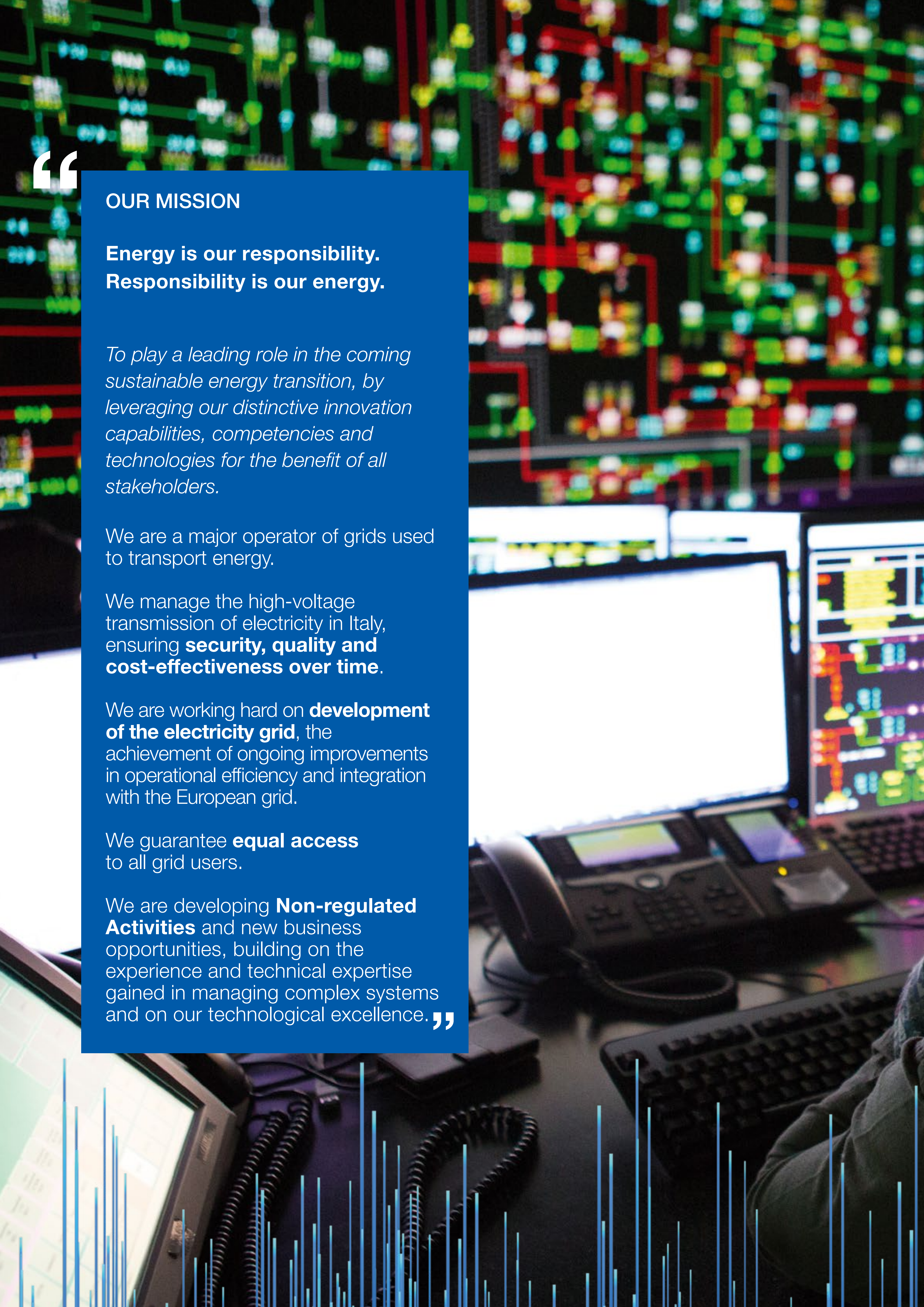
ENERGY IS OUR RESPONSIBILITY

2018

Annual Report
Integrated Report

Terna



OUR MISSION

Energy is our responsibility.
Responsibility is our energy.

To play a leading role in the coming sustainable energy transition, by leveraging our distinctive innovation capabilities, competencies and technologies for the benefit of all stakeholders.

We are a major operator of grids used to transport energy.

We manage the high-voltage transmission of electricity in Italy, ensuring **security, quality and cost-effectiveness over time**.

We are working hard on **development of the electricity grid**, the achievement of ongoing improvements in operational efficiency and integration with the European grid.

We guarantee **equal access** to all grid users.

We are developing **Non-regulated Activities** and new business opportunities, building on the experience and technical expertise gained in managing complex systems and on our technological excellence.

Terna

“

The ongoing energy transition towards an increasingly **sustainable** electricity system poses new challenges and opportunities. Terna is at the centre of this process of achieving decarbonisation goals, guaranteeing the security of the system and minimising the total cost for Italian households and businesses.

This commitment will gain momentum with the objectives set out in the **Strategic Plan 2019-2023**, which provides for investment in expanding the national electricity grid in order to respond to the new needs of the system. In this process, innovation, digital transformation and people underpin our strategy.

The quest for **innovative solutions and technologies** to be used in managing and developing the national transmission grid is one of the enabling factors for dealing with the growing complexity of the system. To this end, Terna has implemented a centralised and coordinated innovation plan to manage electricity flows through the grid in a safe, efficient and reliable way.

Our people are the drivers of change and, for this reason, we are continuing to invest in the development of personal and professional skills. **Our passion** enables us to approach our work proactively and with dedication.

Statement to stakeholders from the Chairwoman and the Chief Executive Officer

We are convinced that investing in continuous training and bringing young people into the world of work are vital elements in the process of generating value.

Given the role the Company plays in the electricity system, Terna has a **responsibility** towards the entire community, both in its daily operations and over the medium to long term. Management and development of the grid is based on listening to stakeholders with a view to fostering mutual **trust and transparency**. Close interaction with **local communities** is one of our priorities, via a development model that is geared towards **dialogue** and pays ever greater attention to **local needs**.

The operating performance in 2018 demonstrates Terna's ability to deliver on pre-set objectives and showing how the need for a safe, efficient and sustainable electricity grid for Italy can be combined with positive returns for our shareholders. The results presented in the financial statements also bear witness to the Group's economic and financial strength, allowing us to look towards the future with optimism and enthusiasm.”

Catia Bastioli
Chairwoman

Luigi Ferraris
CEO

Highlights

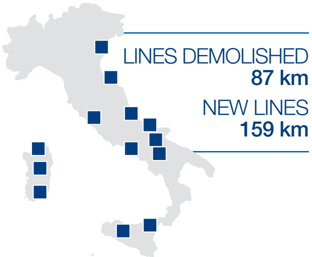
On **21 March 2019**, the revised **Grids and Values corporate strategies for 2019-2023**, approved by the Board of Directors, were presented to the market and to stakeholders.

In 2018, Terna's substantial commitment to developing the grid continued, supporting the energy transition in progress, and building a secure and sustainable electricity system for the benefit of future generations.

2018 was an excellent year: the improvements in all key performance indicators confirm the effectiveness of the management actions implemented, and support the virtuous growth path outlined in the *Grids and Values* Strategic Plan.

Regulated Activities in Italy

P. 42



Reorganisation of the Venetian lagoon:

entry into service of the Sacca Serenella primary substation - Cavallino primary substation 132kV underground and submarine cable, which together with other works will launch the modernisation phase of the lagoon.

Entry into service of 5 new lines, extending for 98 km:

- Bono (SS) - Buddusò (OT)
- Villanova (PE) - Cepagatti (PE)
- Benevento II (BN) - Benevento III (BN)
- Messina Riviera (ME) - Villafranca (AG)
- Cimmina (PA) - Casuzze (AG)

Entry into service of 8 new substations.

Non-regulated Activities

P. 66

Cable laying started for the Italy-France interconnector on the A32.

Acquisition via Terna Plus of a 70% stake in Avvenia The Energy Innovator S.r.l., a leading company in the energy efficiency sector.

Open Fiber project: extraction of value from Terna's assets to serve the digitisation of Italy continues; 5,800 km of regional rings delivered.

Tamini: recovery of operating margins in progress.

International Activities

P. 78

Entry into service of the new 230kV Santa Maria 3 - Santo Angelo 2 power line in south-eastern Brazil, which is vital for the integration of energy from renewable sources (especially wind power). 12 months of work involving 10 companies and 500 technicians: 80% of the project constructed using low environmental impact single-stem pylons.

Activities in **Brazil**, Uruguay and **Peru** continue.

SUSTAINABILITY AWARDS

P. 113

World leader in electric utilities sector - Dow Jones Sustainability Index 2018.

Inclusion for the first time in the Bloomberg Gender Equality Index (GEI).

Inclusion for the 8th consecutive year in the STOXX Global ESG Leaders sustainability indices.

Inclusion for the 10th year in the Ethibel Sustainability Index (ESI) Excellence Europe.

FINANCIAL HIGHLIGHTS

P. 100

(€m)	2018	2017	Δ
Revenue	2,197.0	2,162.8	1.6%
EBITDA	1,650.6	1,603.9	2.9%
Profit attributable to owners of the Parent	706.6	688.3	2.7%
Capital expenditure	1,091.1	1,033.9	5.5%
Net debt (FY)	7,899.4	7,796.4	

STOCK MARKET AND FINANCE

Terna share performance P. 112

Annual performance outstrips main peers and the European DJ Stoxx Utilities benchmark index (-2.1%).

+2.25%

(€4.95 per share at 31 December 2018 compared with €4.84 per share at 31 December 2017)

€5.502 per share, new record high registered on 14 March 2019.

Green Finance P. 94

July 2018: launch of a €750m green bond issue with a 5-year maturity and 1% coupon, reopened in January 2019 in the form of a private placement of €250m maturing on 2023.

September 2018: subscription of a back-up ESG linked Revolving Credit Facility.

"Latin America Transmission/Distribution deal of the year" award for financing the 500kV power line in Uruguay.

April 2019: successful launch of a new green bond for €500m, tenor of 7 years and coupon of 1.000%.

BUSINESS ENABLERS

P. 82 **Our people**

468 new hires to support the Strategic Plan and generational turnover. Important initiatives for the **enhancement of skills** and **occupational safety.**

P. 90 **Innovation**

Launch of a latest-generation green transformer at the Udine West power plant, which combines efficiency, safety and sustainability, thanks to the revolutionary use of ester and renewable and biodegradable vegetable oils. **Two green autotransformers entered service** at Travagliato and Cagno.

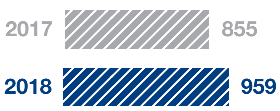
PERFORMANCE OF THE ELECTRICITY SYSTEM

P. 30 **Demand** [TWh]

DEMAND MET BY RENEWABLES

(*) Provisional data. RS: Renewable sources - NRS: Non-renewable sources

P. 56 **ENSR quality** [MWh]

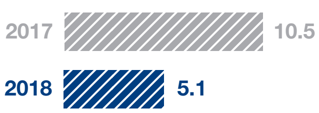


SIGNIFICANT EVENTS

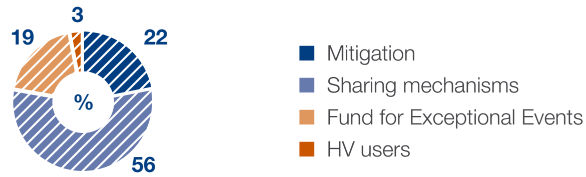
Performance in 2017: significant event due to a weather emergency in Abruzzo and Marche (480 MWh)

Performance in 2018: exceptional event in north-eastern Italy (currently being recognised by ARERA)

P. 57 **Quality costs** [€/m]



COST BREAKDOWN **2018**



NOTE TO THE READER

As in previous years, the Report on Operations constitutes the Terna Group's Integrated Report for 2018.

In keeping with earlier editions, this year's Integrated Report continues to apply the principles contained in the International Integrated Reporting Framework published by the IIRC (International Integrated Reporting Council), the international body set up to oversee this form of reporting, but introduces a number of significant innovations.

In terms of the manner in which content is organised, pride of place has been given to "Our People": this is our way of highlighting the essential and central role played by expertise and human capital throughout the Group's activities. The need to clearly and fully describe our business model has also led us to choose a "horizontal" approach, based on area of business (Regulated Activities, Non-regulated Activities and International Activities), more in line with the connectivity of information.

The materiality principle has been applied in selecting the information to include; in particular, the inclusion of information regarding environmental, social and governance aspects meets the need to show how they relate to the creation of value. The materiality matrix used is attached to this document.

Contents

“We promote the energy transition and sustainable development by focusing on people and innovation. We work every day to build an atmosphere of dialogue and trust in local areas, to which we bring a vital asset for everyone’s economic and social lives: electricity. This translates into choices based on respect for the environment and local communities. Our inclination to listen begins within the Company, among our people, in the awareness that the radical transformation the world is experiencing is a shared responsibility. This responsibility is our energy.”

