



## **REPORT ON THE ACTIVITIES OF THE ENAGÁS, S.A. AUDIT AND COMPLIANCE COMMITTEE IN 2016**

The purpose of this report is to summarize the activities of the Audit and Compliance Committee of Enagás, S.A. during 2016.

### **1.- COMPOSITION DURING 2016**

During the year 2016, the composition of the Committee has remained unchanged.

#### Chairman

Mr Martí Parellada Sabata, Independent Director

#### Members

Sociedad Estatal de Participaciones Industriales (SEPI), represented by its Deputy Chairman, Federico Ferrer Delso. Proprietary Directors

Ms Rosa Rodriguez Díaz, Independent Director.

Mr Gonzalo Solana González, Independent Director.

Mr Luis Valero Artola, Independent Director.

#### Secretary

Mr Rafael Piqueras Bautista.

As provided in the company's constitutional documents, the Committee called on a number of persons related to matters under their competence for consultation. Accordingly, committee meetings were attended by the Chief Executive Officer (Mr Marcelino Oreja Arburúa), the Chief Financial Officer (Mr Borja García-Alarcón Altamirano), and the Director of Internal Audit (Mr Isidro del Valle Santín). The Chief Risk Officer and the Director of Compliance, has also attended meetings of the Committee when the latter has addressed issues related to his functions.

The representatives of the External Auditor, Deloitte, S.L. for 2015 and E&Y for 2016, have also attended regular meetings of the Committee.

### **2.- AMENDMENT TO THE LEGAL REGULATIONS AND CORPORATE TEXTS PERTAINING TO THE AUDIT AND COMPLIANCE COMMITTEE.**

The General Shareholders' Meeting of the company held on 18 March 2016 agreed to amend article 44 ("Audit and Compliance Committee") of the Articles of Association to adapt it to the provisions of EU Regulation no. 527/2014 of 16 April and to the wording given in article 529 quaterdecies of the Corporate Enterprise Act by virtue of Audit Law 22/2015 of 20 July and whose full text is worded as follows:

#### **"ARTICLE 44.- AUDIT AND COMPLIANCE COMMITTEE.**

*There shall be an Audit and Compliance Committee within the Board of Directors and it shall comprise at least three and no more than five Directors, to be appointed by the Board having particular regard to their expertise and experience in accounting, auditing or risk management. No Executive Director may sit on this Committee.*

*Overall, the members of the Audit and Compliance Committee shall have the pertinent technical knowledge of the gas industry.*

*The majority of members of the Committee must be independent and will be appointed in light of his or her knowledge and track record in matters of accountancy, auditing, or both. The Committee Chairperson shall be selected from among the Independent Directors by the Board of Directors, and shall not have the casting vote. The Chairman must be replaced every four years, and may be re-elected after the lapse of one year from his departure from office.*

*The Audit and Compliance Committee shall possess functions and competences in the following areas, in addition to those that may be attributed to it in the Bylaws or the Regulations of the Board of Directors:*

- *To inform the General Shareholders' Meeting on issues raised in the areas that lie within the Committee's competence and, in particular, about the audit result, explaining how it has contributed to the integrity of the financial reporting and the Committee's function during the process.*
- *To oversee the proper operation of the company's internal control, its internal audit function and risk management systems, and discuss with the auditors any significant weaknesses in the internal control system detected in the course of audit, all of this without undermining its independence. For such purposes and, where applicable, they can submit recommendations or proposals to the Board of Directors and the corresponding deadline for dealing with them.*
- *To oversee the process of preparation and presentation of statutory financial reporting and submit recommendations or proposals to the Board of Directors aimed at safeguarding its integrity.*
- *To submit proposals to the Board of Directors for selecting, appointing, re-electing and replacing the auditor, being responsible for the selection process, in accordance with the applicable regulations, along with the terms of their contract, regularly evaluate information on the auditing plan and its implementation, in addition to preserving their independence in the exercise of their functions.*
- *To liaise with the External Auditor to obtain information on any issues that could compromise the latter's independence for review by the Committee or any other subjects related to the audit process and, where applicable, the authorisation of the services other than those forbidden, under the terms envisaged in the applicable regulations, and any other disclosures envisaged in the audit regulations and audit standards. In all cases, on an annual basis, the Audit Committee shall receive from the auditors written confirmation of their independence vis-à-vis the company or entities related to it directly or indirectly, in addition to detailed and individual information on additional services of any kind rendered to these entities by the aforementioned auditors or persons or entities related to them in conformity with the audit regulations.*

