changes in equity, statement of cash flows and the notes thereto for 2015 include comparative figures for 2014, which formed part of the annual accounts approved by the sole shareholder on 15 June 2015. As permitted by the Spanish Accounting and Auditing Institute (ICAC) resolution of 29 January 2016 regarding the information on average supplier payment periods in commercial transactions which must be disclosed in the notes to the annual accounts, no comparative information is provided in note 19 with respect to this new obligation.

In 2013 the Company opted to revalue certain items on the balance sheet in accordance with Vizcaya Provincial Decree 11/2012 of 18 December 2012, which adopted tax measures aimed at consolidating public finances and boosting economic activity. The annual accounts for 2013 included the recognition of this revaluation effective as of 1 January 2013, which amounts to Euros 98,272 thousand net of tax, as follows:

	Thousands of Euros
Property, plant and equipment (note 7)	<u>103,444</u>
	103,444
Tax (note 14)	<u>(5,172)</u>
Revaluation reserve under VPD 11/2012 of 18 December 2012 (note 14)	<u>98,272</u>

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(c) Functional and presentation currency

The figures disclosed in the annual accounts are expressed in thousands of Euros, the Company's functional and presentation currency, rounded off to the nearest thousand.

(d) Critical issues regarding the valuation and estimation of relevant uncertainties and judgements used when applying accounting principles

Relevant accounting estimates and judgements and other estimates and assumptions have to be made when applying the Company's accounting principles to prepare the annual accounts.

(i) Relevant accounting estimates and assumptions

Valuation allowances for bad debts require a high degree of judgement by management and a review of individual balances based on customers' credit ratings, current market trends and historical analysis of bad debts at an aggregated level.

The Company tests goodwill for impairment on an annual basis. The calculation of the recoverable amount of a division to which goodwill has been allocated requires the use of estimates by management.

Other estimates made by the Company relate to the useful life of property, plant and equipment and intangible assets, provisions and settlements for the regulated activities carried out, which are used as a basis for determining the revenues from these regulated activities.

(ii) Changes in accounting estimates

Although estimates are calculated by the Company's directors based on the best information available at 31 December 2015, future events may require changes to these estimates in subsequent years. Any effect on the annual accounts of adjustments to be made in subsequent years would be recognised prospectively.

(3) Distribution of Profit

The distribution of the Company's profit for the year ended 31 December 2014, approved by the sole shareholder on 15 June 2015, is as follows:

	Euros
Basis of allocation	
Profit for the year	80,872,337.01
Distribution	
Goodwill reserve	18,568,846.27
Dividends	62,303,490.74
	80,872,337.01

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

The proposed distribution of the Company's 2015 profit to be submitted to the sole shareholder for approval is as follows:

	Euros
Basis of allocation	
Profit for the year	207,175,464.28
Distribution	
Goodwill reserve	18,333,659.95
Dividends	188,841,804.33
	207,175,464.28

At 31 December non-distributable reserves are as follows:

	Thousands of Euros
Non-distributable reserves	
Legal reserve	20,000
Revaluation reserves	98,272
Goodwill reserve	128,367
Production investment reserve	73,000
	319,639

Profit recognised directly in equity cannot be distributed, either directly or indirectly.

(4) Significant Accounting Policies

(a) Intangible assets

Intangible assets are measured at cost of acquisition. Intangible assets are carried at cost, less any accumulated amortisation and impairment.

(i) Goodwill

Goodwill on business combinations carried out subsequent to the date of transition to the Spanish General Chart of Accounts (1 January 2008) reflects the excess of the cost of the business combination over the acquisition-date fair value of the assets acquired and liabilities and contingent liabilities assumed from the acquired business.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Goodwill is not amortised but is tested for impairment annually or more frequently where events or circumstances indicate that an asset may be impaired. Goodwill on business combinations is allocated to the cash-generating units (CGUs) or groups of CGUs which are expected to benefit from the synergies of the business combination and the criteria described in section (d) Impairment of non-financial assets subject to amortisation or depreciation are applied. After initial recognition, goodwill is measured at cost less any accumulated impairment losses.

(ii) Computer software

Computer software acquired by the Company is recognised at the cost incurred. Computer software maintenance costs are charged as expenses when incurred.

(iii) Patents, licences, trademarks and similar rights

These rights primarily reflect the value assigned to customers / connection points by an independent expert in the acquisition cost identification and allocation process for a number of subsidiaries merged with the Company in prior years.

(iv) Subsequent costs

Subsequent costs incurred on intangible assets are recognised in profit and loss, unless they increase the expected future economic benefits attributable to the intangible asset.

(v) Useful life and amortisation rates

The Company assesses whether the useful life of each intangible asset acquired is finite or indefinite. An intangible asset is regarded by the Company as having an indefinite useful life when there is no foreseeable limit to the period over which the asset will generate net cash inflows.

Intangible assets with indefinite useful lives are not amortised, but are instead tested for impairment on an annual basis or whenever there is an indication that the intangible asset may be impaired.

The Company assesses and determines the impairment to be recognised or reversed based on the criteria in note 4 (d).

Intangible assets with finite useful lives are amortised by allocating the depreciable amount of an asset on a straight-line basis over the following estimated years of useful life:

	Amortisation method	Estimated years of useful life
Computer software	Straight-line	4
Patents, licences, trademarks and similar rights (prior to 1 January 2011)	Straight-line	30

The depreciable amount of intangible assets is measured as the cost of the asset, less any residual value.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

The Company reviews the residual value, useful life and amortisation method for intangible assets at each financial year end. Changes to initially established criteria are accounted for as a change in accounting estimates.

In accordance with final provision one of Audit Law 22/2015 of 20 July 2015, as of 1 January 2016, intangible assets, including goodwill, shall be considered assets with a finite useful life. Where the useful life of intangible assets cannot be estimated reliably, they shall be amortised over a period of ten years. Similarly, it will be presumed that the useful life of goodwill, unless there is evidence to the contrary, is also ten years. As indicated in note 6, the Company has recognised intangible assets with indefinite lives totalling Euros 38,271 thousand and goodwill totalling Euros 366,674 thousand. Furthermore, as indicated in note 14 (iii), the Company has recognised a goodwill reserve of Euros 128,367 thousand, which may be distributed to the extent that it exceeds the carrying amount of goodwill. At the date of authorisation for issue of the annual accounts, the Directors are evaluating the accounting implications of the Law, specifically as regards the estimation of the useful lives of the aforementioned assets, to determine its impact on the Company's equity. At the date of authorisation for issue of the annual accounts, the Royal Decree implementing the Law and, where appropriate, regulating the transitional regime has not yet been passed.

(vi) Impairment losses

The Company measures and determines impairment to be recognised or reversed based on the criteria in section (d) Impairment of non-financial assets subject to amortisation or depreciation.

(b) Property, plant and equipment

(i) Initial recognition

Property, plant and equipment are measured at cost of acquisition or production. The annual accounts for 2013 included the revaluation of assets recognised up to 1 January 2013 permitted by Vizcaya Provincial Decree 11/2012 of 18 December 2012, which contained several tax measures aimed at consolidating public finances and boosting economic activity.

Capitalised production costs are recognised under self-constructed assets in the income statement. Property, plant and equipment are carried at cost less any accumulated depreciation and impairment.

Items of property, plant and equipment recognised prior to 31 December 1996 are carried at a revalued amount as permitted by pertinent legislation.

(ii) Depreciation

Property, plant and equipment are depreciated by allocating the depreciable amount of the asset on a systematic basis over its useful life. The depreciable amount is the cost of an asset, less its residual value.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Property, plant and equipment are depreciated using the following criteria:

	Depreciation method	Estimated years of useful life
Buildings	Straight-line	10 -- 50
Technical installations and machinery (gas distribution network)	Straight-line	12.5 -- 25
Technical installations and machinery (regulation and metering stations: civil works)	Straight-line	5--10
Technical installations and machinery (regulation and metering stations: machinery)	Straight-line	5--10
Technical installations and machinery (synthetic natural gas plants and installations)	Straight-line	12.5
Other installations, equipment and furniture	Straight-line	5 -- 10
Other property, plant and equipment	Straight-line	4 -- 6

The Company reviews residual values, useful lives and depreciation methods at each financial year end. Changes to initially established criteria are accounted for as a change in accounting estimates.

Increases in value resulting from revaluations permitted by law are depreciated over the remaining useful life of the revalued assets.

(iii) Subsequent costs

Subsequent to initial recognition of the asset, only the costs incurred which increase capacity or productivity or which lengthen the useful life of the asset are capitalised. The carrying amount of parts that are replaced is derecognised. Costs of day-to-day servicing are recognised in profit and loss as incurred.

(iv) Impairment

The Company measures and determines impairment to be recognised or reversed based on the criteria in section (d) Impairment of non-financial assets subject to amortisation or depreciation.

(c) Non-current assets held for sale

(i) Non-current assets held for sale

The Company recognises non-current assets or disposal groups as held for sale if their carrying amounts will be recovered principally through a sales transaction rather than through continuing use. Non-current assets or disposal groups are classified as held for sale, provided that they are available for immediate sale in their present condition subject to terms that are usual and customary for sales of such assets and that the disposal is highly probable.

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Non-current assets or disposal groups classified as held for sale are measured at the lower of the carrying amount and fair value less costs to sell and are not depreciated.

Impairment losses on initial classification and subsequent remeasurement of assets classified as held-for-sale are recognised under profit or loss from continuing operations in the income statement, except in the case of discontinued operations. Impairment losses on a cash-generating unit (CGU) are allocated first to reduce the carrying amount of goodwill and then to reduce pro rata the carrying amounts of other assets in the unit. Impairment of goodwill recognised may not be reversed.

Gains due to increases in the fair value less costs to sell are recognised in the income statement to the extent of the cumulative impairment previously recognised due to measurement at fair value less costs to sell or to impairment of non-current assets.