+559%

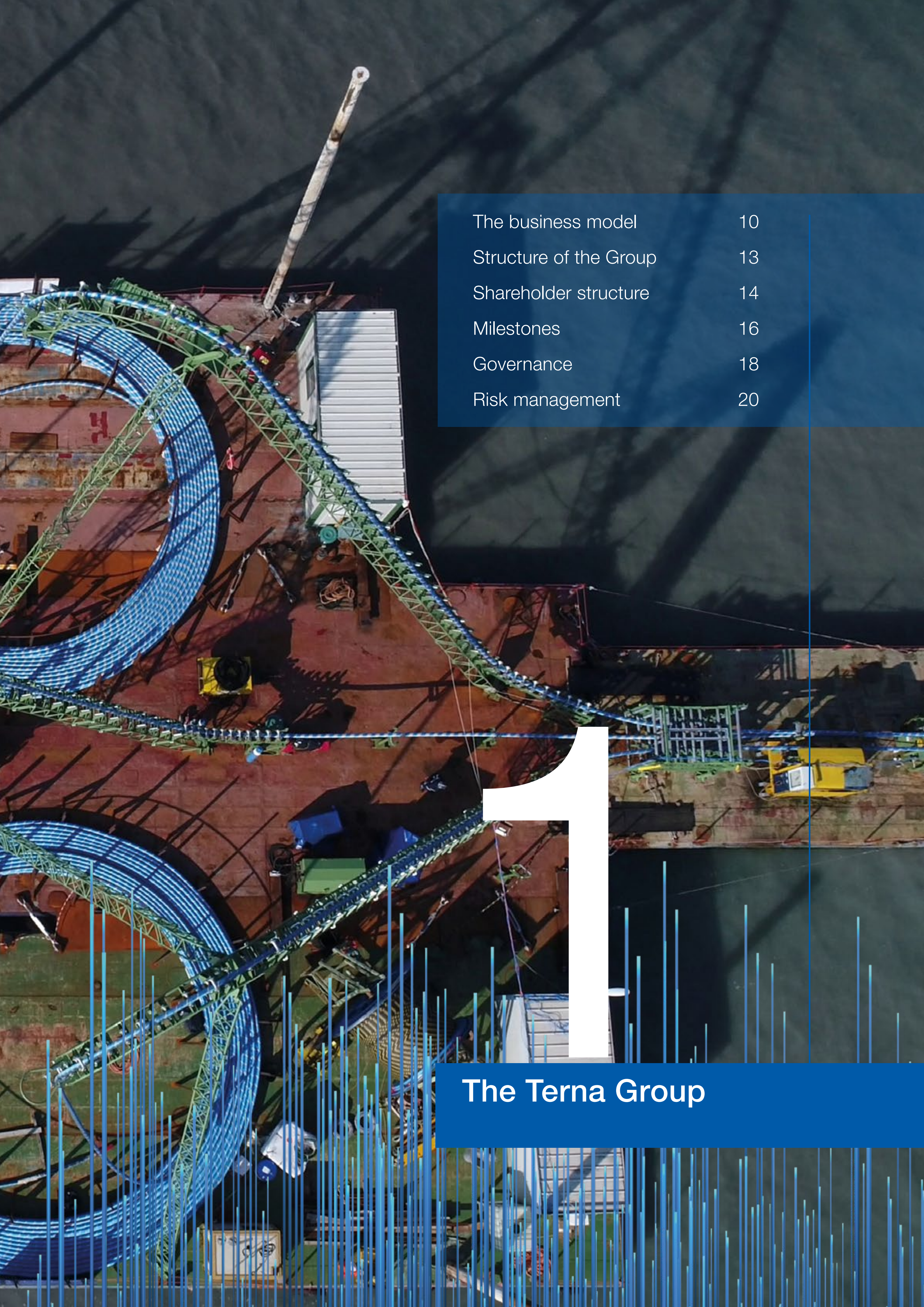
TOTAL SHAREHOLDER RETURN SINCE THE IPO

74,442km

OF HIGH VOLTAGE LINES MANAGED

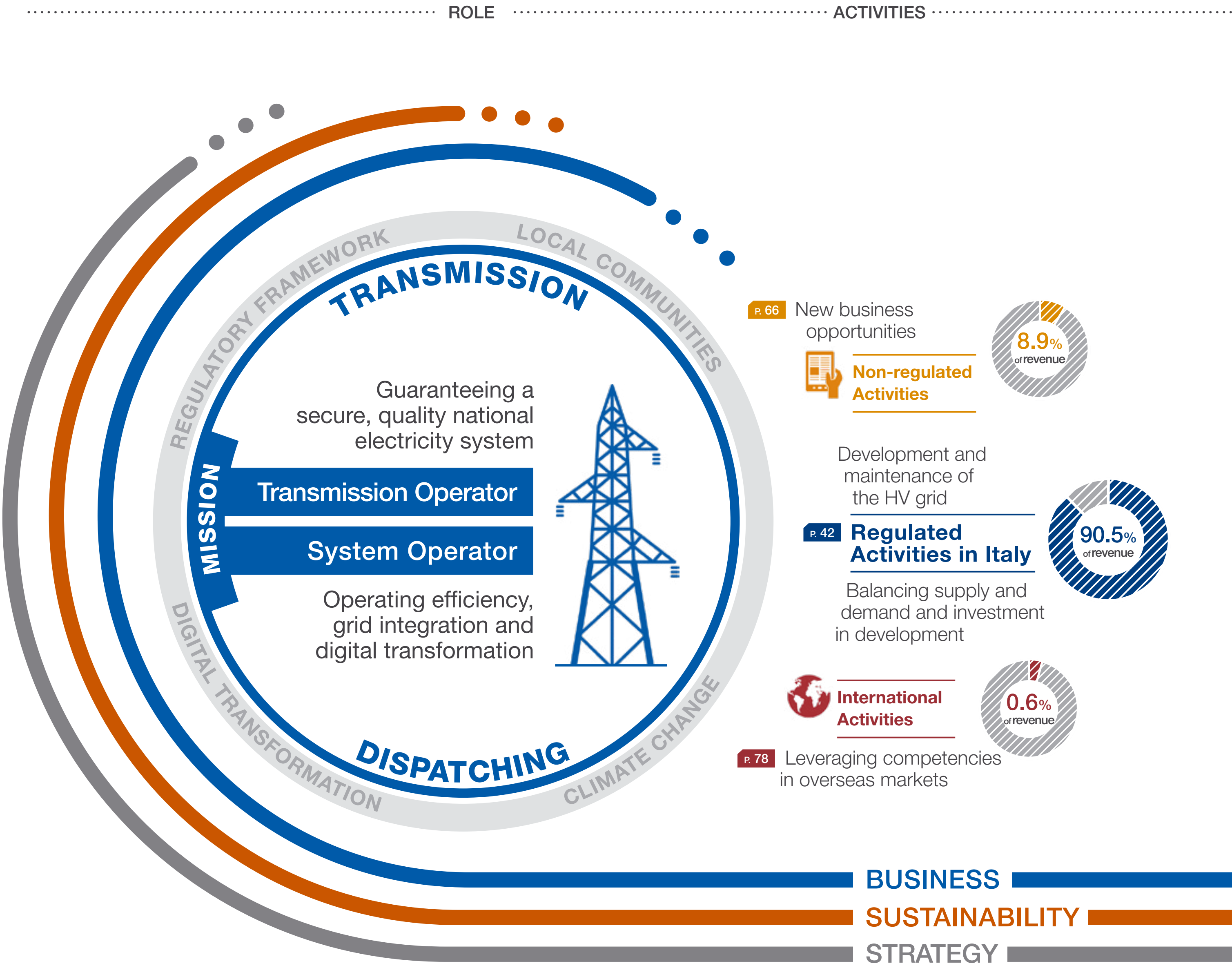
4,252

WORKFORCE AT 31 DECEMBER 2018 INCLUDING 468 NEW HIRES IN 2018



1 The Terna Group

The business model



Terna plays a central role in the energy transition process underway: in a context of radical change with decarbonisation emerging as a global objective, the electricity grid is one of the main enabling factors.

ENABLERS · VALUE CREATION · SYSTEM EFFECTS

ENABLERS

P. 82 **PEOPLE** at the centre of our business
- Competencies
- Integrity and Values
- Safety

P. 90 **INNOVATION** in response to the growing complexity of the system
- Digital solutions
- New technologies
- Open innovation

VALUE CREATION

P. 112 **Shareholder value with constant,** predictable growth in returns over a five-year period

P. 20 **Risk control** through prevention and real-time response

P. 60 **Value for money** of the prices charged to end users

P. 56 **Quality of service** to provide the community with a reliable electricity supply, minimising outages

P. 48 **Resilience** in the face of the increasingly complex challenges posed by climate change

P. 46 **Checks on the impact of our activities** in our approach to every stakeholder

P. 48 **Grid development and maintenance** to maximise the reliability of the service

SYSTEM EFFECTS

CO_2 P. 27 PROGRESSIVE DECARBONISATION

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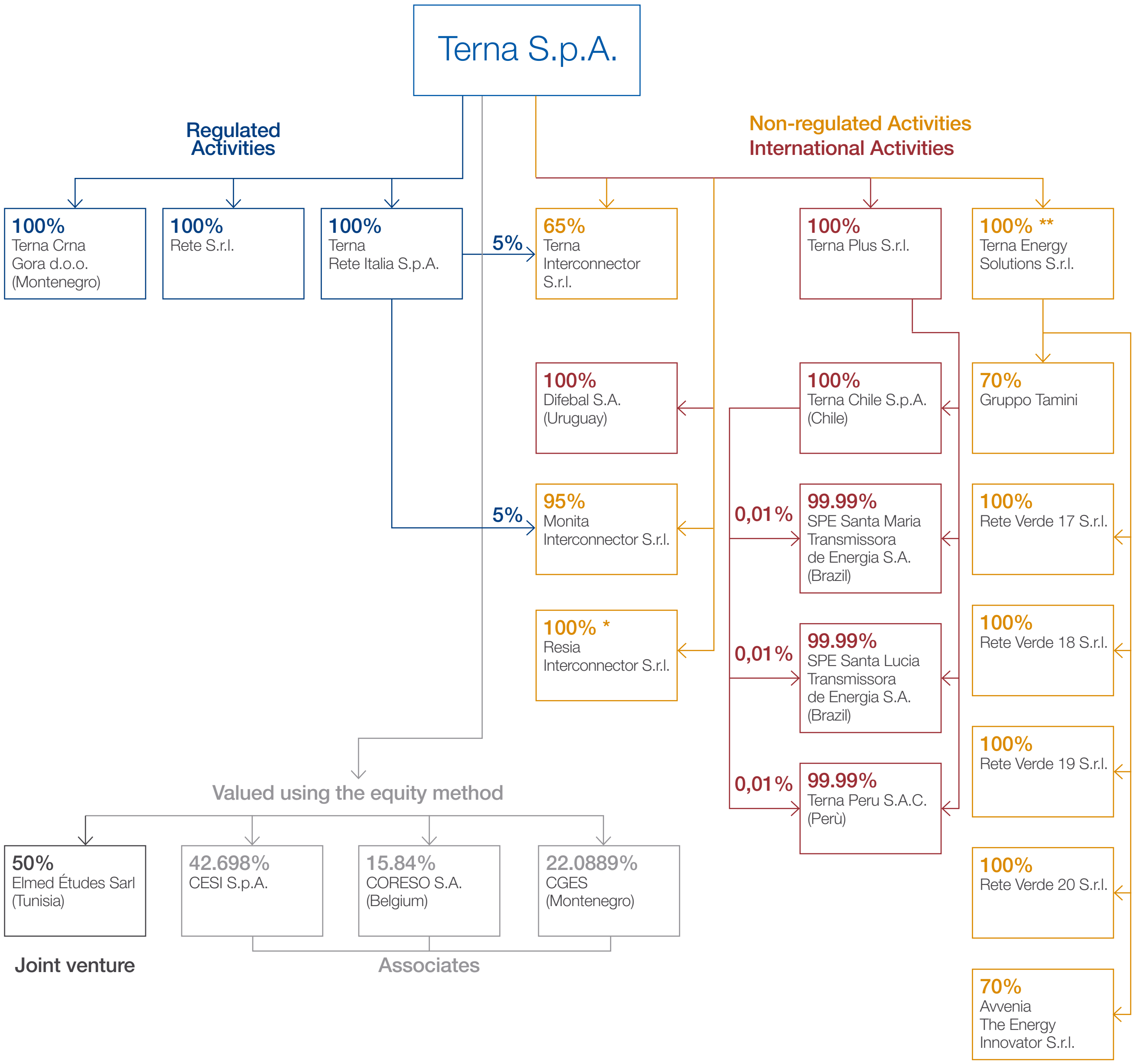
A key role in **ENERGY TRANSITION** P. 26

Structure of the Group



Compared with 31 December 2017:

* On **16 July 2018, Resia Interconnector S.r.l.** was incorporated. This company will be involved in construction of the private Italy-Austria interconnector, for which the process of obtaining the necessary consents for the Passo Resia - Glorenza cable section is currently underway.

** On **2 August 2018, the partial demerger of Terna Plus S.r.l.** (a wholly-owned subsidiary of the parent, Terna S.p.A.), and the transfer of the demerged assets to a newly established company named Terna Energy Solutions S.r.l., came into effect. The demerged business is focused on Non-regulated Activities and on the energy solutions activities already carried out by Terna Plus which, following the demerger, is responsible for the Group's South American activities. The transaction also resulted in the transfer of equity interests in the companies that carry out Non-regulated Activities in Italy: Tamini Trasformatori S.r.l., Rete Verde 17 S.r.l., Rete Verde 18 S.r.l., Rete Verde 19 S.r.l., Rete Verde 20 S.r.l. and Avvenia The Energy Innovator S.r.l. (acquired on 15 February 2018).

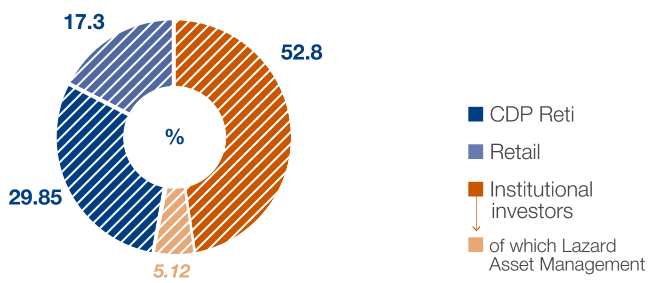
Shareholder structure

At the date of preparation of this report, **Terna's share capital amounts to €442,198,240** comprising 2,009,992,000 fully paid-up ordinary shares with a par value of €0.22 each.

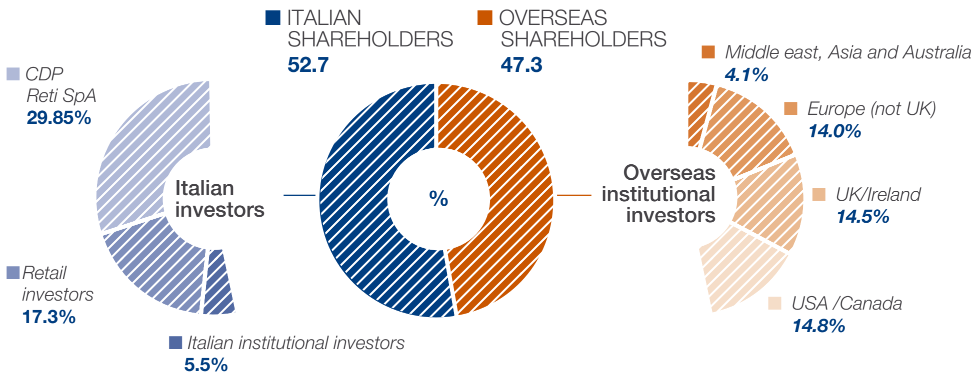
Based on periodic surveys carried out by the Company, it is estimated that 52.7% of Terna's shares are held by Italian shareholders, with the remaining 47.3% held by overseas institutional investors, primarily from the USA and Europe.

Based on information from the shareholder register and other data collected as at February 2019, Terna's shareholder structure breaks down as follows.

SHAREHOLDERS BY CATEGORY



SHAREHOLDERS BY GEOGRAPHICAL AREA AND CATEGORY



Major shareholders[1]

CDP RETI SpA[2]
(a company controlled by Cassa Depositi e Prestiti S.p.A.): 29.851%

LAZARD ASSET MANAGEMENT LLC
(as a discretionary asset manager): 5.122%

Socially Responsible Investors

At the end of 2018, 109 socially responsible investors (SRIs) had invested in Terna's shares in application of an approach that takes into account ESG (Environmental, Social, Governance) aspects.

Overall, **at the end of 2018, SRIs represented 9.52% of Terna's free float** (8.32% at the end of 2017) and 12.86% of the capital held by identifiable institutional investors (approximately 11% at the end of 2017).

Information on the ownership structure, restrictions on the transfer of shares, securities that grant special rights, and restrictions on voting rights, as well as on shareholder agreements, is provided in the "Report on Corporate Governance and Ownership Structures" for 2018. This is available in the Investor Relations section of Terna's website (www.terna.it).

[1] Shareholders who, based on the available information and notifications received from the CONSOB, own interests in Terna S.p.A. that are above the notifiable threshold established by CONSOB Resolution 11971/99.

[2] On 27 November 2014, a shareholder agreement was entered into by Cassa Depositi e Prestiti S.p.A. (CDP), on the one hand, and State Grid Europe Limited (SGEL) and State Grid International Development Limited (SGID), on the other, in relation to CDP RETI S.p.A., SNAM S.p.A. and TERNA S.p.A.. This was later amended and supplemented to extend the scope of the agreement to include Italgas S.p.A..

Milestones

ORIGINS .... THE NEW TERNA ....

1962 1999

2004 2008

2009 2013

From a Monopoly to an Independent System Operator

Terna's principal activities are rooted in Italy's history: in 1962, Law 1943 paves the way for nationalisation of the electricity industry, handing ENEL responsibility for all the stages of the electricity supply chain, previously in private hands.

The monopoly operator is able to complete electrification of the Italian Peninsula, but the driving force behind the changes that have led to the current operating environment is the process of deregulation promoted by the European Union aimed at making grid management independent.

In implementation of Decree 79 of 16 March 1999, focused on separation of ownership the National Transmission Grid from management of the grid itself (involving transmission and dispatching) along the lines of the so-called "Independent System Operator" model, two new companies are established: Terna, owner of the Italian transmission grid, and GRTN (the National Transmission Grid Operator).

Terna's Initial Public Offering

A Cabinet Office Decree gives the Group a new corporate governance system, designed to guarantee the neutrality and impartiality of Terna's management.

In June 2004, 50% of the Company's share capital is floated on the Italian Stock Exchange (in the Blue Chip segment).

Unification of the roles of Transmission Operator and System Operator: Terna's new mission to serve the country

In 2005, ownership and management of the grid are combined. This marks the culmination of a process that began in 1999 and the start of a new stage in Terna's mission to serve the country.

In this period, the Company records continuous growth, acquiring many portions of the grid from other operators. To safeguard Terna's independence as the National Transmission Grid Operator, the Ministry of the Economy and Finance acquires a 29.99% stake in Terna through CDP (Cassa Depositi e Prestiti).

Terna becomes the largest TSO in Europe

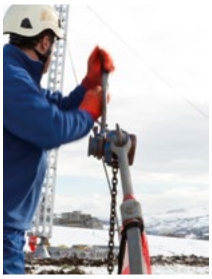
Terna acquires 18,600 km of high-voltage lines from Enel, thereby becoming the leading independent grid operator in Europe and the seventh largest in the world. Terna now owns 98.6% of Italy's national grid.

Shareholder value grows

In 2009, Terna sells 66% of the Brazilian subsidiary, Terna Participações, to Cemig, recording a gain of over €400 million, some of which is invested in development of the Italian electricity network and some is returned cash to shareholders.

New infrastructure projects and growing success of Non-Regulated activities

In 2011, Terna develops infrastructure of international excellence. The SA.PE.I. line (Sardinia to the mainland) starts operating, as does the Chignolo Po-Maleo line in Lombardy. Work begins on the Sorgente-Rizziconi line (linking Sicily and Calabria).
Two new operating companies are established in 2012: Terna Rete Italia S.p.A., responsible for regulated activities, and Terna Plus S.r.l., with responsibility for expanding the Non-regulated services.


THE PRESENT DAY

2014 2017

European leadership consolidated with new investments

In 2015, Terna acquires the Ferrovie dello Stato group's high-voltage grid for €757 million, consolidating its leadership in Europe with approximately 72,600 km of grid managed. Terna's value has more than doubled since its IPO.
In 2016, Terna focuses on strategic power lines. The Villanova-Gissi and Sorgente-Rizziconi lines enter service. The latter is a record-breaking power line, connecting Sicily and Calabria and the Italian Peninsula with the rest of Europe via the country's high-voltage electricity system.

Change of management

In 2017 a new Board of Directors is elected, with Luigi Ferraris appointed as the new Chief Executive Officer and General Manager, new managers appointed to key roles, and Catia Bastioli re-appointed as Chairwoman.