- *To issue annually, prior to the issue of the audit report, a report giving an opinion on the independence of the auditors or audit firms. This report shall in all cases include a reasoned assessment of all the additional services provided, as referred to in the previous section, considered separately and in their totality, that consists of services other than statutory audits and how they relate to the requirement of independence or to the audit regulations standards.*
- *To keep the Board of Directors informed, in advance, on all items provided for in the law, the Articles of Association and the Rules and Regulations on the Board of Directors, in particular, on:*
  - 1 *the financial information that the company must periodically publish,*
  - 2 *the creation or acquisition of shares in special purpose vehicles or entities resident in jurisdictions considered tax havens and*
  - 3 *related party transactions.*

*The meetings of this Committee shall be called by its Chairman and shall be held at least four times a year. The company's External Auditor may attend Committee meetings and the Finance Director, head of the Enagás Internal Audit Unit, or any other senior manager of the company or group that the Committee deems appropriate, may also be asked to give account at meetings. The Committee may obtain support and assistance from the aforesaid Executives in the performance of its duties."*

The Committee issued its favourable report on the proposed amendment to the aforementioned corporate texts.

## **2.- THE COMMITTEE'S ACTIVITIES**

The Committee met six times in 2016. The Chairman of the Committee has reported to the Board the discussions held at each of the meetings of the Committee at the next meeting thereof.

The main areas in which the Audit and Compliance Committee has focused its activity during 2016 are summarized below.

### **Committee activities relating to the formulation and approval of the Enagás Financial Statements for 2015 Report on the independence of the External Auditor. Report on the independence of the External Auditor**

As in previous years, the Audit Committee was entrusted with the task of discussing and analysing the financial statements prior to their authorization for issue by the Board of Directors. To this end the members of the Committee met with the company's External Auditors (Deloitte S.L.) for 2015, on 15 February 2016, and also with Enagás' Chief Financial Officer and Director of Internal Audit.

Both the External Auditors and the financial officers of the company offered the Committee their views on the financial statements. Differences in accounting criteria in no case exceeded the materiality threshold above which Deloitte's opinion on the financial statements could be affected. Deloitte informed the Audit Committee that its report would be without reservations or qualifications.

The External Auditors delivered a letter to the Committee in which they state that *"in connection with the audit of the consolidated financial statements of Enagás, S.A. and subsidiaries (Enagás Group) for the year ended 31 December 2015, we confirm that to our best knowledge, the team in charge of the audit and Deloitte, S.L., with the extensions that apply to them, have complied with the independence requirements applicable under the provisions of the revised text of the Audit Law, issued by Royal Legislative Decree 1/2011, of 1 July, and its implementing regulations."* The letter then states Deloitte's total fees for 2015, categorised by type of service.

For its part, the Committee unanimously approved the "Report of the Audit and Compliance Committee on the independence of the External Auditor", made available to shareholders together with the Notice of the General Shareholders' Meeting held on 18 March 2016 which approved the accounts for 2015. This report concludes that;

*"In view of the information that has been provided, the Audit and Compliance Committee of Enagás has not identified any issues that call into question compliance with the regulations in force in Spain for the audit activity as regards auditor independence and, in particular, the Committee confirms that it has not identified any matters of this nature relating to the provision of additional services to those of the audit, taken individually and as a whole, of any kind".*

The following conclusions emerged from the Audit Committee's examination of the 2015 financial statements:

- *That the financial statements of Enagás and its Consolidated Group, as submitted to the Committee, gave a true and fair view of the company's equity and results of operations for the year.*
- *That the financial statements contained sufficient information to be clearly understood, in addition to a sufficient description of the risks faced by the company.*
- *That the statements respected the generally accepted accounting principles and regulations, on the same terms applied in previous years.*
- *That the principles of equality of treatment for shareholders and transparency of information reported to the markets had been abided by.*

The Committee accordingly resolved to recommend that the Board of Directors of Enagás authorize the financial statements for its issue. At a meeting held on 15 February 2016, the Board of Directors adopted the Committee's recommendation and authorized the financial statements for issue in line with the terms indicated by the Committee. The financial statements and directors' report for 2015 were approved at the General Shareholders' Meeting held on 18 March 2016.

In addition to the above task, as in previous years, the Chairman of the Audit Committee, Mr Parellada, intervened at the Ordinary General Shareholders' Meeting of the company held on 18 March 2016, to explain the most important elements of the financial statements to the company's shareholders and to ensure that they had all the information they needed to be able to vote on the financial statements, which were adopted as proposed by the Board of Directors.

#### **Quarterly accounting reviews**

Throughout 2016, the Committee continued to review the interim financial statements and the limited quarterly reports issued by the auditors.

Specifically, the Committee analysed, together with E&Y, the new Auditor for 2016 to 2018, the reports issued by the latter for the first, second and third quarters, respectively. Performing these reviews enables the Committee to minimize the impact of any accounting issues arising in the course of the year, and the members of the Committee and Board of Directors to keep abreast of the opinions of the company's External Auditors on annual developments in the balance sheet and income statement.