(d) Impairment of non-financial assets subject to amortisation or depreciation

The Company evaluates whether there are indications of possible impairment losses on non-financial assets subject to amortisation or depreciation to verify whether the carrying amount of these assets exceeds the recoverable amount. The recoverable amount is the higher of the fair value less costs to sell and the value in use.

The Company tests goodwill and intangible assets with indefinite useful lives for impairment at least annually, irrespective of whether there is any indication that the assets may be impaired.

Impairment losses are recognised in the income statement.

Recoverable amount is determined for each individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets. If this is the case, recoverable amount is determined for the cash-generating unit to which the asset belongs.

(e) Leases

(i) Lessor accounting

The Company has conveyed the right to use certain assets (mainly gas meters) through lease contracts.

Finance leases are those in which the Company transfers to third parties the significant risks and rewards of ownership of the asset. All other leases are classified as operating leases. The Company has no finance leases at 31 December 2015 and 2014.

Assets leased to third parties under operating lease contracts are presented according to their nature, applying the accounting policies set out in the section on property, plant and equipment.

Income from operating leases, net of incentives granted, is taken to the income statement on a straight-line basis over the lease term.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(ii) Lessee accounting

The Company also has rights to use certain assets through lease contracts.

Leases in which the Company assumes substantially all the risks and rewards incidental to ownership are classified as finance leases, otherwise they are classified as operating leases. The Company has no finance leases at 31 December 2015 and 2014.

Lease payments under an operating lease, net of incentives received, are recognised as an expense on a straight-line basis over the lease term.

The Company recognises initial direct costs of operating leases as an expense when incurred.

(f) Financial instruments

(i) Recognition

The Company recognises financial instruments when it becomes party to the contract or legal transaction, in accordance with the terms set out therein.

Regular way purchases or sales of financial assets are recognised, depending on the type of asset, at the trade date or the settlement date.

(ii) Classification and separation of financial instruments

Financial instruments are classified on initial recognition as a financial asset, a financial liability or an equity instrument in accordance with the economic substance of the contractual arrangement and the definitions of a financial asset, a financial liability and an equity instrument.

The Company classifies financial instruments into different categories based on the nature of the instruments and the Company's intentions on initial recognition.

(iii) Offsetting principles

A financial asset and a financial liability are offset only when the Company currently has the legally enforceable right to offset the recognised amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

(iv) Loans and receivables

Loans and receivables comprise trade and non-trade receivables with fixed or determinable payments that are not quoted in an active market other than those classified in other financial asset categories. These assets are initially recognised at fair value, including transaction costs, and are subsequently measured at amortised cost using the effective interest method.

Nevertheless, financial assets which have no established interest rate, which mature or are expected to be received in the short term, and for which the effect of discounting is immaterial, are measured at their nominal amount.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(v) Financial assets and financial liabilities carried at cost

Investments in equity instruments for which the fair value cannot be reliably estimated are measured at cost less any accumulated impairment. Nonetheless, if the financial assets or liabilities can subsequently be reliably measured on an ongoing basis, they are accounted for at fair value and any gain or loss is recognised in accordance with their classification.

(vi) Investments in Group companies and associates

Group companies are those over which the Company, either directly, or indirectly through subsidiaries, exercises control as defined in article 42 of the Spanish Code of Commerce, or when the companies are controlled by one or more individuals or entities acting jointly or under the same management through agreements or statutory clauses.

Associates are entities over which the Company, either directly, or indirectly through subsidiaries, exercises significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies.

Investments in Group companies and associates are initially recognised at cost, which is equivalent to the fair value of the consideration given, including transaction costs, and are subsequently measured at cost net of any accumulated impairment.

The cost of the investment includes any additional consideration contingent on future events or compliance with certain conditions, provided that it is considered probable that such consideration will be payable and the fair value can be estimated reliably. Adjustments to this consideration in subsequent years entail corrections to the cost.

The cost of acquisition of an investment in a Group company or associate includes its carrying amount immediately before classification. Amounts previously recognised in equity are transferred to the income statement when the investment is derecognised or when an impairment loss is recognised or reversed, as described in section (ix) Impairment of financial assets.

(vii) Interest and dividends

Interest is recognised using the effective interest method.

Dividends from investments in equity instruments are recognised when the Company is entitled to receive them.

(viii) Derecognition of financial assets

Financial assets are derecognised when the contractual rights to the cash flows from the financial asset expire or have been transferred and the Company has transferred substantially all the risks and rewards of ownership.

On derecognition of a financial asset in its entirety, the difference between the carrying amount and the sum of the consideration received, net of transaction costs, including any new asset obtained less any new liability assumed and any cumulative gain or loss deferred in recognised income and expense, is recorded in profit or loss.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(ix) Impairment of financial assets

The Company recognises impairment of loans and receivables when estimated future cash flows are reduced or delayed due to debtor insolvency.

Impairment of financial assets carried at amortised cost

The amount of the impairment loss of financial assets carried at amortised cost is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. For variable income financial assets, the effective interest rate corresponding to the measurement date under the contractual conditions is used.

The impairment loss is recognised in profit and loss and may be reversed in subsequent periods if the decrease can be objectively related to an event occurring after the impairment has been recognised. The loss can only be reversed to the limit of the amortised cost of the assets had the impairment loss not been recognised.

The Company has made a collective or global valuation allowance for trade balances, equivalent to 3% of the total amount of trade receivables at year end, less the recoverable amount of guarantees obtained and without taking into account balances with public entities, or balances that have been individually tested for impairment.

Investments in Group companies and associates and equity instruments carried at cost

Impairment is calculated by comparing the carrying amount of the investment with its recoverable amount. The recoverable amount is the higher of value in use and fair value less costs to sell.

In subsequent years, reversals of impairment losses in the form of increases in the recoverable amount are recognised, up to the limit of the carrying amount that would have been determined for the investment if no impairment loss had been recognised.

(x) Financial liabilities

Financial liabilities, including trade and other payables, that are not classified as held for trading or as financial liabilities at fair value through profit or loss are initially recognised at fair value less any transaction costs directly attributable to the issue of the financial liability. After initial recognition, liabilities classified under this category are measured at amortised cost using the effective interest method.

Nevertheless, financial liabilities which have no established interest rate, which mature or are expected to be settled in the short term, and for which the effect of discounting is immaterial, are measured at their nominal amount.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(xi) Reverse factoring

The Company has contracted reverse factoring facilities with a financial institution to manage payments to suppliers. Trade payables settled under the management of financial institutions are recognised under trade and other payables in the balance sheet until they are settled, repaid or have expired.

(xii) Security deposits

Security deposits received in relation to gas supply contracts are measured using the same criteria as for financial liabilities.

Security deposits paid in relation to lease contracts are measured using the same criteria as for financial assets.

(xiii) Derecognition and modifications of financial liabilities

The Company derecognises all or part of a financial liability when it either discharges the liability by paying the creditor, or is legally released from primary responsibility for the liability either by process of law or by the creditor.

(g) Inventories

Gas inventories in distribution networks are measured at the lower of cost and net realisable value, based on gas prices.

Goods for resale are measured at cost of acquisition, which is calculated as the lower of weighted average price and market value.

When the cost of inventories exceeds net realisable value, materials are written down to net realisable value.

(h) Grants, donations and bequests

Grants, donations and bequests are recorded in recognised income and expense when, where applicable, they have been officially awarded, the conditions attached to them have been met or there is reasonable assurance that they will be received.

Monetary grants, donations and bequests are measured at the fair value of the sum received.

In subsequent years, grants, donations and bequests are recognised as income as they are applied.

(i) Capital grants

Capital grants are recognised as income over the same period and in the proportions in which depreciation on those assets is charged or when the assets are disposed of, derecognised or impaired.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Capital grants basically comprise those received under the agreements between the Company (or Group companies) and the Regional Government of the Basque Country or the Asturias Department of Industry. The Directors consider that all the conditions of award have been met or are being met.

(ii) Connection and extension charges

Amounts received from customers as connection charges in respect of the installation works required to enable new supplies or extend existing supplies are recognised under grants, donations and bequests and taken to profit and loss over the useful life of the extension facilities financed.

(iii) Gas distribution network contracts

Prior to 2000, when contracting supply to customers connected to a network at a pressure exceeding 4 bar, the former Sociedad de Gas de Euskadi, S.A. (now merged into Naturgas Energía Distribución, S.A.U.) undertook to construct a suitable distribution network to supply natural gas to consumers in exchange for monetary consideration at the contract execution date, in addition to the future revenue from gas sales. The constructed network would then be owned by the Company. No contracts of this type have been arranged since 2001, nor have any such amounts been billed to new customers connected to a network at a pressure exceeding 4 bar. This also includes revenues from end customers for the modification of the network layout. The Company recognises this revenue in profit and loss on a straight-line basis over the same period in which the distribution networks are depreciated.

(i) Provisions

(i) General criteria

Provisions are recognised when the Company has a present obligation (legal, contractual, constructive or tacit) as a result of a past event; it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the expenditure required to settle the present obligation at the end of the reporting period, taking into account all risks and uncertainties surrounding the amount to be recognised as a provision and, where the time value of money is material, the financial effect of discounting provided that the expenditure to be made each period can be reliably estimated.

The tax effect and gains on the expected disposal of assets are not taken into account in measuring a provision.

If it is not probable that an outflow of resources will be required to settle an obligation, the provision is reversed.

(j) Revenue from the sale of goods and rendering of services

Revenue from the sale of goods or services is measured at the fair value of the consideration received or receivable.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(i) Revenue from sales

The new regulatory framework for the gas sector in Spain entered into force in February 2002 (see note 1) and governs the settlement procedures for the redistribution between the sector companies of revenues from tolls, charges and tariffs, net of payments for specific purposes, so that each company receives the revenues allocated for its regulated activities. The estimate of these settlements accrued at 31 December 2015 and 2014 and pending settlement by the Spanish National Markets and Competition Commission (CNMC) is recognised as an increase in revenue in the amount accrued or as a decrease in revenue in the amount obtained that corresponds to other companies.