2018

The "Grids and Values" Strategic Plan

In line with the guidance provided by the United Nations (COP21), EU guidelines and the objectives set out in the National Energy Strategy (*Strategia Energetica Nazionale* or "SEN"), Terna has stepped up the pace of investment, focusing on development of the national transmission grid in order to facilitate the integration of renewable sources and improve the system's security. At the same time, it intends to renew the Group's asset base in order to mitigate the risk of interruptions to supply, boost environmental sustainability, and improve the performance of maintenance activities through the use of digital grid technologies, all to the benefit of the quality of the electricity service. The new corporate strategies, presented for the first time in March 2018 by the CEO and General Manager, Luigi Ferraris, are revised at the meeting with investors held on 21 March 2019.

A new organisational structure and the Transmission Operator-System Operator logic

In order to optimise and integrate dispatching and long-term planning activities, on the one hand, and maximise the operational efficiency of design, implementation, operations and maintenance, on the other, two key organisational structures, reporting directly to the Chief Executive Officer, have been redesigned. Terna thus plays two core roles: as System Operator, embodied in the "Strategy, Development and Dispatching" structure, and as Transmission Operator of the "National Transmission Grid".

The new Terna Plus and Terna Energy Solutions

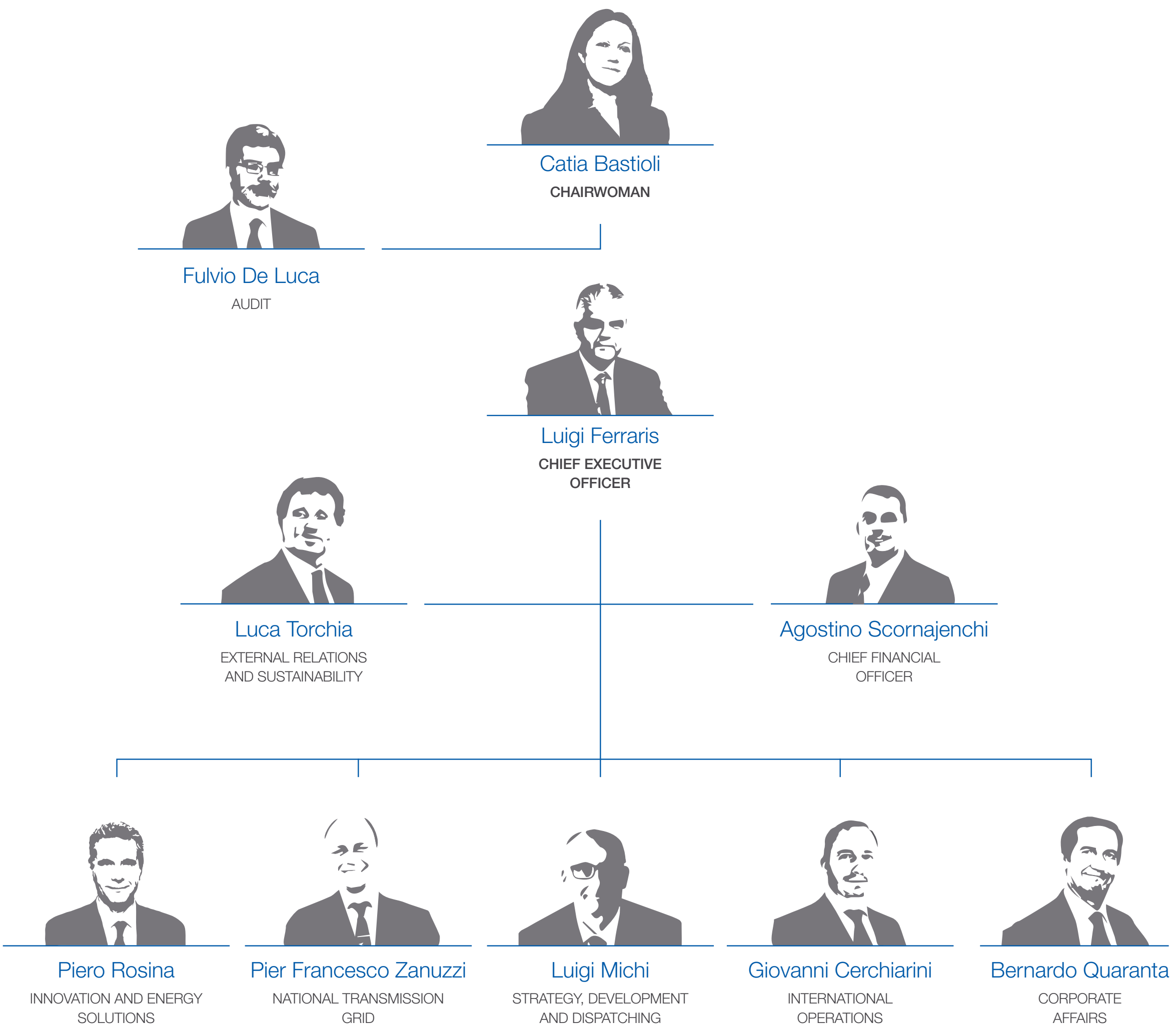
In August 2018, the partial demerger of Terna Plus S.r.l. (a wholly-owned subsidiary of the Parent Company, Terna S.p.A.), and the transfer of the demerged assets to a newly established company named Terna Energy Solutions S.r.l., came into effect. The latter's business is focused on non-regulated activities and energy solutions activities. Terna Plus will now be responsible for the Group's development and plant construction activities in South America, and more generally for the development of new businesses around the world.

Governance

Our corporate governance system has been designed with the aim of creating value for shareholders, based on an awareness of the social significance of our activities.

Promoting collaboration and dialogue in order to tackle future challenges and apply a culture of responsibility are the underlying principles that underpin our approach.

Our managemen team



These objectives are pursued taking into account the social and environmental importance of the Group's operations and the resulting need to adequately consider all stakeholders in conducting our business.
In this regard, the ultimate guide relating to matters of sustainability is the **Code of Ethics**[3], which references the ten principles regarding human rights, labour, the environment and corruption covered by the Global Compact, the *multi-stakeholder network* set up by the United Nations and which Terna has been a member of since 2009. The Code of Ethics also requires the Group to publish an annual Sustainability Report, which in the Group's case also includes the non-financial statement required by art. 4 of Legislative Decree 254/2016. The Sustainability Report contains disclosures on fulfilment of our environmental and social commitments and on the consistency of the results achieved with the targets set.

Board of Directors

Chairwoman
Catia Bastioli

Chief Executive Officer
Luigi Ferraris

Directors
Fabio Corsico
Luca Dal Fabbro
Paola Giannotti
Yunpeng He
Gabriella Porcelli
Paolo Calcagnini[4]
Elena Vasco

Board of Statutory Auditors

Chairman
Riccardo Enrico Maria Schioppo

Standing Auditors
Vincenzo Simone
Maria Alessandra Zunino de Pignier

Alternates
Davide Attilio Rossetti
Cesare Felice Mantegazza
Renata Maria Ricotti

Board committees[6]

Audit, Risk, Corporate Governance and Sustainability Committee
Luca Dal Fabbro[5] (Chairman, independent)
Elena Vasco (independent)
Paola Giannotti (independent)

Remuneration Committee
Fabio Corsico (Chairman, independent)
Gabriella Porcelli (independent)

Nominations Committee
Luca Dal Fabbro (Chairman, independent)
Yunpeng He
Fabio Corsico (independent)

Related Party Transactions Committee
Gabriella Porcelli (Coordinator, independent)
Luca Dal Fabbro (independent)
Paola Giannotti (independent)

Manager responsible for Terna S.p.A.'s financial reporting

Manager responsible for Terna S.p.A.'s financial reporting
Agostino Scornajenchi

Independent auditors

PricewaterhouseCoopers S.p.A.

[3] Available on Terna's website at http://www.terna.it/it-it/investorrelations/corporategovernance/eticadimpresa/codiceetico.aspx, sub: http://download.terna.it/terna/0000/0063/62.pdf e sub http://download.terna.it/terna/0000/0054/05.pdf
[4] On 15 February 2019, after the resignation of Director, Stefano Saglia, from the positions he held on the Board of Directors of Terna S.p.A., as reported to the market on 31 July and 10 August 2018, the Board of Directors co-opted Paolo Calcagnini as a new non-executive Director, subject to the opinion of the Nominations Committee and with the approval of the Board of Statutory Auditors, thereby accepting the invitation made by the Cassa Depositi e Prestiti Group in a letter dated 6 February 2019. The new Director, who does not meet the independence requirements pursuant to art. 3 of the Code of Conduct and pursuant to art. 147 ter, paragraph 4, and art 148, paragraph 3, of Legislative Decree 58/2008, will remain in office until the next Shareholders' Meeting.
[5] Following the resignation of the Director, Stefano Saglia, from the positions he held on the Board of Directors of Terna S.p.A. - as reported to the market on 31 July, 10 August and 9 November 2018 - the Board of Directors appointed the independent, non-executive Director, Luca Dal Fabbro, representing minority shareholders, as Chairman of the Audit, Risk, Corporate Governance and Sustainability Committee.
[6] Following the previously mentioned resignation of Stefano Saglia as a Director, changes were made to the composition of Board Committees, including the appointment of a new member of the Remuneration Committee. Further details are provided in the sections on events after 31 December 2018 in the consolidated and separate financial statements.

Risk management

We closely monitor all types of risk and identify the most appropriate sustainability initiatives to mitigate their impact. For this purpose, we have put in place specific safeguards, tools and organisational structures.

In view of the distinctive and specific nature of the core business, regulated primarily through a government concession arrangement and by the Regulatory Authority for Energy, Networks and the Environment (ARERA, or the *Autorità di Regolazione per Energia reti e Ambiente*), Terna is exposed not to the usual price- and market-related risks (or is so only to a limited extent with regard to its non-regulated and overseas operations), but to regulatory and legislative risk, as well as the traditional operational risks which have become increasingly critical with the energy transition in progress.

Regulatory risk derives from potential changes in the criteria used to determine regulated revenue, particularly following a multi-year review of the regulatory framework. Legislative risk relates to potential changes in Italian and European laws governing matters relating to the environment, energy, tax and social aspects (above all labour and tenders).

Risk management actors

From an organisational point of view, the key players in the risk management process are:

- **Audit, Risk, Corporate Governance and Sustainability Committee:** this committee consists of independent members of the Board of Directors and supports the Board of Directors in making assessments and decisions regarding the Internal Control and Risk Management System (ICRMS). Periodically, it is called on to assess the adequacy and efficacy of this system with respect to the nature of the Company and its risk profile;
- **Chief Risk Officer (CRO):** the CRO has two main tasks: to define the Company's risk assessment, management and control policies and coordinate all the entities involved in the ICRMS, to maximise efficiency and minimise the duplication of work.
- **Security and Services department:** through its Risk Management unit, this department guarantees effective oversight and coordination of the various risk management processes used by the Group.

Risk management methodology

The Terna Group has used **Enterprise Risk Management (ERM) methodology** for some time, appropriately tailored to its own situation as grid operator, to identify, assess, control and monitor its risks. ERM analysis has enabled the Group to create a detailed map of its operations and their inter-relations, which are associated with a catalogue of over a thousand operational risks of differing importance in terms of critical nature and impact. This has provided a significant body of information for use when assessing critical areas.

Over
1,000
operational risks

Alongside the adoption and application of an integrated risk management model, Terna has also developed an enterprise Governance, Risk and Compliance (eGRC) IT tool, allowing it to simplify and classify information to obtain a standardised and comparable representation of the Group's risks and produce an integrated report for senior management.
The risks to which the Terna Group is exposed may therefore be grouped into three macro-categories: **Governance & Compliance** (described below), **Operations and Strategy & Financial** (details are provided below in line with the corresponding activities).

GOVERNANCE AND COMPLIANCE RISK MANAGEMENT

Governance and Compliance models

By continuously monitoring Governance, Integrity Compliance risks, and based on **best governance and compliance practices**, Terna:

- has adopted a *Code of Ethics*;
- has implemented an *Organisational and Management Model, as provided for in Legislative Decree 231 of 2001, as amended;*
- has approved *"Compliance rules for the prevention of administrative offences and violations relating to market abuse" and adopted Anti-corruption Guidelines"*;
- has adopted the *"Global Compliance Program"*;
- has appointed a *"Manager responsible for financial reporting"*;
- has adopted an Integrated Management System, laying down the criteria for the management of Quality, the Environment, Occupational Health and Safety, Energy, Anti-corruption efforts, Information Security, Multi-site Test Lab Security, Live-Line Working and the Calibration Centre;
- has developed an *Information Security Governance Model*;
- has implemented a *Privacy Model* in compliance with EU Regulation 2016/679;

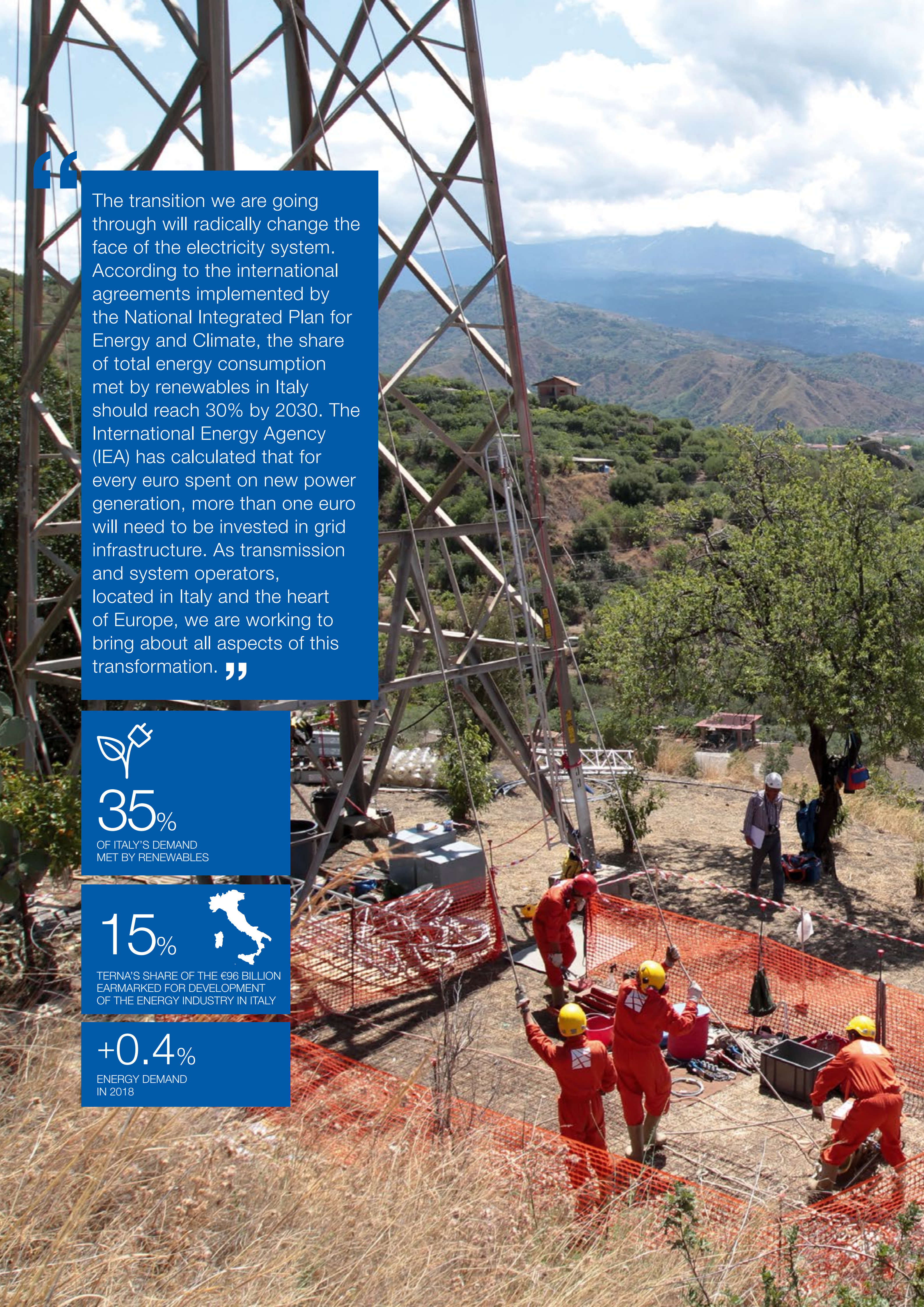
The Group has also adopted a *"Trade Compliance Policy"* on overseas trade and established a *Fraud Management team,* accompanied by an *Anti-Fraud Model*.

Fraud management

The approach to combating fraud is based on the **continuous monitoring of processes, in order to determine the level of exposure to the risk of fraud and the related risk factors**. The aim is to adopt suitable governance measures and increasingly rigorous controls, such as, for example, the definition of new internal rules and procedures.