The Audit Committee considers that both the quarterly reviews carried out by the External Auditor and the Committee's own analysis of these reports are essential to ensure strict control over the company's accounting, and they also facilitate the issue of an unqualified audit report at year-end.

The Committee also reviews and approves financial information disclosed by the company each quarter, in line with the good corporate governance recommendations it has adopted.

In particular, the Committee prepared a favourable report on the financial statements for the first half-year which, on its recommendation, were approved by the Board of Directors on 18 July 2016.

### **Internal Control over Financial Reporting System (ICFR).**

The Committee has supervised the *Internal Control over Financial Reporting System* (hereinafter, ICFR) applied by the company. Both the ICFR and its application during the year are described in the Annual Corporate Governance Report which includes the favourable report of the External Auditor as an Appendix. The Committee has reported favourably on the proposed Annual Corporate Governance Report.

### **External auditor.**

The Committee has sought to ensure the independence of the External Auditor in the performance of its duties. According to the applicable provisions, it has sought the declaration of independence and has issued one of its own as set out above. In addition, following the recommendations of the Good Governance Code of Listed Companies, it has produced a specific report on the independence of the Auditor to be made available to shareholders when publishing the notice of the General Shareholders' Meeting. It has also approved the contracts that the company has signed with the External Auditor, ensuring that they do not affect its independence.

After the enactment of Audit Law 22/2015 of 20 July, which determines the options applicable in Spain from among those envisaged in EU Regulation no. 537/2014 of the European Parliament and of the Council of 16 April 2014, the Audit and Compliance Committee convened a tender designating the auditor for the coming years. The tender process, to which several reputable audit firms were invited, was carried out with complete independence so that the Committee could undertake its task. Likewise, during the process, the Committee took the necessary measures to ensure that the proposed firm met the suitability, independence and compatibility requirements imposed by the aforementioned provisions.

In view of the bids received and other factors, the Audit and Compliance Committee, by exercising the functions attributed to it in article 529 quaterdecies 4. e) of the Corporate Enterprise Act, submitted to the Board the proposal to appoint Ernst & Young, S.L. as the auditor of Enagás, S.A. and its consolidated group for 2016, 2017 and 2018. The Ordinary General Shareholders' Meeting held 18 March 2016 adopted the following resolution:

*"To appoint Ernst & Young, S.L., as Auditor of Enagás, S.A. and its Consolidated Group for 2016, 2017 and 2018. Said firm shall also be placed in charge of providing any other statutory auditing services needed by the company until the next Ordinary General Meeting is held."*

### **Related-party transactions.**

The Committee has assumed the functions that the discussed legal and corporate texts attribute thereto in relation to related-party transactions. Under the supervision of the Committee, the company has published the required regular information in this respect, as well as that contained in the Annual Corporate Governance Report.

Following the recommendations of the Corporate Governance Code of Listed Companies, the Committee produced a report on related-party transactions that was made available to shareholders when together with the Notice of the General Shareholders' Meeting held on 18 March 2016.

### **Internal auditor.**

The Committee in their meeting held on 15 February 2016 approved the Annual Internal Audit Plan for 2016 and the Internal Audit Budget for 2016. The Committee has ensured that the Internal Audit Department has adequate human and material resources to carry out its function.

The Director of Internal Audit has reported regularly to the Committee on the development of the Annual Plan and the results of the audits.

### **Risk control in 2016.**

The Audit Committee considers the work on risk control to be particularly important. Periodically, the Chief Executive Officer and the Director of Risks have informed the Committee of the state of risk control and management at the company.

The Chief Executive Officer, together with the Chief Risk Officer, presented an annual risks report for 2015, a report for each quarter of 2016 and a final report for the whole of 2016, to the Committee.

### **Report of proceedings of the Ethics Committee**

The Committee has examined the activities of the Ethics Committee, and approved its report for 2016. The Committee has been informed in a timely fashion and in detail regarding the incidents arising in relation to the "Ethics Channel". No significant incidents have been detected during the year in question.

### **Activities subsequent to year-end**

In the opening months of 2016, the Committee continued with its usual activities, in particular assisting the Board of Directors in preparing the financial statements. As in the previous year, the accounts for 2016, which will be submitted to the Ordinary General Shareholders' Meeting likely to be held in March 2017, have been previously and favourably informed by the Audit and Compliance Committee at a meeting on 13 February 2017.

And for all appropriate legal reasons, it is hereby stated that the Audit and Compliance Committee approved this report at its meeting held on 13 February 2017.

The Secretary to the Board of Directors  
Rafael Piqueras Bautista  
**Enagás, S.A.**