The final settlements for 2014 and 2013 had not been published at the reporting date of these annual accounts. However, they are not expected to differ significantly from the estimates, including the deficit estimate. The Ministerial Order of 28 October 2002, which regulates the settlement procedures, provides that deviations, arising from the application of final settlement procedures, between final net revenues subject to settlement and the remuneration allocated each year will be taken into account in the calculation of tariffs, tolls and charges for the following two years.

(ii) Services rendered

Revenues associated with the rendering of services are recognised in the income statement by reference to the stage of completion at the reporting date when revenues, the stage of completion, the costs incurred and the costs to complete the transaction can be estimated reliably and it is probable that the economic benefits derived from the transaction will flow to the Company.

(k) Income taxes

The income tax expense or tax income for the year comprises current tax and deferred tax.

Current tax assets or liabilities are measured at the amount expected to be paid to or recovered from the taxation authorities, using the tax rates and tax laws that have been enacted or substantially enacted at the reporting date.

Current and deferred tax are recognised as income or an expense and included in profit or loss for the year, except to the extent that the tax arises from a transaction or event which is recognised, in the same or a different year, directly in equity, or from a business combination.

In 2015 and 2014 the Company filed consolidated tax returns with the following companies: EDP Gas Iberia, S.L.U. (parent of the tax group), EDP Comercializadora, S.A.U., Naturgas Energía Grupo, S.A., Naturgas Energía Servicios, S.A.U. and Cogeneración Montjuic, S.L. In 2014, EDP Gas Iberia, S.L.U. was named Millennium Energy, S.L.

In addition to the factors to be considered for individual taxation, set out previously, the following factors are taken into account when determining the accrued income tax expense for the companies forming the consolidated tax group:

- Temporary and permanent differences arising from the elimination of profits and losses on transactions between Group companies, derived from the process of determining consolidated taxable income.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

- Deductions and credits corresponding to each company forming the consolidated tax group. For these purposes, deductions and credits are allocated to the company that carried out the activity or obtained the profit necessary to obtain the right to the deduction or tax credit.

Temporary differences arising from the elimination of profits and losses on transactions between tax group companies are allocated to the company which recognised the profit/loss and are valued using the tax rate of that company.

A reciprocal credit and debit arises between the companies that contribute tax losses to the consolidated Group and the rest of the companies that offset those losses. Where a tax loss cannot be offset by the other consolidated Group companies, these tax credits for loss carryforwards are recognised as deferred tax assets using the applicable recognition criteria, considering the tax group as a taxable entity.

The Parent of the Group records the total consolidated income tax payable (recoverable) with a debit (credit) to receivables (payables) from/to Group companies and associates.

The amount of the debt (credit) relating to the subsidiaries is recognised with a credit (debit) to payables (receivables) to/from Group companies and associates.

(i) Taxable temporary differences

Deferred tax liabilities derived from taxable temporary differences are recognised in all cases except where they arise from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither accounting profit nor taxable income.

(ii) Deductible temporary differences

Deferred tax assets derived from deductible temporary differences are recognised provided that it is probable that sufficient taxable income will be available against which they can be utilised. Nonetheless, assets arising from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither accounting profit nor taxable income, are not recognised.

Tax planning opportunities are only considered when assessing the recoverability of deferred tax assets and if the Company intends to use these opportunities or it is probable that they will be utilised.

(iii) Measurement

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply to the years when the asset is realised or the liability is settled, based on tax rates and tax laws that have been enacted or substantially enacted. The tax consequences that would follow from the manner in which the Company expects to recover or settle the carrying amount of its assets or liabilities are also reflected in the measurement of deferred tax assets and liabilities.

(iv) Classification

Deferred tax assets and liabilities are recognised in the balance sheet under non-current assets or liabilities, irrespective of the expected date of recovery or settlement.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(l) Environmental issues

Expenses derived from environmental activities are recognised as other operating expenses in the period in which they are incurred.

Property, plant and equipment acquired by the Company for long-term use to minimise the environmental impact of its activity and protect and improve the environment, including the reduction and elimination of future pollution from the Company's activities, are recognised as assets applying the measurement, presentation and disclosure criteria described in section (b) Property, plant and equipment.

(m) Transactions between Group companies

Transactions between Group companies, except those related to business combinations and mergers mentioned in the previous sections, are recognised at the fair value of the consideration given or received. The difference between this value and the amount agreed is recognised in line with the underlying economic substance of the transaction.

(5) Non-current Assets Held for Sale

(a) Assets and liabilities held for sale

At 31 December 2014 the Company reached an agreement with another gas distribution group, Redexis, to sell them their investment in the gas distributor Gas Energía Distribución Murcia, S.A.. A further agreement was reached with this group to sell to them the physical gas distribution assets located outside the autonomous regions of Asturias, Cantabria and the Basque Country.

Consequently, at the 2014 year end, the Group had classified the assets and liabilities included in these agreements as held for sale.

Details of assets and liabilities held for sale and recognised income and expense in relation to the gas distribution assets located outside the autonomous regions of Asturias, Cantabria and the Basque Country are as follows:

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

	Thousands of Euros
<i>Assets held for sale:</i>	
Equity instruments in Group companies	9,332
Technical installations and machinery	37,472
Other property, plant and equipment	2,166
Under construction	326
Goodwill	4,703
Other intangible assets	1,431
Other current financial assets	63,372
Total assets	118,802
<i>Liabilities directly associated with non-current assets held for sale:</i>	
Capital grants	2,251
Total liabilities	2,251
Recognised income and expense	-

These agreements were subject to a number of conditions precedent, including the approval of the Spanish National Markets and Competition Commission. The sale-purchase transaction was not recognised at 31 December 2014 as not all of the conditions precedent had been met at that date.

Lastly, on 30 January 2015, the section of the sale agreement relating to the shares of Gas Energía Distribución Murcia, S.A. was concluded. The price for the 99.98% interest held by the Company, including its debt, was set at Euros 190 million.

As regards the sale of the physical gas distribution assets located outside the autonomous regions of Asturias, Cantabria and the Basque Country, this transaction was completed in June 2015 at a selling price of Euros 51 million.

An overall gain of Euros 125 million was generated on this transaction (see note 23 (d)).

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(6) Intangible Assets

Details of intangible assets, excluding goodwill, and movement are as follows:

	Thousands of Euros		
	Patents, licence	Computer software	Total
2015			
Cost at 1 January 2015	41,692	11,477	53,169
Additions	-	52	52
Cost at 31 December 2015	41,692	11,529	53,221
Accumulated amortisation at 1 January 2015	(3,421)	(10,836)	(14,257)
Amortisation	-	(418)	(418)
Accumulated amortisation at 31 December 2015	(3,421)	(11,254)	(14,675)
Carrying amount at 31 December 2015	38,271	275	38,546
	Thousands of Euros		
	Patents, licence	Computer software	Total
2014			
Cost at 1 January 2014	43,235	11,446	54,681
Additions	-	31	31
Transfers from assets held for sale	(1,543)	-	(1,543)
Cost at 31 December 2014	41,692	11,477	53,169
Accumulated amortisation at 1 January 2014	(3,533)	(9,958)	(13,491)
Amortisation	-	(878)	(878)
Transfers from assets held for sale	112	-	112
Accumulated amortisation at 31 December 2014	(3,421)	(10,836)	(14,257)
Carrying amount at 31 December 2014	38,271	641	38,912

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(a) General

Patents, licences, trademarks and similar rights reflect an intangible asset with an indefinite useful life related to gas supply points. In 2011, the Company reclassified the useful life of this asset from finite to indefinite.

Computer software includes the costs incurred in implementing SAP.

At 31 December 2015 and 2014 the Company has no commitments to acquire intangible assets.

(b) Goodwill and impairment of intangible assets

Details of goodwill and movement are as follows:

	Thousands of Euros	
	2015	2014
Cost at 1 January	366,674	371,377
Transfers to assets held for sale	-	(4,703)
Cost at 31 December	366,674	366,674
Accumulated impairment at 31 December	-	-
Carrying amount at 31 December	366,674	366,674

The balance of goodwill reflects the aggregated goodwill deriving from various merger processes, a summary of which is as follows:

Goodwill arising on the merger of Naturcorp Multiservicios, S.A.U., Sociedad de Gas de Euskadi, S.A., Donostigas, S.A.U., Gas de Asturias, S.A.U. and Gas Figueres, S.A.U., with and into Naturcorp I, S.A. (now Naturgas Energía Grupo, S.A.) in 2003. This goodwill was simultaneously contributed to Naturgas Energía Distribución, S.A.U. (formerly Naturcorp Redes, S.A.U.) which, having assumed the corresponding distribution activities, will generate the future cash flows to recover this goodwill. Details of these corporate transactions were included in the notes to the annual accounts for 2003.

At 31 December 2014 the goodwill allocated to Gas Figueres, S.A.U. was transferred to non-current assets held for sale following the agreement reached with Redexis Gas, S.A. (see note 5), which was executed in June 2015.

Goodwill arose on the merger of Naturcorp Participaciones, S.L., Gas Pasaia, S.A., Gas Hernani S.A., and Compañía Distribuidora de Gas de Bilbao-Bilboko Banaketarako Konpainia Bilbogas, S.A. with and into Naturgas Energía Distribución, S.A.U. in 2006. Details of these corporate transactions were included in the notes to the annual accounts for 2006.

Additional goodwill arose on the merger of Gas Natural de Alava, S.A.U. with and into Naturgas Energía Distribución, S.A.U. in 2007. Details of this corporate transaction were included in the notes to the annual accounts for 2007.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Furthermore, goodwill arose on the merger of Gas Mérida, S.A. with and into Naturgas Energía Distribución, S.A.U. carried out in 2008. Details of this corporate transaction were included in the notes to the annual accounts for 2008.