Adhering to the principle of **integrated security**, the implementation of which requires a constant commitment to identifying potential internal vulnerabilities, assessment and control of the causes and preparation of appropriate measures designed to resolve and prevent their occurrence.

For this purpose, **Terna** has developed a model for identifying critical areas and monitoring potential organisational and operational issues that might give rise to the occurrence of fraud.



“The transition we are going through will radically change the face of the electricity system. According to the international agreements implemented by the National Integrated Plan for Energy and Climate, the share of total energy consumption met by renewables in Italy should reach 30% by 2030. The International Energy Agency (IEA) has calculated that for every euro spent on new power generation, more than one euro will need to be invested in grid infrastructure. As transmission and system operators, located in Italy and the heart of Europe, we are working to bring about all aspects of this transformation.”

35%

OF ITALY'S DEMAND MET BY RENEWABLES

15%

TERNA'S SHARE OF THE €96 BILLION EARMARKED FOR DEVELOPMENT OF THE ENERGY INDUSTRY IN ITALY

+0.4%

ENERGY DEMAND IN 2018

2

The energy environment

Macroeconomic environment

Global economic expansion has continued, whilst showing signs of a slowdown compared with 2017. In the euro area, this trend was associated with the uncertainties generated by trade wars, Brexit and more specific geopolitical issues.

In 2018, the **Italian economy gradually weakened**, after a favourable start encouraged by the positive conditions that characterised 2017.

Moderate expansion at global level

Global economic expansion continued, albeit with a modest slowdown compared to 2017. In 2018, however, the synchronous growth phase was interrupted. The United States saw accelerated GDP growth, supported by expansionary fiscal measures, whereas in the euro area and Japan GDP growth was less dynamic than in the previous year. Economic expansion also weakened in emerging economies, which were affected by a strengthening dollar and the resulting financial tensions.

Slowing GDP in the euro area

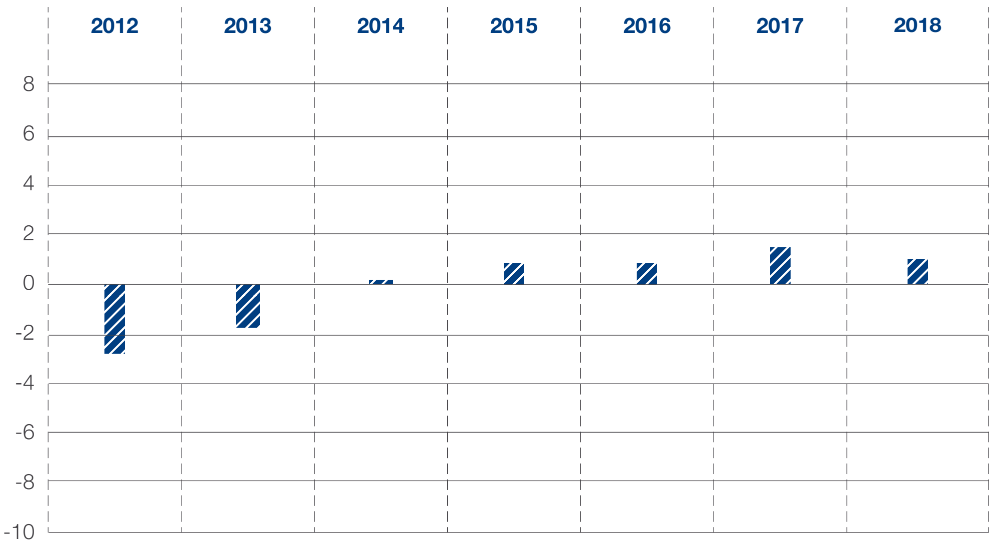
The latest estimates for the euro area in 2018 put GDP growth at 1.8%, marking a slowdown compared with the 2.4% growth recorded in 2017, which is the highest figure for the last ten years (source: Eurostat release of 14 February 2019). **The slowdown is linked to the increase in uncertainty factors** generated by trade wars, the Brexit process and other more specific geopolitical elements. During the year, monetary policy continued to strike an expansionary note, despite the reduction in the volume of securities purchased by the ECB.

In 2018, the Italian economy registered GDP growth of 0.9%, slipping back from the 1.6% growth achieved in 2017 (source: ISTAT, Italy's Office of National Statistics, March 2019). Annual growth was driven by domestic demand. However, signs that the economy was running out of steam emerged during the year, resulting in a technical recession as a contraction in GDP was registered in the last two quarters of 2018, after sixteen quarters of continuous growth. The economic slowdown, while partly due to absence of the positive conditions of 2017, was also affected by an upsurge in internal and external elements of uncertainty. These factors have weighed heavily on business confidence, leading end consumers and investors to think hard before going ahead with their plans.

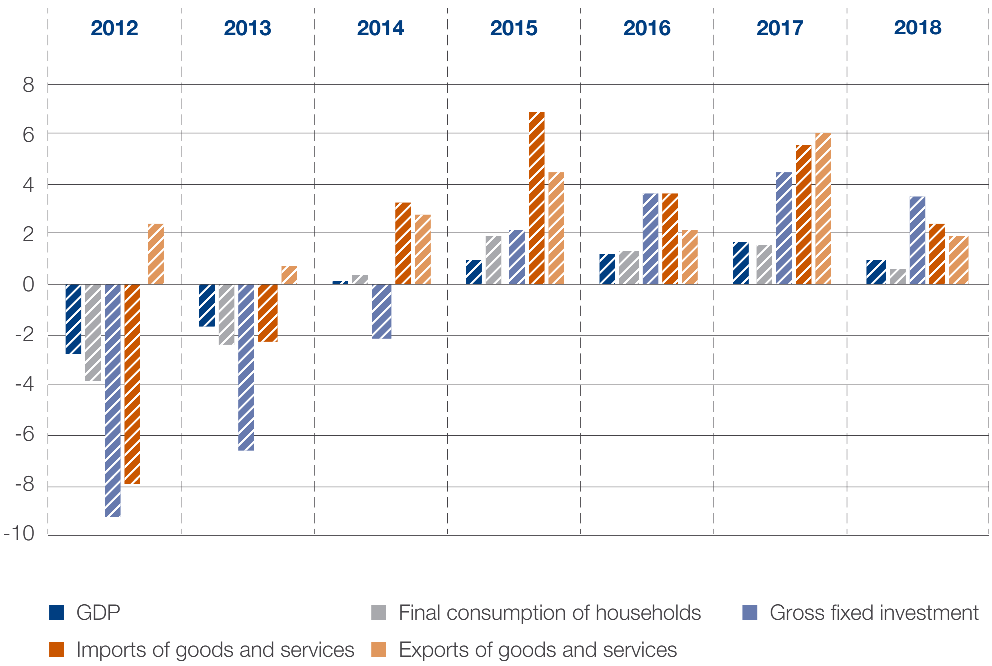
+1.5%
Italian Industrial output in 2018

Industrial production also shows signs of weakness. In 2018, it grew by 1.5% compared to the previous year (up 0.8% with the same number of working days), almost halving the growth recorded in 2017. In addition to this contraction, the last months of the year saw a steady slowdown in activity, with production levels below those of the previous year across almost all sectors.

ITALIAN GDP AND KEY ECONOMIC INDICATORS IN VOLUME TERMS
% annual change in volume



+0.9%
Italian GDP
in 2018



Increased
uncertainty holds
back growth
in 2018

The energy sector

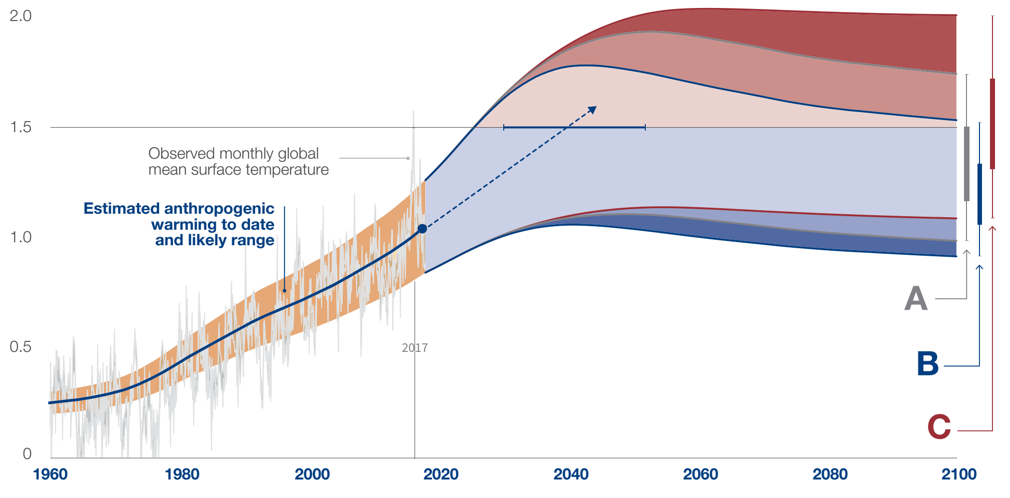
The energy transition is an irreversible process. Changes in generation technologies and consumption patterns, together with international directives and guidelines implemented via Italian energy sector regulations, require Terna to take on a leading role in the current energy transition process. Of the €96 billion of investment earmarked to develop the energy industry in Italy, Terna's investment programmes account for 15%.

The 2019 - 2023 scenario

In order to combat global warming, international climate and energy agreements set an emissions target aimed at **keeping the rise in global temperature below 2°C compared to the pre-industrial level**, and preferably below 1.5°C (COP21 - Paris Agreement, 2015).

The IPCC* study, published on 6 October 2018, officially announced that global warming is already within the range of 0.8 to 1.2 °C, with a rising trend of 0.2 °C per decade.

GLOBAL WARMING COMPARED TO THE PERIOD 1850-1900 (C°)

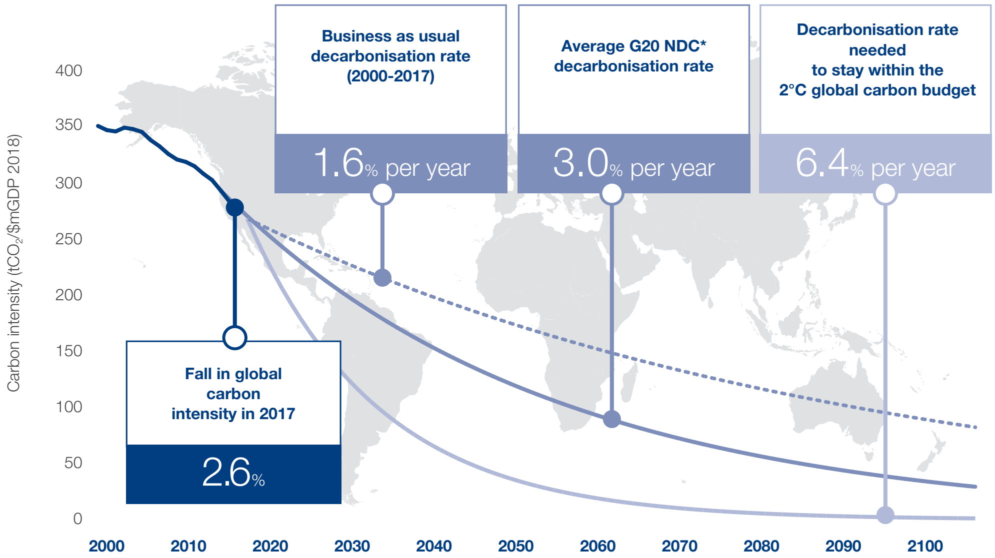


** Intergovernmental Panel on Climate Change*

BASELINE SCENARIO (A)	• Global CO_2 emissions reach net zero by 2055. • Emissions of greenhouse gases other than CO_2 will be reduced from 2030.
SCENARIO (B)	**Improvement hypothesis:** global CO_2 emissions reach net zero by 2040 (greater likelihood of limiting the temperature rise to 1.5 °C).
SCENARIO (C)	**Worsening hypothesis:** emissions of greenhouse gases other than CO_2 are not reduced from 2030 (less likelihood of limiting the temperature rise to 1.5 °C).

To prevent warming from rising above 2°C compared to the pre-industrial **level, the global economy should commit to cutting its carbon intensity by 6.4% per year until 2100**. A necessary condition for achieving the COP 21 targets is decarbonisation of the electricity sector together with acceleration of the decoupling of economic growth and energy consumption.

LOW CARBON ECONOMY INDEX 2018: TRANSITION LEVELS

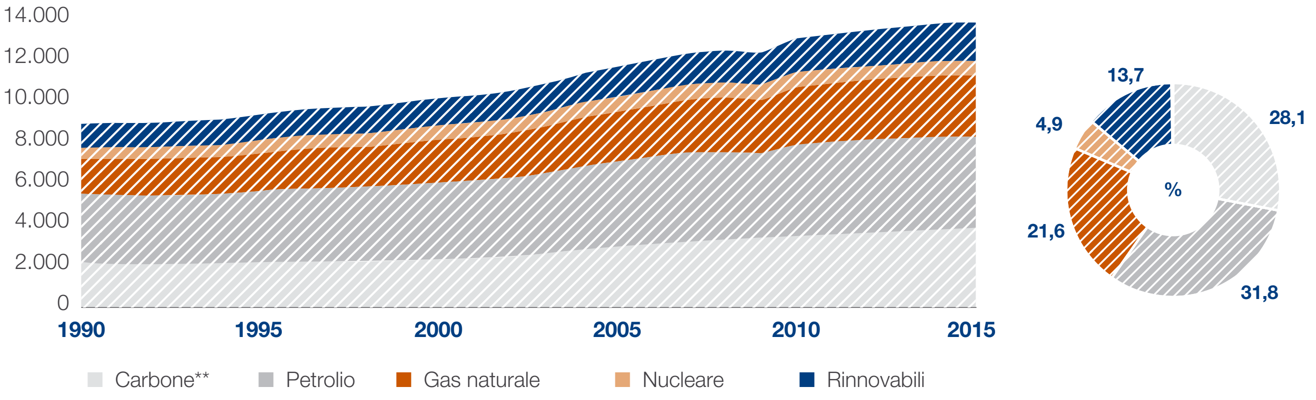


** NDCs: nationally determined contributions*

World primary energy consumption is growing steadily. In 2015, the RES share of primary energy consumption was approximately 14%, almost the same as 25 years previously, despite the growth of RES in the electricity sector.

TOTAL SUPPLY OF PRIMARY ENERGY* AT GLOBAL LEVEL

2015 LEVELS



* Excluding electricity trading..
** In the chart, peat and oil shale were aggregated with coal, where relevant.

Source: International Energy Agency 2017.

Guidelines at european level

The 2018 European guidelines for the development of the energy sector are set out:
- in the guidelines and regulations of the European Union's **Clean Energy Package**;
- in **Regulation (EU) 2018/1999** which established the Governance of the Energy Union and Climate Action, in line with the Paris Agreement of 2015 (COP21) and the United Nations Sustainable Development Goals (SDGs).

Almost at the same time, **two Directives regarding energy sector regulations and policies were published**:
- the Energy Efficiency Directive (EU) 2018/2002;
- the Renewable Energy Directive (EU) 2018/2001.

The United Nations SDGs

Approved by 193 member states of the United Nations in September 2015, the 17 Sustainable Development Goals (SDGs) form the heart of the 2030 Agenda, the global planthat aims to eradicate poverty and promote economic prosperity, social development and protection of the environment.

Terna is playing a central role in enabling the energy system's transition to one in which production is based on renewable sources.

For further details on Terna's commitment to the SDGs, reference should be made to the Sustainability Report.

Key SDGs for Terna

Terna's activities and its mission coincide almost entirely with the SDGs and the related targets, especially Goals 7, 9 and 13.

Ensure access to affordable, reliable, sustainable and modern energy for all.

Build resilient infrastructure, promote inclusive and sustainable industrialization and foster innovation.

Take urgent action to combat climate change and its impacts.

Resolutions at national level

In line with these guidelines, at the end of 2018 the Italian government finally prepared a **Proposal for an Integrated National Plan for Energy and Climate (PNIEC)**, carried out by the Ministry of Economic Development, the Ministry of the Environment and Protection of Land and Sea and the Ministry of Infrastructure and Transport, which provides key guidelines on the development policies for the national Energy System.

The document - which was submitted to the EU at the beginning of 2019 and will soon be subject to consultation with key stakeholders - does not differ widely from the SEN (National Energy Strategy) in quantitative terms, but it does propose some important revisions to the benchmark targets and is closely linked to the five Energy Union dimensions.