Lastly, in 2011 goodwill of Euros 10,766 thousand arose on the merger by absorption of Gas Energía Distribución Cantabria, S.A.U. Details of this corporate transaction were included in the notes to the annual accounts for 2011.

For impairment testing purposes, goodwill has been allocated in full to the Company's only CGU, namely the gas distribution CGU.

The Company tests goodwill for impairment on an annual basis. The calculation of the recoverable amount of a division to which goodwill has been allocated requires the use of estimates by management. The recoverable amount is the higher of fair value less costs to sell and value in use. The Company generally uses cash flow discounting methods to calculate these values. Discounted cash flow calculations are based on the business plan approved by management. The cash flows take into consideration past experience and represent management's best estimate of future market performance. From the fifth year cash flows are extrapolated using individual growth rates. The key assumptions employed when determining fair value less costs to sell and value in use include growth rates, the weighted average cost of capital and tax rates. The estimates, including the methodology used, could have a significant impact on values and impairment. Cash flows beyond this five-year period are extrapolated using the estimated growth rates indicated below. The growth rate should not exceed the average long-term growth rate for the gas distribution business in which the CGU operates.

	2015		2014
	Gas distribution	Total	Gas distribution
Gross margin (thousands of Euros)	107,732	107,732	216,463
Growth rate (%)	2	2	1
Discount rate (%)	4	4	5

Management determined the budgeted gross margins based on past experience and forecast market performance. The weighted average growth rates are consistent with the forecasts included in industry reports. The discount rates used are pre-tax values and reflect specific risks related to the CGU.

(c) Fully amortised assets

The cost of fully amortised intangible assets in use at 31 December 2015 and 2014 is Euros 10,694 thousand and Euros 10,036 thousand, respectively.

(7) Property, Plant and Equipment

Details of property, plant and equipment and movement during the year are shown in Appendix I.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(a) General

Additions to property, plant and equipment under construction in 2015 mostly comprise the Company's investments in new population centres, grid extensions and its own network for amounts of Euros 1,920 thousand, Euros 8,509 thousand and Euros 5,025 thousand, respectively (Euros 1,230 thousand, Euros 5,565 thousand and Euros 2,189 thousand in 2014, respectively). These additions also include an amount of Euros 5,247 thousand (Euros 4,920 thousand in 2014) that has been capitalised in connection with these investments and recognised under self-constructed assets in the income statement.

(b) Fully depreciated assets

Details of the cost of fully depreciated property, plant and equipment in use at 31 December are as follows:

	Thousands of Euros	
	2015	2014
Buildings	1,964	1,964
Technical installations and machinery	123,944	101,372
Other installations, equipment and furniture	33,629	53,273
Other property, plant and equipment	4,274	4,265
	163,811	160,874

(c) Government grants received

The construction of distribution networks has been partly financed by grants of Euros 335 thousand (Euros 517 thousand in 2014) (see note 15). The cost of these distribution networks amounted to Euros 504 thousand at 31 December 2015 (Euros 2,219 thousand in 2014).

(d) Commitments

At 31 December 2015 and 2014 the Company has no commitments to acquire significant items of property, plant and equipment.

(e) Insurance

The Company has taken out insurance policies to cover the risk of damage to its property, plant and equipment. The coverage of these policies is considered sufficient.

(f) Asset revaluations

At 1 January 2013 items of property, plant and equipment were revalued in accordance with Vizcaya Provincial Decree 11/2012 of 18 December 2012, which adopted tax measures aimed at consolidating public finances and boosting economic activity, with an effect of Euros 103,443 thousand. The effect of the revaluation on depreciation for 2015 amounts to Euros 10,335 thousand. At 31 December 2015 accumulated depreciation amounts to Euros 34,007 thousand.

The Company also revalued property, plant and equipment in 1990 and 1996, as permitted by Provincial Law 11/1990 of 21 December 1990, and Provincial Law 6/1996 of 21 November 1996, respectively.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

The amount recognised in the balance sheet at 31 December 2015 is Euros 38,001 thousand, depreciated by Euros 36,609 thousand (Euros 38,165 thousand, depreciated by Euros 36,129 thousand at 31 December 2014).

(8) Operating Leases – Lessor

The Company has primarily leased gas meters under operating leases to third parties.

The meter lease agreements are entered into upon contracting the gas supply and the lease payment is billed every two months, together with the gas supply bill. The lease has no expiry date and is terminated automatically when the gas supply is terminated, with no contingencies for the lessee.

(9) Risk Management Policy

(a) Financial risk factors

The Company's activity consists of gas distribution in Spain, thus it is not subject to currency risk, country risk, exchange rate insurance, etc. Furthermore, the Company does not have any loans or borrowings, or financial derivatives of any kind. Since 1 July 2008, following the change in regulation of the gas sector (see note 1), the Company has not carried out transactions with end customers, only with gas suppliers and other agents in the gas system.

The Company's activities are exposed to various financial risks: credit risk, liquidity risk and cash flow interest rate risk. The Company's global risk management programme focuses on uncertainty in the financial markets and aims to minimise potential adverse effects on the Company's profits.

Adaptation of the systems to the Company's risk profile is managed individually by specifically analysing each of the risks and their conditioning factors and taking into consideration their nature, origin, possibility and probability of occurrence and the significance of their impact. Management measures (hedges, mitigation, opportunity, etc.) that are viable for each risk are also considered.

Controls are based on the approval of management policies and include mechanisms to set and control operational limits, as well as authorisation and supervision processes, together with operational procedures.

(i) Credit risk

The Company is not exposed to significant credit risk as its main operations are carried out with EDP Comercializadora, S.A.U., which belongs to the group headed by Naturgas Energía Grupo, S.A. and acts as market agent, and with other, highly solvent suppliers operating in the gas sector.

(ii) Liquidity risk

Adverse situations in the debt markets may hinder the procurement of the financing required by the Company to conduct its business activities.

The liquidity policy adopted ensures that payment obligations are met through the arrangement of sufficient credit facilities and access to the credit facilities of the ultimate Parent, Naturgas Energía Grupo, S.A.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(10) Investments in Equity Instruments of Group Companies and Associates

Details of investments in equity instruments of Group companies and associates are as follows:

	Thousands of Euros	
	2015	2014
	Non-current	Non-current
Associates		
Equity investments	329	329
	329	329

At 31 December 2015 investments in equity instruments of Group companies reflect the 40% shareholding (Euros 260 thousand) in the associate Tolosa Gasa S.A. and the 12.5% shareholding (Euros 69 thousand) in the associate Inkolan A.I.E.

- (a) Investments in Group companies and associates

Details of investments in Group companies and associates are provided in Appendix II.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(12) Investments and Trade Receivables

(a) Investments in Group companies and associates

Current investments in Group companies and associates reflect other financial assets and include the cash pooling balance of Euros 936,231 thousand receivable from the sole shareholder at 31 December 2015 (Euros 575,270 thousand in 2014). This cash pooling account accrues variable interest at market rates. The rest of this balance reflects current accounts with other Group companies.

At 31 December 2014 the Company reclassified the cash pooling account with Gas Energía Distribución Murcia, S.A. totalling Euros 63,372 thousand to non-current assets held for sale, in accordance with the agreement reached with Redexis Gas, S.A. (see note 5). This account accrued interest at variable market rates.

(b) Investments

Details of investments are as follows:

	Thousands of Euros			
	2015		2014	
	Non-current	Current	Non-current	Current
Unrelated parties				
Equity instruments	-	-	2	-
Receivables	69,000	-	-	-
Security and other deposits	517	115	528	124
Total	69,517	115	530	124

Equity instruments reflect the Company's interest in Oficina de Cambios de Suministrador, as required under Law 12/2007 of 2 July 2007.

Non-current security and other deposits have no established expiry date.

At 31 December 2015 non-current receivables amount to Euros 69 million in relation to gas sector deficits pending collection (see note 1 (c)).

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(c) Trade and other receivables

Details of trade and other receivables are as follows:

	Thousands of Euros	
	2015	2014
	Current	Current
<i>Group (note 22)</i>		
Trade receivables	32,212	90,811
Other receivables	-	2,651
<i>Associates (note 22)</i>		
Trade receivables	1,555	1,299
<i>Unrelated parties</i>		
Trade receivables	8,152	4,256
Other receivables	6,452	34,534
Personnel	149	181
Public entities, other (note 22)	1	-
Impairment	(20)	(641)
Total	48,501	133,091

At 31 December 2015 and 2014 other receivables from unrelated parties include the amount pending collection from the Ministry of Industry, Energy and Tourism for the gas sector intercompany settlements, reflecting the estimated current cumulative deficit corresponding to the 15/2014 settlement (see note 1 (c)) and the cumulative deficit corresponding to the 14/2013 settlement, respectively, attributable to the Company, totalling Euros 1,000 thousand and Euros 20,214 thousand, respectively.

Other Group receivables at 31 December 2015 include a balance of Euros 720 thousand receivable from EDP Gas Iberia, S.L.U. (parent of the tax group) for value added tax, as the Company files consolidated tax returns for this tax (Euros 1,253 thousand receivable from EDP Gas Iberia, S.L.U. at 31 December 2014).

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(d) Impairment

An analysis of the changes in allowance accounts related to impairment of financial assets measured at amortised cost due to credit risk is as follows:

	Thousands of Euros	
	2015	
	Trade	Total
	receivables	Total
<i>Current</i>		
Balance at 1 January	(641)	(641)
Reversals	621	621
Balance at 31 December	(20)	(20)
	Thousands of Euros	
	2014	
	Trade	Total
	receivables	Total
<i>Current</i>		
Balance at 1 January	(998)	(998)
Reversals	13	13
Eliminations against the accounting balance	344	344
Balance at 31 December	(641)	(641)

In 2015 the Company wrote off bad debt amounting to Euros 623 thousand.

(13) Inventories

Details of inventories are as follows:

	Thousands of Euros	
	2015	2014
Production and distribution business		
Propane gas inventories in tanks	72	72
Advances of fixed assets	70	46
	142	118

(14) Equity

Details of equity and movement during the year are shown in the statement of changes in equity.

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(a) Capital

At 31 December 2015 and 2014 the Company's share capital is represented by 1,000,000 registered shares of Euros 100 par value each, subscribed and fully paid. All shares have the same voting and profit sharing rights.

These shares are freely transferable.

At 31 December 2015 and 2014 the sole shareholder of the Company is Naturgas Energía Grupo S.A., thus the Company is solely owned and is entered as such on the Mercantile Register. Transactions with the sole shareholder are detailed in note 22.

The Company holds a management services agreement with its sole shareholder.

(b) Share premium

This reserve is freely distributable.

(c) Reserves

Details of reserves and profit, and movement during the period, are shown in Appendix III.

(i) Legal reserve

The legal reserve has been appropriated in compliance with article 274 of the Spanish Companies Act, which requires that companies transfer 10% of profits for the year to a legal reserve until this reserve reaches an amount equal to 20% of share capital.

The legal reserve is not distributable to shareholders and if it is used to offset losses, in the event that no other reserves are available, the reserve must be replenished with future profits.

At 31 December 2015, the Company has appropriated to this reserve the minimum amount required by law.

(ii) Revaluation reserves

Revaluation reserves comprise the reserve permitted by Vizcaya Provincial Decree 11/2012.

In accordance with Vizcaya Provincial Decree 11/2012 of 18 December 2012, which introduced several tax measures to consolidate public finances and boost economic activity, the Company revalued its property, plant and equipment, effective from 1 January 2013. The revaluation amounted to Euros 98,272 thousand, net of the 5% capital gains tax, which totalled Euros 5,172 thousand.

The revaluation is open to inspection by the Spanish taxation authorities for a three-year period from the date of filing the 2012 income tax return. Once the balance has been inspected and agreed, or the three-year period has elapsed, it may be used to offset losses or increase the Company's capital. Once a period of ten years has elapsed this balance may be released to freely distributable reserves.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

The balance of this account will only be distributable, either directly or indirectly, to the extent that gains have been realised. The gain will be deemed to have been realised to the extent that the revalued assets have been depreciated, transferred or derecognised.

(iii) Goodwill reserve

The goodwill reserve has been appropriated in compliance with article 273.4 of the Spanish Companies Act, which requires companies to transfer profits equivalent to at least 5% of goodwill to a non-distributable reserve until this reserve reaches an amount equal to recognised goodwill. In the absence of profit, or if profit is insufficient, freely distributable reserves should be used.

(ii) Production investment reserve

As permitted by Provincial Law 24/1996 of 5 July 1996, in 2012, 2011 and 2010 the Company created a special reserve for production investment with appropriations of Euros 18,000 thousand, Euros 30,000 thousand and Euros 25,000 thousand, respectively.

The production investment reserve will be restricted to the extent that the assets invested in should continue to be used for the Company's activity.

(v) Voluntary reserves

These reserves are freely distributable.

(15) Grants, Donations and Bequests Received

Movement in non-refundable grants, donations and bequests received is as follows:

	Thousands of Euros	
	2015	2014
Balance at 1 January	39,015	41,401
Additions	1,282	1,804
Disposals	(12)	(19)
Amounts transferred to the income statement	(2,503)	(2,550)
Transfers to liabilities associated with non-current assets held for sale	(12)	(1,621)
Balance at 31 December	37,770	39,015

Grants, donations and bequests include capital grants, connection and extension charges, and other deferred income (see note 4 (h)).

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Details of the amounts recognised in the income statement by type of grant are as follows:

	Thousands of Euros	
	2015	2014
Capital grants	1,374	1,370
Connection and extension charges	1,709	1,775
Other deferred income	204	204
	3,287	3,349

(a) Grants

(i) Details of main capital grants

Grantor	Thousands of Euros		Purpose	Grant date
	2015	2014		
European Economic Community	1,226	1,446		
Principality of Asturias	8,977	10,427		
Basque Government	2,837	2,933		
	13,040	14,806		

(16) Other Provisions

Movement in other provisions is as follows:

	Thousands of Euros	
	Provisor	Total
At 1 January 2015	503	503
Charges	54	54
Reversals	(281)	(281)
Payments	6	6
Other	(12)	(12)
At 31 December 2015	270	270

(a) Provision for other liabilities

The provision for other liabilities includes the estimated amounts required to cover probable liabilities arising from claims or other obligations deriving from the Company's activity.

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

- (b) Commitments undertaken with third parties

Guarantees provided to third parties (local councils and other public entities) at 31 December 2015 total Euros 8,965 thousand (Euros 11,186 thousand in 2014), whereas guarantees received from suppliers amount to Euros 7,228 thousand (Euros 7,205 thousand in 2014).

Guarantees provided to local councils and other public entities are for the use and replacement of public assets affected by construction work for gas pipelines and distribution networks. No losses are expected in respect of these guarantees.

(17) Financial Liabilities by Category

- (a) Classification of financial liabilities by category

A classification of financial liabilities by category and class is presented in Appendix IV.

The carrying amount of financial liabilities carried at amortised cost does not differ significantly from their fair value.

Net losses and gains on financial liabilities at 31 December 2015 and 2014 amount to Euros 72 thousand and Euros 99 thousand, respectively, and comprise borrowing costs on debts and payables at amortised cost.

(18) Payables and Trade Payables

- (a) Group companies and associates

Current payables to Group companies and associates at 31 December 2015 reflect the balances of the current accounts held with Group companies.

- (b) Payables

Details of payables are as follows:

	Thousands of Euros			
	2015		2014	
	Non-current	Current	Non-current	Current
<i>Unrelated parties</i>				
Suppliers of fixed assets	-	3,573	-	2,677
Payables	959	142	962	139
Dividends payable	-	19	-	19
Security and other deposits received	778	112	781	112
Other	-	-	-	6
Total	1,737	3,846	1,743	2,953

Non-current payables reflect interest-free loans from public entities at amortised cost.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(c) Trade and other payables

Details of trade and other payables are as follows:

	Thousands of Euros	
	2015	2014
	Current	Current
<i>Group (note 22)</i>		
Suppliers	-	6,031
Payables	-	23,135
<i>Associates</i>		
Payables	429	98
<i>Unrelated parties</i>		
Suppliers	-	104
Payables	84,054	6,268
Personnel	2,832	1,621
Public entities, other	3,910	3,808
Total	91,225	41,065

Payables to unrelated parties include a balance of Euros 55,631 thousand in respect of gas sector intercompany settlements, reflecting the estimate at 31 December 2015 of the amount that corresponds to the Company in the pertinent settlement period, based on the authorised costs for distribution activities, in order to adjust operating profit to the remuneration calculated by the Ministry of Industry, Energy and Tourism pursuant to the regulations applicable to the gas sector (Euros 2,404 thousand at 31 December 2014).

The Company has estimated its settlements for 2015 and 2014 based on a comparison between the sales made in each year, less other related costs, and the accrued balance at 31 December 2015 and 2014 of the Company's authorised costs, calculated based on the distribution of total allocated fixed remuneration for 2015 and 2014, distributed proportionally.

Group payables at 31 December 2015 include income tax of Euros 21,355 thousand payable to EDP Gas Iberia, S.L.U. (parent of the tax group) (Euros 18,235 thousand at 31 December 2014), as a result of filing consolidated tax returns (see note 4 (k)).

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(19) Average Supplier Payment Period "Reporting Requirement". Third Additional Provision of Law 15/2010 of 5 July 2010

Details of the average supplier payment period are as follows:

	Days
Average supplier payment period	19
Transactions paid ratio	19
Transactions payable ratio	13
	Amount in Euros
Total payments made	54,903
Total payments outstanding	6,476

(20) Taxation

Details of balances with public entities are as follows:

	Thousands of Euros			
	2015		2014	
	Non-current	Current	Non-current	Current
Assets				
Deferred tax assets	8,438	-	10,271	-
Value added tax and similar taxes (note 13)	-	1	-	-
	8,438	1	10,271	-
Liabilities				
Deferred tax liabilities	200,895	-	200,758	-
Value added tax and similar taxes (note 18)	-	-	-	31
Social Security (note 18)	-	248	-	266
Withholdings and charges (note 18)	-	3,662	-	3,511
	200,895	3,910	200,758	3,808

At 31 December 2015 and 2014 withholdings and charges include Euros 3,346 thousand and Euros 3,146 thousand, respectively, of charges for the use of subsoil.

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

The Company has the following main applicable taxes open to inspection by the Spanish taxation authorities:

Tax	<u>Years open to inspection</u>
Income tax	2011-2014
Value added tax	2012-2015
Personal income tax	2012-2015

Income tax returns must be filed within 25 calendar days after the six months subsequent to the conclusion of the tax period. Consequently, income tax for 2015 will not be open to inspection until 25 July 2016.

The Company files consolidated VAT returns with the following companies: EDP Gas Iberia, S.L.U. (parent of the tax group), Naturgas Energía Servicios, S.A.U., Naturgas Energía Grupo, S.A. and EDP Comercializadora, S.A.U.

(a) Income tax

The Company files consolidated tax returns as indicated in note 4 (k).

A reconciliation of net income and expenses for the year with the taxable income is provided in Appendix V.