PROPOSAL FOR AN INTEGRATED NATIONAL PLAN FOR ENERGY AND CLIMATE - PNIEC	THE 5 DIMENSIONS
• For final energy consumption: 116.6 Mtep by 2020 and 103.8 Mtep by 2030.	Energy efficiency
• RES to increase from 18.6% in 2020 to 30% in 2030 as a share of total energy consumption. • In the electricity sector, the increase will be from 34.1% in 2017 to 55.4%, compared to expected gross domestic electricity consumption.	Decarbonisation
• Competitive auction mechanisms. • Promotion of self-consumption for smaller power plants and renewable energy communities. • Full deregulation of the retail market.	Internal energy market
• Introduction of the Capacity Market. • Development of the grid to facilitate integration with renewable production plants and resolve congestion. • 6,000 MW expansion of central storage, pumping and electrochemical plants.	Energy security
• In the industrial sector, reconversion of infrastructure to improve sustainability. • Additional measures to combat energy poverty.	Research, innovation and competitiveness

To **reduce energy demand**, it will be necessary to deploy major initiatives. The expected reduction in final energy consumption will result in overall savings of 51.4 Mtoe, and development of renewable resources that will enable an increase in the consumption of RES as a share of total consumption.

Even more challenging are the goals set for the electricity sector, which will see a rise in the share of total electricity consumption represented by renewables from 34.1% in 2017 to 55.4% in 2030. This will increase the amount generated from renewables to 186.8 TWh by 2030, compared with 113.1 TWh in 2017.

Sustainable growth will also be enabled through the development of new technologies - such as **electric vehicles** (up to 6 million vehicles by 2030, including hybrid and fully electric models) - and **applications relating to air conditioning** that ought to be used more widely, in view of the energy efficiency savings they offer. Finally, a measure adopted in the 2017 SEN for the electricity sector regarding the phase-out of coal for power generation by 2025 is maintained.

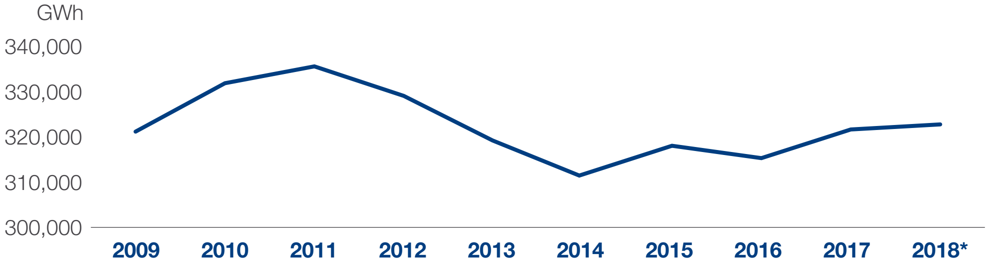
6 million
ELECTRIC VEHICLES BY 2030

The regulatory measures regarding the **security of supply for energy**, above all electricity, are dependent on the introduction of the Capacity Market, as well as revision of the Emergency Plan for the Security of the Electricity System (*piano di Emergenza per la Sicurezza del Sistema Elettrico or "PESSE"*).
There are also plans to increase the capacity of storage systems (up 6,000 MW, net of distributed stockpiles), above all through the use of pumps, and for further expansion of interconnections with neighbouring countries. **Investment in resilience**, in relation to transmission grids and interconnector projects, will also play a major role, by helping to increase the network's ability to cope with increasingly frequent extreme weather events and the emergencies they create, including boosting coordination at European level. This has taken on added importance given the structural changes currently taking place in the electricity systems of many European countries, primarily linked to progressive decarbonisation and the reduction in nuclear generation capacity.

Electricity demand and production in Italy

Terna monitors domestic demand trends and takes appropriate actions, in full implementation of EU directives.

DEMAND TREND OVER THE LAST 10 YEARS



*provisional data

Demand for electricity in Italy

Demand for electricity in Italy amounted to 321,910* GWh in 2018, an **increase of 0.4% compared with 2017**, which registered a rise of 2% compared with the previous year.

ELECTRICITY BALANCE IN ITALY (GWH)	2018**	2017	Δ	Δ%
Net production	280,234	285,265	(5,031)	(1.8)%
From overseas suppliers (imports)	47,179	42,895	4,284	10.0%
Sold to overseas customers (exports)	(3,270)	(5,134)	1,864	(36.3)%
For use in pumping***	(2,233)	(2,478)	245	(9.9)%
Total demand in Italy	321,910	320,548	1,362	0.4%

** Does not include demand for energy for ancillary services related to electricity production.*
*** Provisional data.*
**** Electricity used for pumping water, for sole subsequent use in electricity production.*

Monthly demand for electricity in Italy in 2018* was slightly higher in most months of the year compared with the previous year.

MONTHLY DEMAND FOR ELECTRICITY IN ITALY (2018* vs. 2017)

** Provisional data.*



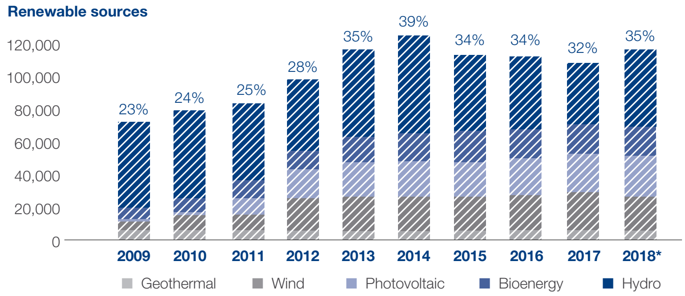


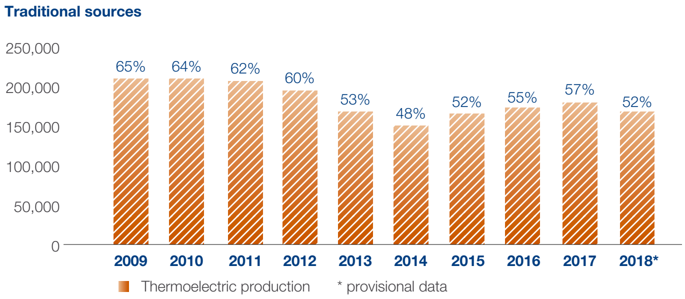
Meeting demand and energy production

In 2018 approximately **35% of total energy demand was met by renewable energy sources**, up from 32% in 2017.

This performance is mainly due to the strong recovery of hydroelectric production (up 31% on 2017), which offsets the slight contraction in other renewable sources.

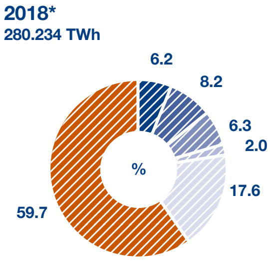
PERFORMANCE OF PRODUCTION SOURCES IN TERMS OF DEMAND[7]

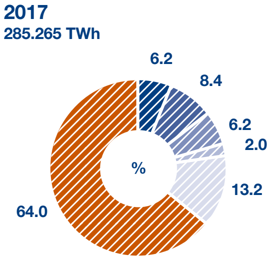




The two charts show the performanceof renewable production in Italy over the last ten years, compared with the performance of thermoelectric production over the same time period.

NET ELECTRICITY PRODUCTION BY SOURCE





- Net wind production
- Net photovoltaic production
- Net biomass production
- Net geothermal production
- Net hydroelectric production
- Net thermoelectric production

* provisional data

As can be seen from the charts, **the progressive increase in production from renewable sources has been matched by a similar reduction in thermoelectric production.**

This demonstrates Italy's commitment to observing European Community directives requiring that renewable sources account for over 27% of demand by 2020. From as early as 2012, Italy has achieved, maintained and then improved on this target.

[7] The percentages shown in the two charts compared refer to the share of demand met by renewable sources (blue chart) and thermoelectric sources (orange chart).

European and international relations

We have a strategic role to play in integrating Europe's principal electricity networks: our aim is to build a more secure and efficient system for the benefit of citizens and businesses. As the leading independent grid operator in Europe, we are members of various associations at European, national and industry level.

Opportunities for engagement and dialogue are provided by Terna's membership of the **principal national and international trade associations**, as well as of the leading associations connected with sustainability issues.

Stakeholder	EUROPEAN RELATIONS
ENTSO-E European Network of Transmission System Operators for Energy	ENTSO-E is the European Network of Transmission System Operators for Electricity including 43 operators which is involved in the process of integrating national electricity markets, coordinating the secure operation of interconnected electricity systems and developing electricity transmission grids, in implementation of the EU's Third Energy Package. ENTSO-E's main objectives are to: draw up European network codes, guarantee the coordinated development of the electricity grid at European level by drawing up the European Electricity Grid Development Plan (TYNDP) and the related benchmark scenarios, and draw up the Research, Development and Innovation Plan at European level.
EASE European Association for Storage of Energy	The European association that is responsible for promoting industrial research and development in the field of electricity storage system applications in Europe and around the world and the use of this technology for the transition to a stable, flexible, sustainable and cheaper continental energy system. In particular, EASE is working on the development of a European platform for sharing information in the field of energy storage.
RGI Renewables Grid Initiative	An association consisting of nine European TSOs and eight environmental NGOs which aims to promote the integration of renewable energy sources through the development of electricity grids. RGI is committed to promoting strategic planning and participating in the construction of new power lines, via a meeting platform involving environmental NGOs and European TSOs.

During the year, at bilateral level, Terna initiated a series of contacts with the senior managements of European and non-European system operators, with the aim of **entering into cooperation agreements in areas of common interest**, especially in these sectors:

- technological innovation
- grid development
- electricity system operation.

The **Brussels Office, which has been operating since July 2018**, was set up to strengthen Terna's links with European institutions, including from a technical standpoint, and to take advantage of the Company's technical contribution regarding European matters ahead of implementation of European legislation to reform the electricity sector (the so-called Clean Energy Package) in support of the energy transition.

INTERNATIONAL RELATIONS	Stakeholder
An international non-profit association that conducts research regarding high-voltage grids. It has 58 member countries, and Terna has been appointed as the Chair and Vice Chair of the Italian Committee.	CIGRE - Conseil International des Grands Réseaux Electriques (International Council on Large Electric Systems)
An international association bringing together the 19 leading grid operators worldwide in order to share best practices in the management of electricity transmission grids. Terna chairs the "Reliability and security" group, which deals with the resilience of the electricity system.	GO15 Reliable and Sustainable Power Grids
This association brings together the TSOs from 19 Mediterranean countries, with the aim of promoting the standardisation of development plans and the coordinated management of grids. The association also works to facilitate the creation of a legislative and regulatory framework designed to drive the development of interconnection projects and promote the exchange of electricity between electricity systems in the Mediterranean area. Terna hosts the association's registered office and operational headquarters in Rome and appoints its Secretary General, as well as chairing the Technical Committee, which is responsible for planning the Mediterranean electricity grid.	Med-TSO Mediterranean Transmission System Operators
The associations aim to promote renewable energy and energy efficiency projects in the southern Mediterranean and sub-Saharan Africa, enabling the development of projects in these areas to meet local energy needs.	RES4MED&AFRICA (Renewable Energy Solutions for the Mediterranean & Africa)
The Italian national committee of the WEC, an international organisation that brings together operators from over 90 countries, with the aim of promoting a sustainable energy system worldwide.	WEC (World Energy Council (Italian committee)

During 2018, in addition to consolidating its presence in industry associations, Terna actively participated in **World Energy Week held in Milan** in October, which was attended by the world's leading energy experts to discuss the current energy transition.

In addition, in synergy with this event, **Terna hosted a meeting of the CEOs of the 19 largest electricity system operators in the world belonging to the GO15 association**, which focused on the importance of having increasingly resilient and sustainable electricity infrastructure as a key factor in the energy transition.

The Company also continued to participate in the activities of organisations with a broader thematic scope (such as Diplomacy, the Council on Foreign Relations, etc.) in order to monitor the socio-political and economic contexts in which to develop or consolidate its business, focusing its attention on Latin America and the Mediterranean basin. In Latin America, in 2018 Terna joined the regional body, **CIER (Comision de Integracion Energetica Regional)**, participated in by energy companies and local authorities, which pursues the objective of regional energy integration through cooperation between its members.

Regulatory environment

We operate as a natural monopoly in a market regulated by the Regulatory Authority for Energy, Networks and the Environment (ARERA).

Regulated revenue accounts for approximately 86% of the Group's total revenue

Regulated revenue, which represents approximately 86% of the Group's total revenue, mostly derives from transmission and dispatching, subject to regulation by the **Regulatory Authority for Energy, Networks and the Environment (ARERA)**.

In Resolutions 653/2015/R/eel, 654/2015/R/eel and 658/2015/R/eel, ARERA set the tariff regime for electricity transmission, distribution, metering and dispatching services and regulations regarding the quality of the transmission service for the 2016-2023 regulatory period (the fifth regulatory period). This period has been divided into two sub-periods: NPR1 (2016-2019) and NPR2 (2020-2023).

In the first four years, the situation is essentially in line with the past, despite a number of changes and, more generally, a **greater emphasis on output-based regulation**. Instead, for the second-four-year period, ARERA has adopted a new method of regulation for the transmission service, involving the recognition of costs based on the total expenditure incurred (operating expenses and capital expenditure), also known as the **"TOTEX"** approach. Subsequently, in consultation document no. 683/2017/R/eel containing the first guidelines for the introduction of incentive regulation schemes based on overall control of expenditure, ARERA specified a period of 30 months between the decision to adopt TOTEX methodology and its actual implementation. Given that, at the date of publication of this document, the decision to actually adopt TOTEX methodology has not yet been taken, it seems unlikely that the TOTEX approach could start before 2022.

In Resolution 583/2015/R/com, ARERA announced the procedure for determining and revising the **Weighted Average Cost of Capital (WACC)** for a period of six years (2016-2021). This applies to infrastructure services in the electricity and gas sectors and is subject to revision, mid-way through the period, which, with Resolution 639/2018/R/COM, enabled adjustment of the WACC in a predictable and transparent manner in keeping with the economic cycle. The WACC the period 2019-2021 has been set at 5.6%. This is a vital element in guaranteeing revenue stability, a key factor in enabling Terna to complete the substantial investment programme needed to meet the challenges of the energy transition.

A number of key aspects of regulation in the period NPR1 are described below, with regard to allowed revenue for transmission and dispatching services.

Transmission revenue makes up the most significant portion of regulated revenue and is generated from application of the related transmission charge (**TC**), billed by Terna to distributors connected to the National Transmission Grid. This charge pays for the transmission services provided by all transmission service operators, including the owners of residual portions of the grid (external to the Terna Group), and is divided into two components: a power component (equal to 90% of revenue, expressed in euro cents/kW/year) and an energy component (10% of revenue, expressed in euro cents/kWh).

Transmission revenue makes up the most significant portion of regulated revenue

The **dispatching service charge (DSC)** aims to recompense Terna for carrying out the activities relating to the dispatching service and is billed by Terna to users of the dispatching service in proportion to the quantity of energy dispatched.

Allowed costs that combine to determine the TC and DSC components are attributable to three main categories, as summarised below:

THE THREE MAIN TYPES OF ALLOWED COST

Determined on the basis of the Regulated Asset Base (RAB) and the Weighted Average Cost of Capital (WACC). The RAB represents net invested capital for regulatory purposes. It is revalued annually on the basis of data from ISTAT (Italy's Office of National Statistics) on the change in the deflator applied to gross fixed investment and revised on the basis of the performance of investment and disposals. The WACC[8] represents the weighted average cost of equity and debt. The methods of determining and revising the WACC are established by the regulator.	1. To cover the return on capital (RAB)
Allowed depreciation (calculated on the basis of an asset's useful life for regulatory purposes) is revalued annually based on the change in the deflator applied to gross fixed investment.	2. To cover depreciation
Allowed costs are determined by the regulator at the beginning of the regulatory period, based on operating costs recognised during the relevant year (which, in the case of NPR1, was 2014) and increased by any remaining portions of additional efficiencies achieved in the previous two regulatory periods. The resulting amount is revalued annually to take account of inflation and reduced by an efficiency factor designed to ensure that additional efficiencies are, over time, passed back to end users in full.	3. To cover operating costs

[8] The real pre-tax regulatory WACC for the transmission service was 5.3% for the period 2016-2018, and is set at 5.6% for the period 2019-2021.

“With our projects and a substantial injection of investment in network infrastructure we are laying the foundations to promote and support the energy transition underway with a fit-for-purpose electricity system: safe, efficient and that makes increasing use of renewables. Thanks to the unique skills of our people, constant dialogue with local communities and the adoption of innovative solutions, we contribute to the growth and development of sustainable projects for the benefit of Italy.”

€6.8bn

TOTAL CAPITAL EXPENDITURE - FIVE-YEAR PERIOD 2019-2023

EBITDA >4%

AVERAGE ANNUAL GROWTH DURING THE PLAN PERIOD

€1,989.6bn

REVENUE FROM REGULATED ACTIVITIES IN ITALY IN 2018

3 The Group’s strategy and businesses

Strategic Plan 2019-2023

To play a leading role in the sustainable energy transition, by leveraging our distinctive innovation capabilities, competencies and technologies for the benefit of all stakeholders: this is the mission set out in the new *Grids and Values* Strategic Plan for the period 2019-2023.