Details of the income tax expense related to profit for the year are shown in Appendix VI.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Details of the income tax expense are as follows:

	Thousands of Euros	
	2015	2014
Current income tax		
Present year	21,539	19,379
Prior year adjustments	60	228
Previously unrecognised tax deductions applied	(117)	(182)
Previously capitalised tax deductions applied	(27)	(874)
	21,455	18,551
Deferred tax		
Source and reversal of temporary differences		
Property, plant and equipment	8,584	10,048
Goodwill	(1,453)	376
Other intangible assets	1,049	1,390
Provisions	5	263
Other	(10)	18
Previously capitalised tax deductions applied during the year	27	874
	29,65	31,52

In accordance with Vizcaya Provincial Decree 11/2012 of 18 December 2012 on asset revaluations, depreciation resulting from the revaluation of property, plant and equipment in 2013 and 2014 was not tax deductible until 2015. In this regard, at 31 December 2015 the Company reversed a deferred tax asset of Euros 2,399 thousand and recognised a deferred tax asset totalling Euros 4,450 thousand (Euros 6,849 thousand at 31 December 2014).

Taxable temporary differences associated with property, plant and equipment are mostly due to the accelerated depreciation taken on certain fixed assets, as approved by the corresponding taxation authorities.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Details of deferred tax assets and liabilities by type of asset and liability are as follows:

	Thousands of Euros			
	Assets		Liabilities	
	2015	2014	2015	2014
Property, plant and equipment	4,588	6,983	(76,074)	(75,195)
Goodwill	-	-	(102,665)	(103,756)
Other intangible assets	-	-	(9,109)	(8,060)
Connection charges up to 31 December 2007	1,911	2,039	-	-
Connection charges since 1 January 2008	-	-	(875)	(924)
Capital grants	-	-	(11,131)	(11,385)
Provisions	37	42	-	-
Other	3	24	(1,041)	(1,438)
Rights to tax deductions and credits	1,898	1,183	-	-
Total assets/liabilities	8,437	10,271	(200,895)	(200,758)

Details of deferred tax assets and liabilities that are expected to be realised or reversed in periods exceeding 12 months are as follows:

	Thousands of Euros	
	2015	2014
Deferred tax assets relating to temporary differences	5,396	5,165
Rights to tax deductions and credits	1,899	1,000
Total assets	7,295	6,165
Deferred tax liabilities	196,267	200,000
Net	(188,972)	(193,835)

The Company has recognised deductions relating to investment as deferred tax assets, the amounts of which are as follows:

Year	Thousands of Euros		Final year
	2015	2014	
2009	814	98	
2010	316	316	
2011	205	205	
2012	517	517	
2013	47	47	
	1,899	1,183	

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Provincial Corporate Income Tax Law 11/2013, of 5 December 2013, was approved as effective from 1 January 2014 and restricts the offsetting of tax loss carryforwards and the use of tax deductions to 15 years from the law's entry into force.

(21) Environmental Information

The very nature of the Company's activity, the distribution of natural gas as a substitute for oil and coal derivatives, which are more polluting due to the effects of combustion, helps to improve the environment and provides greater thermal efficiency that promotes energy efficiency and therefore savings.

Natural gas contributes to improving the environment as it reduces the emission of greenhouse gases and causes less air pollution since its composition (90% methane) generates less CO₂ during combustion. Furthermore, natural gas contains practically no sulphur.

Throughout 2015 the Company has continued its efforts to coordinate environmental safety in gas distribution works, having expanded this action to network maintenance work, including periodic visits. In accordance with the environmental procedures of the integrated management system, noise levels are measured at the distribution regulation and metering stations, the location of which makes them susceptible to exceeding the permitted limits.

The Company has received no environmental grants or income from activities related to the environment in 2015 or 2014.

As a result of the aforementioned actions undertaken by the Company, the Directors consider that any contingencies that could arise from environmental issues, which are very unlikely, are sufficiently covered by their civil liability insurance policies.

(22) Related Party Balances and Transactions

(a) Related party balances

Balances receivable from and payable to Group companies, associates and related parties, and the main details of these balances, are disclosed in notes 10, 12 and 18.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

Details of balances by category are as follows:

	Thousands of Euros			
	Sole shareholder	Group companies	Associates	Total
2015				
Non-current investments in Group companies and associates				
Equity instruments	-	-	329	329
Loans to companies	-	-	13	13
Total non-current assets	-	-	342	342
Trade and other receivables				
Trade receivables, current	-	32,212	1,555	33,767
Current investments in Group companies and associates				
Other financial assets	936,231	-	-	936,231
Total current assets	936,231	32,212	1,555	969,998
Total assets	936,231	32,212	1,897	970,340
Group companies and associates, current	-	1	-	1
Trade and other payables				
Suppliers, Group companies and associates, current	-	2,861	429	3,290
Other payables	-	21,355	-	21,355
Total current liabilities	-	24,217	429	24,646
Total liabilities	-	24,217	429	24,646

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

	Thousands of Euros			
2014	Sole shareholder	Group companies	Associates	Total
Non-current investments in Group companies and associates				
Equity instruments	-	-	329	329
Loans to companies	-	-	25	25
Total non-current assets	-	-	354	354
Non-current assets held for sale	-	72,704	-	72,704
Trade and other receivables				
Trade receivables, current	-	90,811	1,299	92,110
Other receivables	635	2,016	-	2,651
Current investments in Group companies and associates				
Other financial assets	575,270	6	-	575,276
Total current assets	575,905	165,537	1,299	742,741
Total assets	575,905	165,537	1,653	743,095
Group companies and associates, current	50	2	-	52
Trade and other payables				
Suppliers	6,031	-	-	6,031
Other payables	2,151	20,984	98	23,233
Total current liabilities	8,232	20,986	98	29,316
Total liabilities	8,232	20,986	98	29,316

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(b) Related party transactions

The Company's transactions with related parties are as follows:

	Thousands of Euros			Total
	Sole shareholder	Group companies	Associates	
2015				
Income				
Net sales				
Sales	-	137,778	8,428	146,206
Services rendered	-	19,062	1,404	20,466
Other services rendered	-	14	306	320
Financial instruments				
Finance income	1,377	263	-	1,640
Dividends	-	-	126	126
Total revenues	1,377	157,117	10,264	168,758
Expenses				
Other services received	9,297	9,635	1,910	20,842
Total expenses	9,297	9,635	1,910	20,842

	Thousands of Euros			Total
	Sole shareholder	Group companies	Associates	
2014				
Income				
Net sales				
Sales	-	135,145	8,370	143,515
Services rendered	-	20,372	1,661	22,033
Other services rendered	-	45	285	330
Financial instruments				
Finance income	2,971	525	-	3,496
Dividends	-	-	150	150
Total income	2,971	156,087	10,466	169,524
Expenses				
Other services received	13,550	4,699	8,131	26,380
Total expenses	13,550	4,699	8,131	26,380

(c) Information on the Company's Directors and senior management personnel

In 2015 and 2014 the Company's Directors and senior management accrued remuneration of Euros 223 thousand and Euros 214 thousand, respectively, and Euros 29 thousand and Euros 34 thousand, respectively, were receivable from them in respect of advances. The Company has not extended any guarantees on their behalf. The Company has no pension or life insurance obligations with its former or current directors.

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

- (d) Conflicts of interest concerning the directors

The Directors of the Company and their related parties have had no conflicts of interest requiring disclosure in accordance with article 229 of the Revised Spanish Companies Act.

(23) Income and Expenses

- (a) Revenues

Details of revenues by category of activity and geographical market are as follows:

	Thousands of Euros	
	Domestic	
	2015	2014
Revenue from the sale of propane gas	230	400
Revenue from installations	3	3
Revenue from regulated activities	174,995	178,522
Charges	(1,395)	(1,478)
Revenue from the rendering of services	28,982	29,827
	202,815	207,274

Revenue from regulated activities comprises the amount accrued in 2015 for regulated remuneration for gas distribution companies.

Charges at 31 December 2015 reflect the charge levied by the National Markets and Competition Commission (CNMC) and the payment to the system technical manager, totalling Euros 375 thousand and Euros 1,020 thousand, respectively (Euros 390 thousand and Euros 1,089 thousand, respectively, at 31 December 2014).

- (b) Supplies

At 31 December 2015 and 2014 subcontracted work comprises periodic inspections subcontracted to third parties.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

(c) Employee benefits expense

Details of employee benefits expense are as follows:

	Thousands of Euros	
	2015	2014
Employee benefits expense		
Social Security payable by the Company	2,367	2,390
Pension plan contributions	311	313
Other employee benefits expenses	259	322
	2,937	3,025

The Company has a defined contribution pension plan arranged through an insurance policy.

(d) Gains/losses on disposal of fixed assets

Details of gains and losses on the disposal of fixed assets are as follows:

	Thousands of Euros	
	2015	2014
Gains		
Property, plant and equipment	125,464	54
Losses		
Property, plant and equipment	61	(86)
	125,403	(32)

(24) Employee Information

The average headcount of the Company in 2015 and 2014, distributed by category, is as follows.

	Number	
	2015	2014
Directors	6	6
Managers	28	24
Other	136	145
	170	175

(Continued)

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Notes to the Annual Accounts

At 2015 and 2014 year end the distribution by gender of Company personnel and the members of the board of directors is as follows:

	Number			
	2015		2014	
	Female	Male	Female	Male
Directors	-	3	-	3
Management	-	6	-	6
Other	36	122	37	132
	36	131	37	141

(25) Audit Fees

The auditor of the Company's annual accounts has invoiced net fees for audit services of Euros 49 thousand and Euros 50 thousand during the years ended 31 December 2015 and 2014, respectively.

The amounts detailed above include the total fees for services rendered in 2015 and 2014, irrespective of the date of invoice.