The electricity sector is rapidly evolving as a result of the radical transition underway, which aims to achieve challenging objectives linked to sustainability, competitiveness and security. In particular, the expected increase in global electricity consumption, in a context of progressive decarbonisation, will see strong development of renewables, resulting in measures designed to integrate them within the electricity system. The pursuit of energy security by strengthening interconnections, the development of power grid resilience and, finally, greater competitiveness in the market, will be the determining factors in the management of complex trading relations between TSOs and other parties operating within the system.
In this context, Terna has redesigned the strategy set out in the 2018-2022 Plan by further stepping up infrastructure investment to meet the new requirements of the electricity system, as part of an integrated approach based on sustainability values, community engagement, skills development and the promotion of innovation.

Consequently, the strategic guidelines for the various areas of the Group have been identified:

- **Regulated Activities in Italy:** to give top priority to all the activities that enable Italy to tackle its energy challenges in a safe, efficient and sustainable way by leveraging the specific characteristics of local areas;
- **Non-regulated Activities:** to launch new services to support the energy transition, taking advantage of opportunities beyond our core activities, to be pursued in line with Terna's mission, and if distinctive and/or of high added value;
- **International Activities:** to leverage the core competencies developed in Italy as a TSO through growth opportunities overseas.

Strategy

TO PLAY A LEADING ROLE IN THE SUSTAINABLE ENERGY TRANSITION,
BY LEVERAGING OUR DISTINCTIVE INNOVATION CAPABILITIES,
COMPETENCIES AND TECHNOLOGIES FOR THE BENEFIT OF ALL STAKEHOLDERS

Pillars

- Stronger core business in Italy
- New services to support the transition
- Overseas use of core competencies

Enablers

- Digital transformation and innovation leadership
- Insourcing of key competencies and flexibility in operations

A key driver of this strategy will be investment in the innovation and digital solutions needed to facilitate proactive management of the system. Attention will also be paid to the development and insourcing of the strategic skills required to cope with projects of growing size and complexity.

The guidelines identified for the Group's various strategic business areas have been divided into appropriate priority actions to be carried out over the life of the Plan.

With reference to **Regulated Activities in Italy**, the system needs a new investment drive to respond to developing needs, with a focus on maximising long-term use and sustainability. The role of proactive system operator in defining the grid's structure and in digitally managing assets should also be strengthened by combining Terna's specialist expertise with the experience gained in the most advanced markets.

Non-regulated Activities will be geared towards supporting the energy transition, especially as an energy solutions provider, involving the development of a portfolio of solutions for companies in the energy efficiency and grid infrastructure sectors, and taking advantage of value added market opportunities for traditional and renewable energy customers.
The connectivity business will continue to be aimed at pursuing opportunities based on leveraging the Group's infrastructure assets.

International Activities will focus on the execution of projects in progress and the management of projects in operation, taking advantage of the Group's specialist expertise by leveraging the new organisational structure. Among the priority actions, the main focus will be on selecting international growth opportunities with a high technological content (a key aspect for Terna) and involving potential agreements/partnerships, including the management of assets without the need to tie up large amounts of capital.

Maintenance of a strong capital structure through robust cash generation will also help to support an attractive dividend policy.

	Plan 2019-2023	Plan 2018-2022	
Net capex	~ €6.2bn	~ €5.3bn	Regulated Italy
RAB (end of Plan)	~ €18.5bn	~ €17.5bn	
CAGR RAB[1]	> 4%	> 3%	
EBITDA	> €400mln	~ €350mln	Non-regulated
Capex	> €300mn	~ €300mn	International
EBITDA[2]	€150mn	~ €150mn	
Capex[3]	~ €700mn	~ €600mn	Digital transformation and innovation
CAGR EBITDA	> 4%	> 3%	Efficiency and value creation
CAGR EPS	> 3%	~ 3%	

1. Calendar RAB, including work in progress.
2. Includes financial income on Uruguay project.
3. Investment already included in Development Plan for Regulated Activities in Italy.

Outlook

As described above, the electricity industry is evolving rapidly as a result of the energy transition underway, which requires the achievement of challenging objectives relating to sustainability, competitiveness and security. In particular, the expected increase in global electricity consumption, in a context of progressive decarbonisation, will see strong development of renewables, resulting in measures designed to integrate them within the electricity system. The pursuit of energy security by strengthening interconnections, the development of power grid resilience and, finally, greater competitiveness in the market, will be the determining factors in the management of complex trading relations between TSOs and other parties operating within the system.

Therefore, in 2019, the Group will be engaged in implementing the provisions of the 2019-2023 Strategic Plan. With specific reference to the total investment of €6.8 billion planned over the next five years, investment of approximately €1.2 billion is planned for 2019.

The principal electricity infrastructure under construction includes the interconnections with Montenegro and France, which are expected to come on stream in 2019 and 2020 respectively, as well as the start of work on the new SA.CO.I.3 project (strengthening of the link between Sardinia, Corsica and the Italian mainland). In addition, the main projects to increase the exchange capacity between the various areas of the Italian electricity market include the Colunga-Calenzano and Gissi-Foggia power lines, while rationalisation of electricity grids in metropolitan areas will concern the cities of Milan, Rome, Naples and Palermo, and primarily entail renewal of the current infrastructure with more technologically advanced connections in line with the best environmental sustainability standards.

In terms of our Non-regulated Activities, in line with previous years, the Group will focus on supporting the energy transition via innovative services. Specifically, Terna will consolidate its role as an Energy Solution Provider, developing services with high added value for businesses and grasping market opportunities for traditional and renewable customers, including in the telecommunications sector, where *connectivity* opportunities will be pursued based on extracting value from the Company’s infrastructure and dark fibre.

Overseas, 2019 will see the Group focusing on completing projects in Brazil, and continuing projects in Uruguay and Peru.

To provide operational support for these initiatives, the Company plans to step up investment in innovation and digital solutions in order to manage the growing complexity of the system. Attention will also be paid to the development and insourcing of strategic competencies, to the strengthening of departments, and to the consolidation of project execution and project control capabilities.

The Plan should ensure sustainability and respect for ESGs, guaranteeing minimisation of environmental impact, involvement of local stakeholders and respect for the principles of integrity, responsibility and transparency on which Terna's business management has always been based.

The above objectives will be pursued whilst maintaining our commitment to maximising cash generation and ensuring a sound, balanced financial structure.

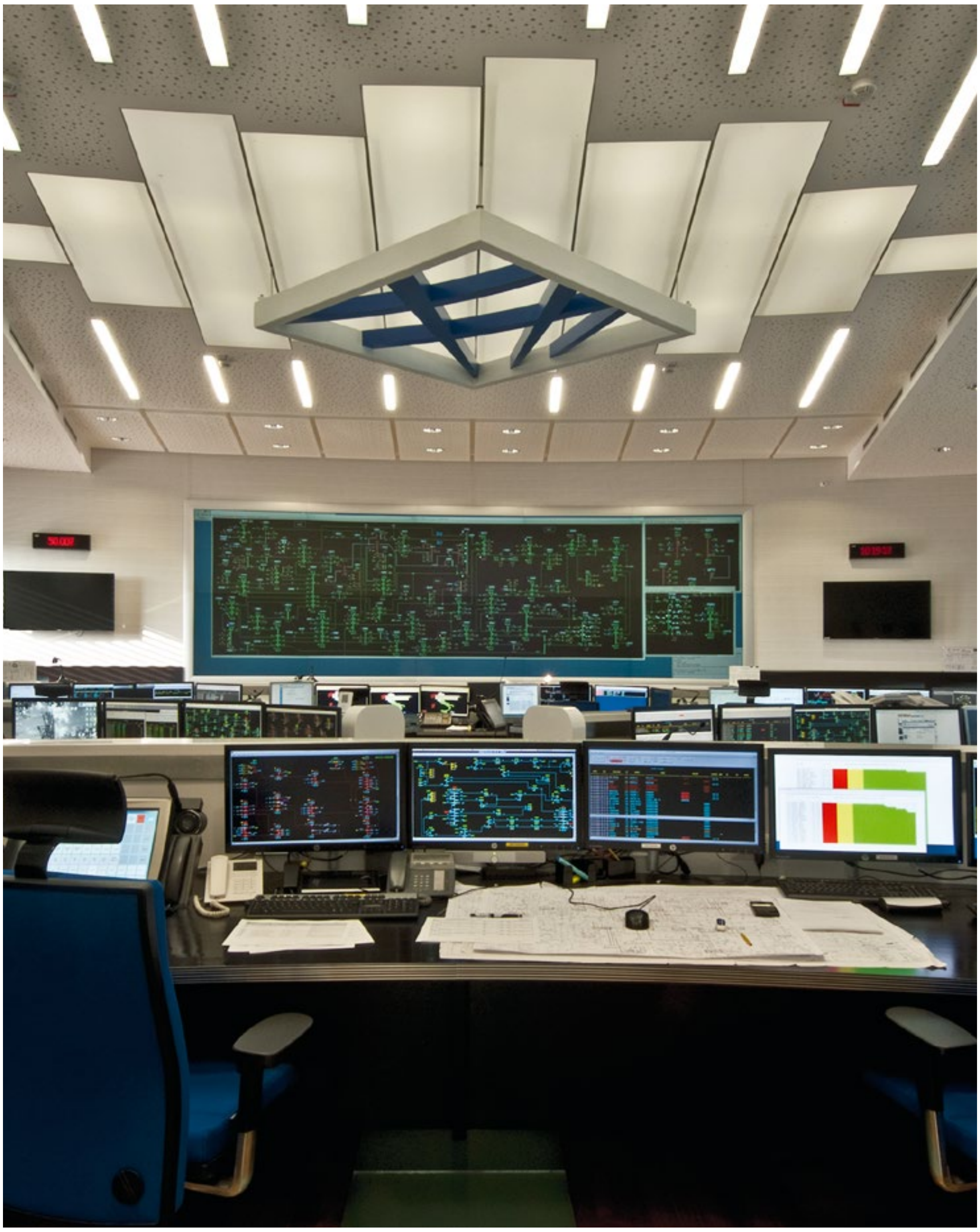
Regulated Activities in Italy

We are responsible for planning, development and maintenance of the grid, contributing our expertise, technology and innovation (as the Transmission Operator). We are responsible for the transmission and dispatching of electricity (as the System Operator), with the aim of ensuring access to electricity for everyone with the highest level of quality and at the lowest possible cost.

3.5%

The cost of the transmission service in electricity bills

(among the lowest with respect to the European average)



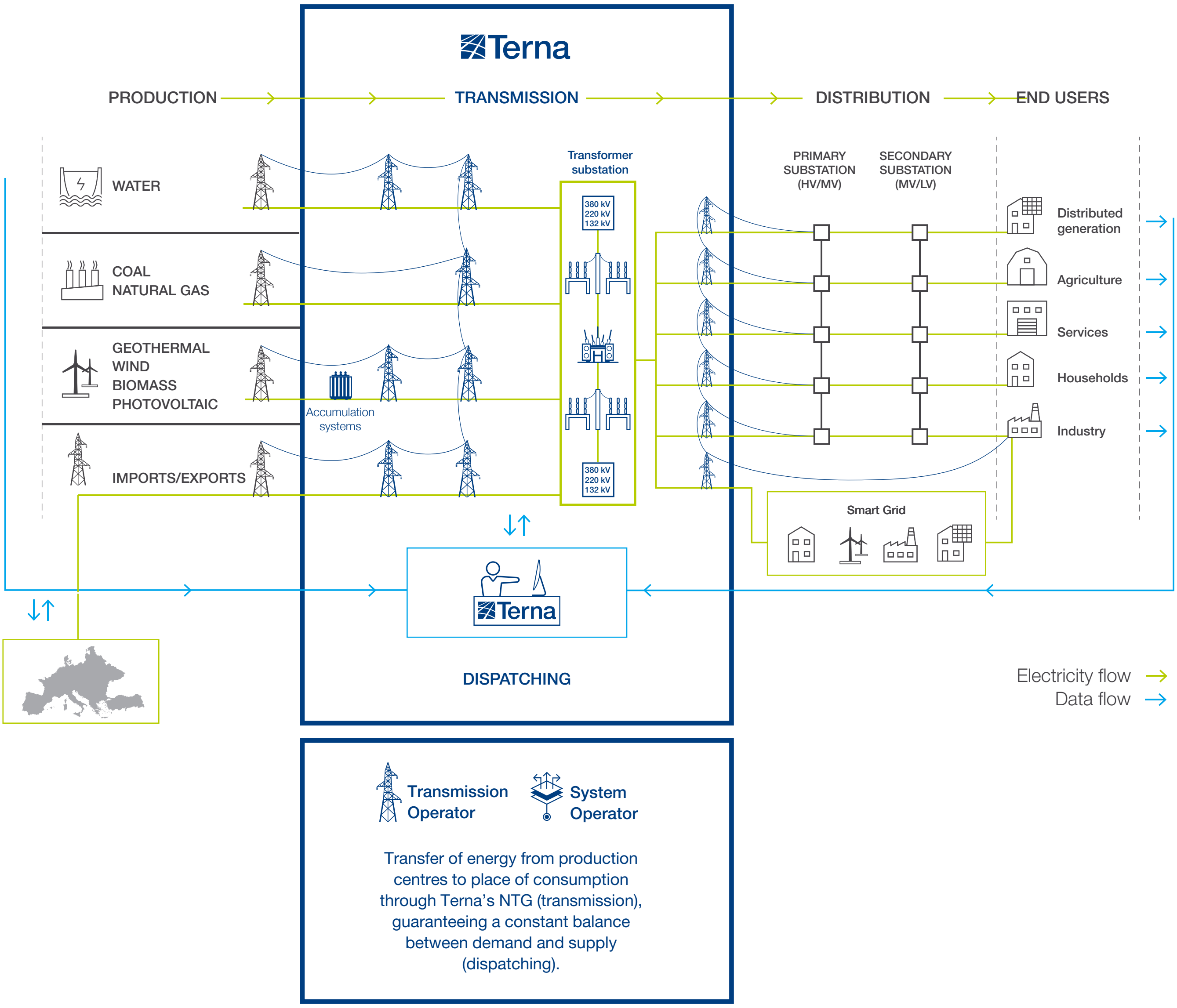
Terna's role in the Italian electricity supply chain

The Italian electricity supply chain consists of four segments: production, transmission, distribution and the sale of electricity.

The Terna Group's main regulated activities are the transmission and dispatching of electricity in Italy.

Terna performs these activities in its role as the Italian TSO (Transmission System Operator) and ISO (Independent System Operator), under a monopoly arrangement and a government concession.

THE NATIONAL ELECTRICITY SYSTEM SUPPLY CHAIN







Electricity transmission

Planning for development of the National Transmission Grid, the performance of construction services and the maintenance of electricity infrastructure are the three areas of responsibility included in the regulated electricity transmission business.

01 Planning of works > **02 Implementation** of development projects > **03 Maintenance** of infrastructure

APPROACH TO SUSTAINABILITY

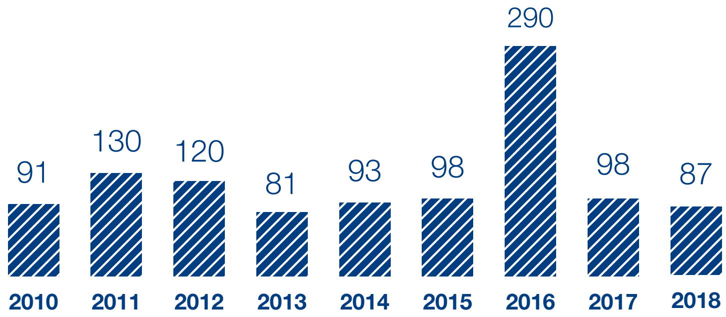
- **Transparency**
- **Dialogue** with stakeholder
- **Awareness** raising

The Group adopts a sustainable approach throughout every stage of the process. This takes the form of transparency in managing the Group's social capital through engagement with the stakeholders directly affected by the Group's development initiatives, with a view to building awareness of the importance of delivering the planned new electricity infrastructure.

Terna's infrastructure

- 881 ELECTRICITY SUBSTATIONS
- 74,442 KM OF CIRCUITS
- 67,671 KM OF LINES (95% overhead)
- N° 4 CONTROL CENTRES
- 723 TRANSFORMERS
- 5 STORAGE SITES
- 6,310 BAYS

Risk management permeates each phase of the operational process for regulated transmission activities. Each risk identified by the Group's adopted ERM methodology is assigned a level of importance. For risks that are above the selected acceptance threshold (risk appetite), possible mitigation actions are identified and implementation times estimated.



1,089 km

OF POWER LINES REMOVED SINCE 2010

The figure for 2016 is exceptional due to the demolition of over 200 km of obsolete power lines in Valtellina, which had been in preparation in previous years. After adjusting for this removal, demolitions amounted to approximately 87 km, in line with previous years (approximately 100 km per year).

Integration within the environment

The main initiatives designed to mitigate Terna's environmental impact are described below.

- **Rationalisation:** Complex initiatives involving several components of the grid, replacing certain components with others of a superior type, thereby eliminating parts of the grid that are of little use following the installation of new infrastructure or adding new elements of the grid to avoid the upgrade of power lines that have reached saturation point. The demolition of obsolete lines represents one of the most important positive contributions that Terna makes to improving the environment: 87 km of lines were demolished in 2018, bringing the total number of kilometres of line demolished since 2010 to 1,089. Demolition is defined as the physical removal of overhead lines (or their replacement with underground cable) and does not include declassified or upgraded lines.
- **Use of pylons with reduced visual impact:** Terna increasingly uses new single-pole pylons with a low environmental impact (occupying only 10 m^2 of ground, rather than the 150 m^2 occupied by the traditional pad/pyramid type pylons); other mitigation measures consist of camouflaging pylons with paint and the use of coloured insulators that enable the new lines to blend in better with the landscape.
- **Use of underground cables:** may eliminate or reduce the typical visual impact of overhead lines. Over 60% of the new power lines entering service during the timeframe of the new Plan will be "invisible", as they will be made of terrestrial or submarine cable.
- **Camouflaging electricity substations:** use of natural engineering techniques for habitat reconstruction and the stabilisation of slopes and embankments.

Electricity substations are significant from an environmental viewpoint partly as they are the principal source of the Group's direct greenhouse gas emissions. These consist of leakages of SF_6 (sulphur hexafluoride), a gas used as insulation in certain electrical equipment (circuit breakers, current transformers and armoured equipment). Leakages as a percentage of installed gas capacity in 2018 stood at 0.38%.

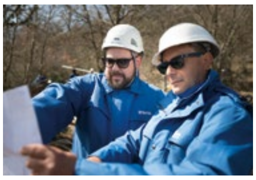
The Group's direct CO_2 equivalent emissions have thus fallen.

TOTAL DIRECT AND INDIRECT GREENHOUSE GAS EMISSIONS - TONNES OF CO_2 EQUIVALENT[9]	2018	2017	2016
Direct emissions			
Total direct emissions	**62,999.2**	**75,792.9**	**61,991.7**
of which: Leakages of SF_6	54,846.1	67,371.4	54,101.9
Indirect emissions			
Electricity[10]	**64,050.5**	**72,489.3**	**74,715.5**

[9] The conversion of direct energy consumption and leakages of SF6 (sulphur hexafluoride) and refrigerant gases into equivalent CO_2 emissions has been carried out using the parameters indicated in the IPCC Fifth Assessment Report (AR5) and the Greenhouse Gas Protocol (GHG) Initiative.

[10] The conversion of indirect electricity consumption is carried out taking into account the share of total Italian electricity production represented by thermoelectric production in 2018. Allocation for the purposes of the production mix was based on the December 2018 issue of the "Monthly Report on the Electricity System", available on the website at www.terna.it.




CARBON INTENSITY - TONNES OF CO_2 EQUIVALENT / REVENUE (€M)	2018	2017	2016
Total emissions (direct and indirect)	127,049.7	148,282.2	136,707.1
Ratio of total emissions to revenue	57.8	66.0	65.9

At the end of their normal lifecycle, the materials used in electricity infrastructure are recovered for reuse in operations. Only a residual portion is sent to landfill and has an impact on the environment.

The percentage of waste recovered amounted to 87% in 2018 (87% in 2017 and 93% in 2016). The effective amount recovered depends on the materials contained in the waste: some of them are easy to separate out and thus reuse (for example, the iron parts of pylons); in other cases, instead, it is not possible or it is too costly to separate the various parts, above all when dealing with the most obsolete equipment. For this reason, annual changes in the amount of waste generated and the percentage of waste recycled should not be interpreted as indicating a trend.

OPERATIONS RISK MANAGEMENT

Terna has established a Risk Observatory with the objective of ensuring proper application of the Company's Corporate Governance policies and the management of information flows to the CRO, as well as monitoring environmental, social, political, authorisation and judicial issues that may impact on the Terna Group's plans for new projects and those currently in progress, while also promptly providing information to senior management. The Risk Observatory is a way of monitoring local issues in the areas in which projects are located, with the aim of taking preventive action or, where an event has occurred, identifying the most correct and appropriate response to mitigate the risk. The resulting actions are discussed by the **Local Communities and Consents Committee**, which meets at least once a month and comprises the heads of the first level departments involved in the entire life cycle of a project (from planning through to operation).

Environmental, social and political issues

The 2019 Development Plan

CAPITAL EXPENDITURE

- **To boost overall exchange capacity with other countries.**
- **To reduce congestion.**
- **To cut energy losses.**
- **To reduce CO_2** emissions as a result of the production mix and lower grid losses.

DRIVERS

DECARBONISATION

1. The electricity system's transition to complete decarbonisation requires use of all the tools necessary in order to fully integrate renewable production plants in order to reduce emissions over the long term, guaranteeing the system's security.

MARKET EFFICIENCY

2. The structure and mix of Europe's generation mix in general and of Italian generation in particular are undergoing a radical transformation, just as transmission lines are being developed in keeping with new European directives regarding Market Design. The adoption of new mechanisms at national level (in particular, the Capacity Market and the reform of the dispatching services market) will have a major impact on development of the electricity system.

SECURITY OF SUPPLY

3. The third driver for the Plan aims to ensure ensures the security of the national electricity system and, at the same time, creates an increasingly resilient system, capable of handling critical events external to the system itself.

SYSTEMIC SUSTAINABILITY

4. The fourth driver consists of the ability to conceive, design and implement following rigorous analysis capable of maximising the environmental and economic benefits.

PROJECT GUIDELINES

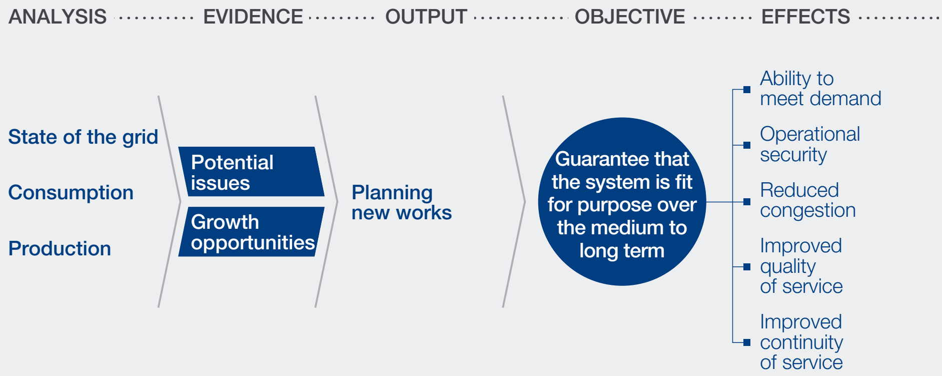
PAYING ATTENTION TO LOCAL NEEDS	GRID OPERATION	ENVIRONMENTAL SUSTAINABILITY
Focus on local development needs and support Italy's new challenges, such as the new electric mobility projects, paying attention to metropolitan areas and reviewing projects in order to make them environmentally-friendly.	Identify and develop initiatives aimed at improving grid operation, with a special focus on enhancing service quality of service and the resilience of the system.	Support and guide the energy transition by connecting and integrating new renewable energy plants.

With regard to decarbonisation, in line with Legislative Decree 93/11 and Resolution 627/16, as amended[11], Terna has included a specific section in the National Development Plan setting out the actions needed in order to make full use of the power produced by renewable plants. The network assessments conducted with a view to facilitating the use and development of renewable production have led to the identification of the work to be carried out on both the primary 380-220kV transmission grid and on the 150-132kV high-voltage grid.

[11] Resolution 627/2016/R/eel, as amended - Provisions for consultation on the ten-year National Transmission Grid Development Plan and approval of the minimum requirements for the Plan, in relation to the assessments for which the regulator is competent.

The national electricity grid planning process

Analysis of the state of the grid (electricity flows through the grid and electricity market trends), and the evolution and distribution of consumption and production, enables Terna to identify critical issues and development opportunities and, consequently, to plan the new works required to ensure that the system is adequate, including in the medium to long term with regard to meeting demand, operational safety, reducing congestion and improving service quality and continuity.



The new works to be carried out are included in the **National Transmission Grid Development Plan**, which is submitted annually to the Ministry of Economic Development for approval. The approval process also includes adoption by the Ministry of the Environment and Protection of Land and Sea (MATTM) in agreement with the Ministry of Cultural Heritage (MIBAC) of the opinion relating to the Strategic Environmental Assessment (SEA) pursuant to Legislative Decree 152/06.

The **NTG Development Plan** sets out the grid development initiatives envisaged over the next ten years, as well as the state of progress of the development works planned in previous years.

The Plan contains all the investments that Terna is committed to carrying out in order to guarantee the efficiency of the grid, the security of supply and of the service and the integration of production from renewable sources in keeping with the objectives identified in the recent **Proposal for an Integrated National Plan for Energy and Climate (PNIEC)**, provided for by Regulation 2016/0375 of the European Parliament and of the Council on the Governance of the Energy Union.

All investment in development of the grid is subject to a prior cost-benefit analysis, comparing the related expenditure with the resulting benefits, expressed in monetary terms, resulting from its implementation.

A positive cost-benefit ratio is a necessary condition for an investment project's inclusion in the Development Plan.

Principal projects for the National Transmission Grid

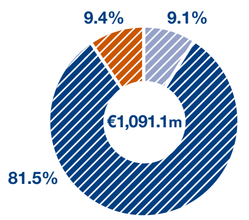
Investment in 2018 up

5.5%

versus 2017

Key to main projects included in the Development Plan

- Lines
- Restructuring in urban areas
- Overseas interconnections
- Grid upgrades



- Incentives for regulated assets*
- Other regulated assets
- Other non-regulated assets

* *Mapping of I-NPR1 and O-NPR1 baskets (Del. 579/17).*

GROUP CAPITAL EXPENDITURE

(€m)	2018	2017	Δ	Δ%
Development Plan	471.7	656.6	(184.9)	(28.2%)
Security Plan	135.9	65.3	70.6	108.1%
Projects to renovate electricity assets	296.0	205.7	90.3	43.9%
- *of which electricity assets (before functional separations)*	*227.6*	*158.4*	*69.2*	*43.7%*
- *of which functional separations*	*68.4*	47.3	21.1	*44.6%*
Other capital expenditure	85.0	35.6	49.4	138.8%
Total regulated assets	988.6	963.2	25.4	2.6%
Other non-regulated assets*	102.5	70.7	31.8	45.0%
TOTAL CAPITAL EXPENDITURE	1,091.1	1,033.9	57.2	5.5%

* *Includes financial expenses of €15 million in 2018 and €13 million in 2017.*

DEVELOPMENT PLAN - €472 million

Interconnectors and lines	Km of circuit	Status	Driver
Italy-Montenegro interconnector	445	⊙	Decarbonisation, Market efficiency
Italy-France interconnector	190	⊙	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Italy-Austria interconnector	24	○	Decarbonisation, Market efficiency, Systemic sustainability
Italy-Switzerland interconnector	100	○	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Italy-Slovenia interconnector	114	○	Decarbonisation, Market efficiency, Systemic sustainability
Sardinia-Corsica-Italy interconnector	540	○	Market efficiency, Security of supply, Systemic sustainability
HVDC Centre South - Centre North	221	○	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
HVDC Italy-Tunisia	200	○	Decarbonisation, Market efficiency, Systemic sustainability
HVDC Mainland Sicily-Sardinia	882	○	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Venetian lagoon cables	20	●	Market efficiency, Systemic sustainability, Security of supply
Sorrento Peninsula interconnector	20	⊙	Systemic sustainability, Security of supply
Reorganisation of metropolitan areas ✓	182	⊙	Systemic sustainability, Security of supply
Foggia-Benevento II power line	18	●	Decarbonisation, Market efficiency, Systemic sustainability
Bono-Buddusò	29	●	Decarbonisation, Security of supply, Systemic sustainability
Messina-Riviera-Villafranca	12	●	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Ciminna-Casuzze	35	●	Security of supply, Systemic sustainability
Chiaramonte-Gulfi-Ciminna	173	○	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Rationalisation in the Mid Piave Valley ✓	90	○	Decarbonisation, Security of supply, Systemic sustainability
Colunga-Calenzano ✓	85	○	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Gissi-Foggia	140	○	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Cassano-Chiari	36	○	Market efficiency, Security of supply
Deliceto Bisaccia	36	⊙	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Upgrade Northern Calabria	10	○	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Paternò-Pantano-Priolo	63	⊙	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Elba-Mainland	35	○	Decarbonisation, Market efficiency, Security of supply, Systemic sustainability
Substations			
8 new substations entered service (San Severo, Quartu Quartucciu, Santa Teresa, San Salvo9, Portella Pero, Siciliana, Ravenna industrial estate, Canino)		●	Security of supply, Systemic sustainability

SECURITY PLAN - €136 million

Projects	Status	Driver
Fiber for the Grid	⊙	Market efficiency, Security of supply, Systemic sustainability
Ice and snow risk mitigation systems ✓	⊙	Decarbonisation, Security of supply, Systemic sustainability
Control devices	⊙	Market efficiency, Security of supply, Systemic sustainability

RENEWAL PLAN - €296 million

The Renewal Plan of electricity assets provides for widespread initiatives across the entire NTG, aimed at improving the reliability of the electricity grid. Work continued in 2018 on replacing assets and individual components in the interests of service quality, adopting the most modern market solutions in terms of plant digitisation (replacement of substation systems with digital technology) and in terms of better environmental compatibility with the host environment (replacement of fluid oil cable connections with extruded insulation and use of machinery with insulation using vegetable esters instead of mineral oil).

Key *

✓ Resilience Plan	○ Awaiting consents/under design	⊙ Under construction	● Completed/in service
Decarbonisation	Market efficiency	Security of supply	Systemic sustainability

* *The other initiatives completed in 2018 are shown in the section "Changes in the dimensions of the NTG" in the annexes.*

Focus on the main works carried out and expected benefits

VENETIAN LAGOON CABLES

Status

Construction of the 132kV power lines between the “Sacca Serenella Primary Substation - Cavallino Primary Substation” and “Fusina 2 - Sacca Fisola” in cable, provided for in the Development Plan approved by the Ministry for Economic Development, have been completed.
This project **was needed to increase the security and reliability** of the grid that serves the Venice lagoon.

Benefits

→ **For the electricity system:** this infrastructure will improve operational security and increase the reliability of the grid that serves the city of Venice, whilst also overcoming the current structural antenna that powers the Cavallino primary substation and simultaneously increasing connections with the portion of the grid associated with the 380/132kV Salgareda substation.

→ **For the country as a whole:** the new infrastructure is expected to result in savings of between €9 and €18 million a year for the Italian electricity system.

→ **For local communities:** in terms of the environment, the infrastructure will make it possible to retire around 7 km of 132kV lines.

Targets

RES integration	Quality of service	Inter-connectors	Congestion solutions	NTG connection	Resilience	RFI integration	SEN 2018
●		●		●			

ITALY-MONTENEGRO INTERCONNECTOR

Status

The interconnector between Italy and Montenegro is a **strategic project at European level, marking a major opportunity for the Italian electricity system** as part of efforts to develop the interconnection between Italy and the Balkans. The project involves construction of a direct current connection, part in submarine cable and part in terrestrial cable, between the substations of Villanova (IT) and Lastva (ME) and covering a distance of approximately 445 km.
Construction, which is currently in progress, will involve the use of engineering and technical solutions capable of minimising the environmental impact. To date, the laying and protection of the first pole of the submarine cable between Italy (Pescara) and Montenegro (Kotor) has been completed, as has the laying of the terrestrial cables. The converters in both Italy and Montenegro are at an advanced stage of completion.

Benefits

→ **For the electricity system:** the work, which when completed at the end of 2019 will provide interconnection capacity of 600 MW, has been included by the European Commission among the Projects of Common Interest (PCIs), after the Commission had already co-financed the feasibility studies in connection with the Trans-European Network (TEN-E) programme. The interconnector will enable an increase in cross-border energy exchange, whilst also improving security and the operational flexibility of the national electricity system and facilitating the integration of energy from renewable sources.

→ **For the country as a whole:** the infrastructure is a key step for the European Energy Union and crucial for integrating the electricity system serving the entire Balkan area into the European system, via Italy. As indicated in the NTG Development Plan and in the ENTSO-E TYNDP, the interconnector will lead to major increase in social and economic welfare in Italy and Europe, facilitating the use of more efficient resources, including production from renewable sources in both Italy and the Balkans. The project also an important role to play in boosting security and service continuity at national level.

→ **For local communities:** the project involves the creation of direct current infrastructure extending a total of 445 km between Villanova (Pescara) and Kotor. There will be minimal environmental impact, as it involves the use of cables placed 1,200 metres beneath the Adriatic sea and buried for the remaining terrestrial portion.

Targets

RES integration	Quality of service	Inter-connectors	Congestion solutions	NTG connection	Resilience	RFI integration	SEN 2018
●		●		●			

ITALY-FRANCE INTERCONNECTOR

Status

The new Italy - France interconnector is a project **unique in the world in terms of the engineering, technological and environmental solutions used**: 190 km of line connecting the substations of Piossasco (Italy) and Grand'Ile (France) through 25 municipalities in the province of Turin, consisting entirely of direct current underground cable.
The power line will be the longest underground line in the world and will have a very low impact on the environment and the local area, thanks to the latest in design techniques.