(26) Events after the Reporting Period

No significant events have occurred since the 2015 reporting date that require disclosure in these annual accounts, other than the sale-purchase agreement entered into on 25 January 2016 by the Group company Naturgas Energía Distribución, S.A.U. and Repsol Butano, S.A. for the liquefied petroleum gas facilities owned by Repsol Butano, S.A. in Asturias, Cantabria and the Basque Country, for approximately Euros 116 million. This agreement is subject to compliance with certain conditions precedent, which are expected to be met during 2016.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Details of Property, Plant and Equipment and Movement
for the year ended 31 December 2015

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

Thousands of Euros

2015	Land	Buildings	Technical installations	Other installations	Under construction and advances	Other property, plant and equipment	Total
Cost at 1 January 2015	3,434	11,648	1,016,261	110,839	6,542	6,858	1,155,582
Additions	-	-	74	1,804	16,784	367	19,029
Disposals	-	(25)	(6)	(23,235)	(96)	(208)	(23,570)
Transfers	-	-	17,851	16	(17,867)	-	-
Transfers to assets held for sale	-	-	(131)	(135)	(204)	-	(470)
Cost at 31 December 2015	3,434	11,623	1,034,049	89,289	5,159	7,017	1,150,571
Accumulated depreciation at 1 January 2015	-	(4,142)	(538,836)	(82,854)	-	(5,282)	(631,114)
Depreciation	-	(302)	(45,186)	(4,726)	-	(286)	(50,500)
Disposals	-	9	(2)	23,231	-	209	23,447
Accumulated depreciation at 31 December 2015	-	(4,435)	(584,024)	(64,349)	-	(5,359)	(658,167)
Carrying amount at 31 December 2015	3,434	7,188	450,025	24,940	5,159	1,658	492,404

This appendix forms an integral part of note 7 to the annual accounts, in conjunction with which it should be read.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Details of Property, Plant and Equipment and Movement
for the year ended 31 December 2014

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

Thousands of Euros

2014	Land	Buildings	Technical instal	Other installatic	Under construc	Other property, plant and equipment	Total
Cost at 1 January 2014	3,078	11,321	1,050,742	111,781	11,919	6,803	1,195,644
Additions	356	327	26	2,558	13,795	55	17,117
Disposals due to spin-offs or contributions	-	-	(244)	(2)	-	-	(246)
Transfers to assets held for sale	-	-	17,786	1,060	(18,846)	-	-
Transfers from assets held for sale	-	-	(52,049)	(4,558)	(326)	-	(56,933)
Cost at 31 December 2014	3,434	11,648	1,016,261	110,839	6,542	6,858	1,155,582
Accumulated depreciation at 1 January 2014	-	(3,845)	(504,534)	(79,976)	-	(4,817)	(593,172)
Depreciation	-	(297)	(48,929)	(5,271)	-	(465)	(54,962)
Disposals	-	-	50	1	-	-	51
Transfers from assets held for sale	-	-	14,577	2,392	-	-	16,969
Accumulated depreciation at 31 December 2014	-	(4,142)	(538,836)	(82,854)	-	(5,282)	(631,114)
Carrying amount at 31 December 2014	3,434	7,506	477,425	27,985	6,542	1,576	524,468

This appendix forms an integral part of note 7 to the annual accounts, in conjunction with which it should be read.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Information Relating to Group Companies and Associates
for the year ended 31 December 2015

(Expressed in thousands of Euros)

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

Name	Registered office	Activity	% ownership	Capital	Reserves	Other €	Profit/(loss)	Total equity	Carrying am	Dividends received 2015
Inkolan, A.I.E.	Bilbao (Vizcaya)		12.50	96	71	107	250	524	69	-
Tolosa Gasa, S.A.	Tolosa (Guipuzcúa)	Supply and disti	40.00	651	346	21	233	1,251	260	126
								1,775	329	126

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Information Relating to Group Companies and Associates
for the year ended 31 December 2014

(Expressed in thousands of Euros)

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

Name	Registered office	Activity	% ownership	Capital	Reserves	Other €	Profit/(loss)	Total equity		Dividends received 2014
								Carrying am		
Inkolan, A.I.E.	Bilbao (Vizcaya)		12.50	96	112	12	66	286	69	-
Tolosa Gasa, S.A.	Tolosa (Guipuzcúa)	Supply and disti	40.00	651	346	4	316	1,317	260	150
								1,603	329	150

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Details of Reserves and Profits and Movement
for the year ended 31 December 2015

(Expressed in thousands of Euros)

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

	Legal and statutory reserve	Revaluation reserves	Goodwill reserve	Redeemed capital reserve	Voluntary reserves	Profit for the year	Total
Balance at 31 December 2014	20,000	98,272	109,798	73,000	129,431	80,872	511,373
Profit for 2015	-	-	-	-	-	207,175	207,175
Distribution of profit for 2014							
Reserves	-	-	18,569	-	-	(18,569)	-
Dividends	-	-	-	-	-	(62,303)	(62,303)
Balance at 31 December 2015	20,000	98,272	128,367	73,000	129,431	207,175	656,245

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Details of Reserves and Profits and Movement
for the year ended 31 December 2014

(Expressed in thousands of Euros)

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

	Legal and statutory reserve	Revaluation reserves	Goodwill reserve	Redeemed capital reserve	Voluntary reserves	Profit for the year	Total
Balance at 31 December 2013	20,000	98,272	91,230	73,000	129,431	74,478	486,411
Profit for 2014	-	-	-	-	-	80,872	80,872
Distribution of profit for 2013							
Reserves	-	-	18,568	-	-	(18,568)	-
Dividends	-	-	-	-	-	(55,910)	(55,910)
Balance at 31 December 2014	20,000	98,272	109,798	73,000	129,431	80,872	511,373

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Details of Financial Liabilities by Category
for the year ended 31 December 2015

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

	Thousands of Euros			
	Non-current		Current	
	Carrying amount	Total	Carrying amount	Total
2015				
<i>Debts and payables</i>				
Security deposits	778	778	112	112
Other financial liabilities	959	959	3,735	3,735
Trade and other payables				
Payables	-	-	84,483	84,483
Other payables	-	-	2,832	2,832
Total financial liabilities	1,737	1,737	91,162	91,162

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Details of Financial Liabilities by Category
for the year ended 31 December 2014

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

	Thousands of Euros			
	Non-current		Current	
	Carrying amount	Total	Carrying amount	Total
2014				
<i>Debts and payables</i>				
Security deposits	781	781	112	112
Other financial liabilities	962	962	2,893	2,893
Trade and other payables				
Suppliers	-	-	6,135	6,135
Payables	-	-	29,501	29,501
Other payables	-	-	1,621	1,621
Total financial liabilities	1,743	1,743	40,262	40,262

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Reconciliation of Net Income and Expenses for the Year with Taxable Income
for the year ended 31 December 2015

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

2015	Thousands of Euros						Total
	Income statement			Income and expense recognised in equity			
	Increases	Decreases	Net	Increases	Decreases	Net	
Income and expenses for the period			207,135			(1,245)	205,890
Income tax			29,657			(307)	29,350
Profit before income tax			236,832				236,832
Permanent differences							
Individual company			-			-	
Temporary differences:							
Individual company							
originating in current year		27,235	(27,235)	1,552	-	1,552	(25,683)
originating in prior years	7,032	8,993	(1,961)		-		(1,961)
Taxable income			207,640			1,552	209,192

This appendix forms an integral part of note 20 to the annual accounts, in conjunction with which it should be read.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Reconciliation of Net Income and Expenses for the Year with Taxable Income
for the year ended 31 December 2014

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

2014	Thousands of Euros						Total
	Income statement			Income and expense recognised in equity			
	Increases	Decreases	Net	Increases	Decreases	Net	
Income and expenses for the period			80,872			(2,386)	78,486
Income tax			31,520			(751)	30,769
Profit before income tax			112,392				112,392
Permanent differences							
Individual company	17	1	16		-		16
Temporary differences:							
Individual company							
originating in current year	11,742	54,000	(42,258)	3,137	-	3,137	(39,121)
originating in prior years	537	1,475	(938)		-		(938)
Taxable income			69,212			3,137	72,349

This appendix forms an integral part of note 20 to the annual accounts, in conjunction with which it should be read.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

**Relationship between the tax expense and accounting profit
for the year ended 31 December 2015**

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

	Thousands of Euros		
	Gains and losses	Equity	Total
Income and expenses for the period before tax	236,832	(1,552)	235,280
Tax at 28%	66,313	(435)	65,878
Non-taxable income			
Exempt gains on the sale of shares in Gas Energía Distribución Murcia S.A	(31,759)		(31,759)
Exempt gains on sale of assets	(4,841)		(4,841)
Non-deductible expenses			
Other			
Prior year adjustments	60		60
Previously unrecognised tax deductions applied	111		(117)
Income from reversal of a reduction in deferred tax assets		128	128
Income tax expense			
Continuing operations	29,65	(307)	29,350

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

**Relationship between the tax expense and accounting profit
for the year ended 31 December 2014**

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

	Thousands of Euros		
	Gains and losses	Equity	Total
Income and expenses for the period before tax	112,392	(3,137)	109,255
Tax at 28%	31,470	(879)	30,591
Non-deductible expenses			
Other			
Prior year adjustments	228		228
Previously unrecognised tax deductions applied	(182)		(182)
Expense for reduction in deferred tax assets		128	128
Income tax expense			
Continuing operations	31,520	(751)	30,769

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Directors' Report

2015

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

1. Most significant events in 2015

In 2015 Naturgas Energía Distribución, S.A.U. continued its normal activity in the regulated market of the natural gas sector. This consists of the management of regulated distribution assets, including the promotion, development and construction of new infrastructure, as well as operating, maintenance and optimisation services.

The sale of the shares of Gas Energía Distribución Murcia, S.A. was concluded in January 2015. As regards the sale of gas distribution assets owned by Naturgas Energía Distribución, S.A.U. located outside the autonomous regions of Asturias, Cantabria and the Basque Country, this transaction was completed in June 2015. An overall gain of Euros 125 million was generated on this transaction.

The Company continued its network expansion activity within its areas of influence. The following noteworthy initiatives were carried out in these areas in 2015:

- Naturgas Energía Distribución continued to expand its networks in the Basque Country, Asturias and Cantabria.
- The Laguardia municipality (Álava) made the switch to natural gas.
- The Gijón medium pressure B (MPB) network was connected to the Enagas Musel-Llanera basic transmission pipeline, leading to improvements in the quality and security of the supply to Gijón, Carreño and Gozón.
- The first two stages of the project to upgrade the low pressure network in Santander, so as to improve the gas supply, were completed and connected.
- Work was carried out in coordination with the local city council to renew the cast-iron networks in San Sebastian, with the aim of replacing infrastructure in the areas affected by the town paving plan in 2015. As part of this project, infrastructure has been replaced on the Aldapeta slope, Avenida Zurriola (San Sebastian) and the MPB branch, which has allowed for the Kursaal auditorium to switch from a low pressure (BP) supply to MPB, thereby improving the quality of supply to the area.
- An agreement was signed by Seat-Volkswagen-Audi España, EDP Empresa de Servicios Energéticos, S.L. and NED to promote natural gas vehicles within Spain.
- Investments totalling Euros 13 million were made to extend the distribution network by 38 kilometres, to achieve a total length of 7,715 kilometres at 31 December 2015 (following the sale of the assets located outside Asturias, Cantabria and the Basque Country), accounting for 9.2% with respect to the sector in Spain as a whole.
- The investments in new networks and the saturation of points of supply in existing networks have led to the creation of a further 8,094 points of supply, bringing the total to 917,846, following the sale of 25,239 points of supply. Power totalling 27,093 GWh was distributed through the networks.

Operating profit of Euros 235 million was generated in 2015 after amortisation/depreciation charges of Euros 50.9 million. Net profit for the year, taking into account net finance income, other income and expenses and income tax, totalled Euros 207.2 million.

2015 was characterised by a number of important legislative changes affecting the gas sector, specifically the amendments to the Hydrocarbon Industry Law through Law 8/2015, regulating, inter alia, the bases for the creation of the organised gas market and the opening-up to other market agents of periodic gas tank inspections, which were previously the sole responsibility of the distributors.

- Ministry of Industry, Energy and Tourism Order IET/2445/2014 of 19 December 2014, establishing the tolls and charges for third-party access to gas facilities and the remuneration for regulated activities in 2015.
- Law 2/2015 of 30 March 2015 on the de-indexation of the Spanish economy.
- Law 8/2015 of 21 May 2015, amending Hydrocarbon Industry Law 34/1998 of 7 October 1998 and regulating certain tax and non-tax measures relating to the exploration, investigation and exploitation of hydrocarbons.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Directors' Report

2015

- Spanish National Markets and Competition Commission (CNMC) Circular 2/2015 of 22 July 2015 establishing the balancing rules for the gas transmission network.
- Royal Decree 984/2015 of 30 October 2015, regulating the organised gas market and third-party access to natural gas system facilities.
- The resolution of 16 October 2015 of the Spanish National Markets and Competition Commission (CNMC) publishing the list of main operators in the energy sectors, announced in the Official State Gazette (BOE) on 14 November 2015.
- The resolution of 1 October 2015 of the Spanish National Markets and Competition Commission (CNMC) publishing the list of dominant operators in the energy sectors, announced in the Official State Gazette (BOE) on 14 November 2015.
- Royal Decree 1085/2015 of 4 December 2015 on the fostering of bio-fuels, which includes amendments to articles of RD 1434/2002.

2. Outlook

The Company's outlook is based on the following:

- Continued investment in the construction of new distribution networks in new population centres and expansion of current distribution networks to saturate the catchment areas.
- Continuous improvement of quality and security of supply. Development of a very efficient operational system entailing a high level of responsibility and based on excellence in terms of operations, inspection and maintenance.
- Anticipation of risks and efficient regulatory management, which are fundamental given the nature of Naturgas' results.

3. Research and development activities

In 2015 the EDP Naturgas Energia Group continued its efforts to develop cutting-edge projects and take part in the leading forums. It maintained an active presence in the following R&D&i forums:

- Programme Committee F (R&D&i) of INTERNATIONAL GAS UNION (IGU). Committee meetings in Rio de Janeiro (Brazil) and Berlin (Germany).
- European Gas Research Group (GERG): The Group holds the position of vice-chairman. Board and plenary meeting in Warsaw (Poland) and Bruges (Belgium).
- European Gas Research Group (GERG): The Group actively participated in the GERG Strategy Group meetings held in Warwick (UK).
- Energy Cooperative Research Centre (CIC energiGUNE): The Group is a trustee. Meetings in Parque Tecnológico de Miñano (Álava).
- 26th World Gas Conference (WGC PARIS 2015) in Paris (France). Active participation: One speech given on the European LIFE BIOGRID project.
- Presentation of the eight "Aula EDP NATURGAS ENERGIA" projects developed in 2014-15.
- Public presentation of the five "Aula EDP NATURGAS ENERGIA" projects proposed for development in 2015-16.

The following noteworthy projects were carried out in 2015:

- Project GAITEK METACO2: Research project with the TECNALIA foundation "NEW REACTOR FOR METHANE PRODUCTION FROM CO₂ AND ITS INJECTION INTO POWER TO GAS SYSTEMS"

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Directors' Report

2015

- Project GAITEK BIOHYSIS: Research project with the TECNALIA foundation and the company NOVARGI; "FLEXIBLE ADAPTABLE HYBRID BIOGAS SYSTEM TO INJECT BIOGAS INTO THE NATURAL GAS NETWORK".
- Project CIEN SMART GREEN GAS: Research project with the TECNALIA foundation and six other companies; "Energy recovery from residuals and effluent (SMART GREEN GAS)" Strategic programme of the National Business Research Consortium (CIEN) of the Spanish Centre for the Development of Industrial Technology (CDTI) and the Ministry of Economy and Competitiveness (2014-18).
- Project RETOS RENOGAS: Research project being carried out in 2015, 2016 and 2017 with the Bilbao Higher Engineering Technical College (UPV-EHU); "Process for generating methane in remote areas from renewable electricity". This is an R&D project co-financed through the RETOS INVESTIGACIÓN programme of the General Directorate for Scientific and Technical Research of the Ministry of Economy and Competitiveness. In 2015 the EDP Naturgas Energia Group continued its efforts to develop cutting-edge projects and take part in the leading forums. It maintained an active presence in the following R&D&i forums:
 - Programme Committee F (R&D&i) of INTERNATIONAL GAS UNION (IGU). Committee meetings in Rio de Janeiro (Brazil) and Berlin (Germany).
 - European Gas Research Group (GERG): The Group holds the position of vice-chairman. Board and plenary meeting in Warsaw (Poland) and Bruges (Belgium).
 - European Gas Research Group (GERG): The Group actively participated in the GERG Strategy Group meetings held in Warwick (UK).
 - Energy Cooperative Research Centre (CIC energiGUNE): The Group is a trustee. Meetings in Parque Tecnológico de Miñano (Álava).
 - 26th World Gas Conference (WGC PARIS 2015) in Paris (France). Active participation: One speech given on the European LIFE BIOGRID project.
 - Presentation of the eight "Aula EDP NATURGAS ENERGIA" projects developed in 2014-15.
 - Public presentation of the five "Aula EDP NATURGAS ENERGIA" projects proposed for development in 2015-16.

The following noteworthy projects were carried out in 2015:

- Project GAITEK METACO2: Research project with the TECNALIA foundation "NEW REACTOR FOR METHANE PRODUCTION FROM CO₂ AND ITS INJECTION INTO POWER TO GAS SYSTEMS"
- Project GAITEK BIOHYSIS: Research project with the TECNALIA foundation and the company NOVARGI; "FLEXIBLE ADAPTABLE HYBRID BIOGAS SYSTEM TO INJECT BIOGAS INTO THE NATURAL GAS NETWORK".
- Project CIEN SMART GREEN GAS: Research project with the TECNALIA foundation and six other companies; "Energy recovery from residuals and effluent (SMART GREEN GAS)" Strategic programme of the National Business Research Consortium (CIEN) of the Spanish Centre for the Development of Industrial Technology (CDTI) and the Ministry of Economy and Competitiveness (2014-18).
- Project RETOS RENOGAS: Research project being carried out in 2015, 2016 and 2017 with the Bilbao Higher Engineering Technical College (UPV-EHU); "Process for generating methane in remote areas from renewable electricity". This is an R&D project co-financed through the RETOS INVESTIGACIÓN programme of the General Directorate for Scientific and Technical Research of the Ministry of Economy and Competitiveness.

4.- Own shares

At 31 December 2015 the Company does not hold any own shares, nor did it acquire any during the period then ended.

NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)

Directors' Report

2015

5. Events after the reporting period

No significant events have occurred since the 2015 reporting date that require disclosure in these annual accounts, other than the sale-purchase agreement entered into on 25 January 2016 by the Group company Naturgas Energía Distribución, S.A.U. and Repsol Butano, S.A. for the liquefied petroleum gas facilities owned by Repsol Butano, S.A. in Asturias, Cantabria and the Basque Country, for approximately Euros 116 million. As mentioned in note 26 to the accompanying annual accounts, this agreement is subject to compliance with certain conditions precedent, which are expected to be met during 2016.

6. Risks

The Company has analysed the risks and uncertainties of its activity and the board of directors deems that the internal procedures established sufficiently cover the risks identified.

7. Financial instruments

At 31 December 2015 the Company has not arranged any financial instruments.

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

**NATURGAS ENERGÍA DISTRIBUCIÓN, S.A.
(Sociedad Unipersonal)**

At their meeting held on 24 February 2016, pursuant to the requirements of article 253.2 of the Revised Spanish Companies Act and article 37 of the Spanish Code of Commerce, the Directors of Naturgas Energía Distribución S.A.U. authorised the issue of the annual accounts and directors' report for the year ended 31 December 2015. The annual accounts comprise the accompanying documents that precede this certification.

Signed:

Mr. Juan Ramón Arraibi
Dañobeitia

Mr. Luis Álvarez Arias de
Velasco

Mr. Rui Pedro Ávila
Campos Marques

Mr. Carlos Arias Chausson
(Non-executive secretary)