Benefits

→ **For the electricity system:** the increase in the quantity of energy exchanged will result in a reduction in congestion between the two countries and the possibility of more efficient use of renewable sources. This therefore also makes the interconnector a Project of Community Interest (PCI)..

→ **For the country as a whole:** the infrastructure will increase social and economic welfare at European level, reducing the price differential between Italy and France. Additionally, based on the content of the ENTSO-E TYNDP, the interconnector will increase production from renewables in Italy and improve energy efficiency at European level.

→ **For local communities:** the use of underground cable technology guarantees lower environmental and visual impacts, thereby preserving the Alpine landscape in both France and Italy. The creation of the new infrastructure in the same location as road infrastructure, such as the Fréjus safety tunnel, offers another strategic advantage in terms of social/environmental issues.

Targets

RES integration	Quality of service	Inter-connectors	Congestion solutions	NTG connection	Resilience	RFI integration	SEN 2018
●		●		●			

QUARTU - QUARTUCCIU

Status

The **new 150kV power line linking the primary substations of Quarto and Quartuccio, in the Cagliari area**, entered service in 2018. The new cable link, which runs along the existing road network, is 5.9 km long and goes through the municipalities of Quartu, Maracalagonis and Quartucciu.

Benefits

→ **For the electricity system:** the new power line brings significant benefits for the electricity system in Cagliari, in terms of both the security and efficiency of the electricity service and greater reliability in the event of maintenance.

→ **For the country as a whole:** the new grid development project took one year to complete, during which around 10 companies and 40 workers, many of them local, were involved.

→ **For local communities:** the project plan will enable the subsequent demolition of around 7.7 km of the old "Quartu-Quartucciu" overhead line and 26 pylons, which are located, among other things, in areas close to houses in the Pitz'e Serra neighbourhood, built after the construction of the power line, and in public green spaces such as the Parco Europa. The decommissioning will also be the final phase of grid rationalisation in the Cagliari area provided for in the Protocol with the Sardinia Region. The 150kV "Selargius - Molentargius" line and the power lines passing through the Molentargius - Saline environmental park had already been demolished in 2008 and 2009.

Targets

RES integration	Quality of service	Inter-connectors	Congestion solutions	NTG connection	Resilience	RFI integration	SEN 2018
	●	●		●			●





Infrastructure maintenance

APPROACH

Predictive maintenance of the electricity grid

Maintenance of electricity grid infrastructure is essential in order to guarantee quality of service, security of the assets managed and extension of their useful lives. These operations are carried out on the basis of a predictive and conditional approach. **The tools used to support maintenance activities are subject to continuous innovation**. In particular, the maintenance engineering "engine" is the expert decision support system (DSS) called **MBI (Monitoring and Business Intelligence)** whose engineering models are continuously updated. For scheduling and execution of operations **(WFM - Work Force Management)** software is used, and aerial inspection techniques for the electricity grid have now been consolidated. Terna has, for many years, participated in international benchmarking for the sector, with the aim of sharing best maintenance practices. It has consistently ranked as one of the best TSOs in terms of fault rates and the efficiency of its maintenance process.

2018 MAINTENANCE FIGURES

Infrastructure monitoring and control

28,100 checks on substations of various voltage levels; **visual inspections of 107,700 km of power line, of which 58,484 km using helicopters** (visual + infra-red) with an average total frequency of around 1.5 inspections a year for each transmission line; a further 46,432 km of power line underwent instrumental controls, both from the ground (including with the use of the LLW or live-line working technique), and from the air using helicopters to operate flights that use laser scanning surveys to identify any obstructions, particularly trees; inspections of **44,800 km of underground cable** with a total average frequency of 24.2 inspections per year.

Routine maintenance

Repairs are carried out when signs of deterioration are identified as a result of the monitoring process or by on-line sensors. These indications and any problems identified are processed by the expert system used to support decision-making (MBI - Monitoring and Business Intelligence) since 2005. This system draws up the maintenance plan on the basis of engineering models developed by the Asset Management department.

Vegetation management

During 2018, vegetation was cut back on around 21,200 km of power line; this has to be done to ensure the correct and safe operation of the lines.

Live-line working

Approximately **3,400 checks and line maintenance interventions using live-line working were carried out**. These activities, performed with the line in operation, increase the availability of the infrastructure and help to improve quality of service.

Extraordinary maintenance

Renewal work (the replacement of components and entire systems) was carried out in 2018 in order to prolong the useful lives of power lines and substations. In terms of **power lines, 1,100 km of conductors, 1,400 km of ground wires and 400 pylons were replaced**. in terms of substations, 10 static machines, 70 circuit breakers, 120 disconnectors, 289 current transformers and 130 voltage transformers were replaced. Protection and control systems for approximately 165 HV bays were also replaced.

OPERATIONS RISK MANAGEMENT

Relations with institutional partners

Following an innovative approach to risk reduction policies, **Terna cooperates with institutional partners (national and international regulatory bodies and authorities) with which to share the risks resulting from its activities**. These include the Ministry of the Interior, the Italian tax police, the Fire Service, the National Association of Italian Municipalities, Prefectures and CNAIPIC (the National Centre for Combating Cyber Crime and for the Protection of Critical Infrastructure). In 2018, Terna and the **Civil Protection Department signed a Memorandum of Understanding** with a view to achieving maximum operating efficiency and effectiveness in relation to predicting, preventing and mitigating the related risks and managing and overcoming emergencies. In the agreement, attention is paid to the prevention and management of natural and man-made risks that may be detrimental to the continuity of the electricity service in Italy, and for which Company resources may need to be used. The agreement provides for the optimisation of procedures and the flow of communications between Terna and the Department under both ordinary and emergency conditions. This may include potential integration of the respective information systems, and the creation of specific training programmes and exercises for staff engaged in managing emergencies.

Physical threats to plant

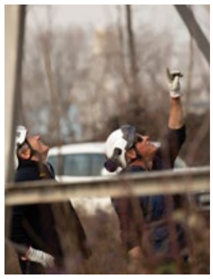
The physical security of substations is assured by using devices, systems and units operating 24 hours a day, seven days a week. **To safeguard the security of the Company's premises and plant, Terna has also developed a surveillance platform called the Integrated Physical Security System for Terna Substations**, which allows the dedicated surveillance centre - the Security Operations Centre or SOC - to continuously monitor (VideoBox) any intrusion alarms and video from 212 substations.
Terna has partnered with the Italy's **Carabinieri police force** to further strengthen its new communications and rapid intervention system, which enables the SOC to quickly alert the police in the event of attempts at forced entry to critical substations, all equipped with video surveillance equipment. The new system has been called "O.D.I.N.O." (Operational Device for Information, Networking and Observation) and is connected, via a secure link, to the centralised operating system used by Carabinieri operations rooms throughout Italy.
In 2018, a technical specification was signed with the State Police, which provided for linking up the video surveillance systems and the SOC to the Police local surveillance technological platform called Mercury NRG. This integration enables reports of geolocalised intrusion events (previously validated by the Terna SOC) to be rapidly and directly sent to the CEN (National Electronic Centre) of the State Police. The reports are then sorted at the Operations Centre of the competent local police headquarters, and passed on to the flying squad in the area.

Supplier risk

Terna uses a Supplier Qualification System, set up pursuant to the related EU directives (Legislative Decree 50 of 18 April 2016 "Public contracts code for the supply of works, services and goods"), for all the main core categories of goods, works and services that Terna intends to procure, established on the basis of strategic importance, degree of competitiveness and annual procurement volumes.







Quality of service

Each segment of the electricity system - generation, transmission and distribution - plays a role in ensuring the availability of electricity in Italy, guaranteeing adequate quality standards and keeping the number of outages below pre-set thresholds.

Terna monitors service continuity through various indicators defined by ARERA (Resolution 250/04) and in Terna's Grid Code.

These continuity indicators are significant for the system, as they monitor the frequency and impact of events that have occurred on the electricity grid as a result of faults or due to external factors, such as weather events. In all cases, the period of observation is four years, a period in which there have been no significant changes, testifying to the high quality of service achieved.

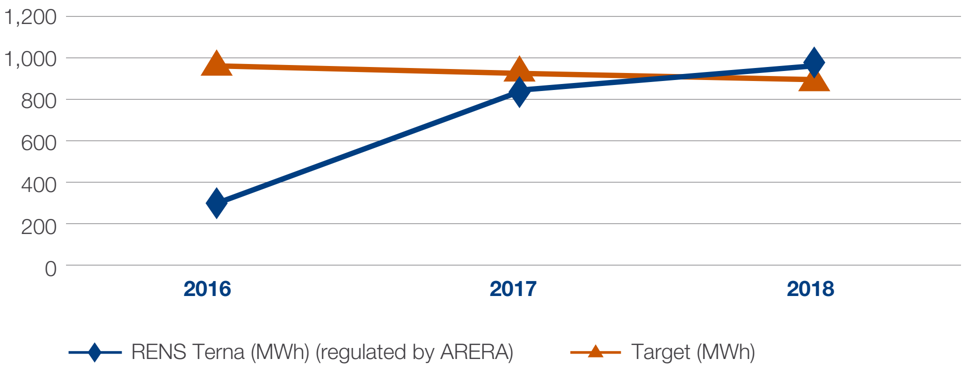
CONTINUITY INDICATORS USED

RENS*

What it measures
Energy not supplied following events affecting the relevant grid**

How it is calculated
The sum of the energy not supplied to users connected to the NTG (following events affecting the relevant grid, as defined in the ARERA regulations governing quality of service).

RENS[12] INDICATOR PERFORMANCE 2016-2018



[12] For the RENS indicator, the targets for 2012-2015 have been set as an average of the RENS 2008-2011 indicator, referred to in ARERA Resolution ARG/elt 197/11, with a 2% improvement in performance required for each year compared with the previous one. The targets for 2016-2023 have been set as an average of the 2012-2015 RENS indicator, referred to in ARERA Resolution 653/15/R/eel, with a 3.5% improvement in performance required for each year compared with the previous one. Since 2016, Terna's bonus/penalty mechanism also includes the performance of the grid operated by Terna Rete Italia S.r.l., established in 2017. The 2018 and 2017 figures are provisional and the RENS indicated takes into account the major incident of 29 October, which affected northern Italy and led to the misalignment of numerous primary substations in the areas around Padua and Milan (above all in the provinces of Belluno, Trento, Vicenza and Brescia), amounting to 625 MWh. Terna is in talks with ARERA with a view to having the event classified as a catastrophe. The RENS indicator calculated on this basis is 969 MWh and falls within the quality of service allowance.

* *Regulated Energy Not Supplied.*

** *The "relevant grid" refers to all of the high-voltage and very high-voltage network.*

As regards the **ASA** indicator, the operating performance shows that ASA has remained stable at a high level over the years (the higher the indicator, the better the performance). This indicator shows that the energy not supplied following a fault on the owned grid represents a minimal part of the total quantity of energy supplied to users of the grid. In particular, availability was 99.99981% in 2017, compared with 99.99974% in the previous year.

CONTINUITY INDICATORS USED

ASA*

What it measures
Availability of the service provided by the NTG

How it is calculated
Based on the ratio of the sum of energy not supplied to users connected to the NTG (ENS) and energy fed into the grid.

QUALITY OF SERVICE (€M)	2018	2017	Δ
RENS bonuses/(penalties)	7.4	7.4	0
Revenue	**7.4**	**7.4**	**0**
Mitigation and sharing mechanisms	7.5	10.6	(3.1)
Contributions to the Fund for Exceptional Events	2.0	2.4	(0.4)
Compensation mechanisms for HV users	0.4	0.6	(0.2)
Contingent assets	(4.8)	(3.1)	(1.7)
Costs	**5.1**	**10.5**	**(5.4)**
TOTAL	**2.3**	**(3.1)**	**5.4**

Existing regulations (set out in Resolution 653/2015/R/eel) envisage a series of mechanisms designed to regulate and encourage improvements in the quality of service provided by Terna. The overall economic effects of the bonus/penalty mechanisms related to quality of service for 2018, compared with 2017, are shown below.

** Average Service Availability.*

Dispatching of electricity

"Dispatching" is the set of activities necessary to ensure that there is a balance between supply and demand in the country's electricity system. The high degree of complexity and coordination necessary to guarantee the correct operation of the system require the presence of a central coordinator, the provider of the dispatching service. This coordinator has control over a high number of both supply-side and demand-side players, and in the last few years also over production from non-programmable renewable sources.

Constant balance between energy demand and supply

Dispatching includes planning for the unavailability of the grid and of production plants over different time-scales, forecasting national demand for electricity, comparing demand for consistency with planned production in the free energy market (the Power Exchange and over-the-counter contracts), the acquisition of resources for dispatching and monitoring power transfers for all the power lines that make up the grid.

This area of operation also includes management of the **Dispatching Services Market (DSM)**, through which the resources for dispatching services are procured.

In particular, "real-time" control of the National Electricity System is ensured by the **National Control Centre**, the nerve centre for Italy's National Electricity System, which coordinates the other centres around the country, monitors the system and dispatches electricity. The Centre intervenes, by issuing instructions to producers and Remote Centres, in order to modify supply and capacity on the grid. To avoid the risk of prolonged power outages, it may also intervene in an emergency to reduce demand.

The following key events in relation to efficient management of the grid took place in 2018.

KEY EVENTS IN 2018

Review of market zones

On 1 January 2019, the new zonal configuration came into force. Compared to the past, the new arrangement has combined the production nodes with limited capacity in Brindisi, Foggia and Priolo with neighbouring zones (the South and Sicily zones, respectively), as well as transferring the Gissi node from the South to the Central-South zone. This change was made in accordance with the European CACM Regulation, which all the regulatory authorities and TSOs of European Union member states must comply with. In particular, **the changes made are aimed atensuring safe operation of the transmission system, as well as boosting the efficiency and cost-effectiveness of the electricity market**. In Resolution 386/2018/R/eel, ARERA has approved Terna's proposed revision of the zonal configuration following the review process carried out in 2018 pursuant to the European CACM Regulation and ARERA Resolution 22/18/R/eel.

TERRE project

The TERRE (Trans-European Replacement Reserve Exchange) project began in 2013 as an early implementation of the Electricity Balancing Guideline (EB GL) regarding the design, development, implementation and management of a platform to share balancing resources among European countries. The project involves 11 countries of which nine are full members (France, the UK, Switzerland, the Czech Republic, Poland, Spain, Portugal, Romania and Italy) and two are observers (Bulgaria and Hungary).

The platform that will manage the TERRE process, called Libra, **will enable the exchange of Replacement Reserves (RR)** among participating countries which, in the current Italian dispatching market, corresponds to the share of the tertiary reserve that can be activated in more than 15 minutes. Access to Libra is only granted to TSOs, which will be responsible for collecting offers from their respective local operators and then submitting them to the platform, together with the capacity available among the market zones and the TSO's own RR needs.

The introduction of Libra will contribute to the creation of a single European balancing market, thereby increasing the security of the electricity system in terms of the availability of reserves that may be activated.

Aggregate Virtual Mixed Units

Following the approval by ARERA of Resolution 300/2017/R/eel, in 2017, two pilot projects regarding UVAC (Aggregate Virtual Consumption Units) and UVAP (Aggregate Virtual Production Units) were launched in order to diversify the type of enabled resources for the Dispatching Services Market (DSM), in line with the principle of technological neutrality, and to increase the amount of resources available to ensure greater reliability and security of supply.
On 1 November 2018, the two projects were merged into a new pilot project relating to UVAM (Aggregate Virtual Mixed Units) which enables **aggregate participation in the DSM, not only regarding electricity demand and distributed generation, but also storage systems** (including charging stations for e-mobility).
The dispatching services for which the authorisation of UVAMs may be requested, both upstream and downstream, are: congestion resolution, the "rotating" tertiary reserve, the "replacement" tertiary reserve and balancing.

Black start simulations

Black start simulations are needed to check that the electricity system is working properly and to improve its efficiency by ensuring a rapid reboot of the system in the event of a blackout. In 2018, **four blackouts were successfully simulated, followed by the related black starts**. The simulations involved all of Terna's regional areas; two were carried out in the North-west Area (including one in Sardinia), one in the North-east Area and one in the Central-South Area.

Dynamic Rating

With a view to ensuring ever greater flexibility in the management of our assets, in line with the activities carried out in 2017, the National Dispatching department and the North-west and Central-South Offices studied new Dynamic Thermal Rating (DTR) applications in 2018.

By exploiting the cool conditions of the lines concerned, above all during the winter when loads are highest, the DTR is able **to increase load capacity so as to meet demand in the short term**. The increase in capacity also has the advantage of supporting increased production from renewables plants.

Therefore, as with other DTR applications already in service, a system for recording weather and temperature conditions has been installed.

STRATEGY & FINANCIAL RISK MANAGEMENT

Dispatching

The transition to a new model of distributed generation from renewable sources is rapidly changing the market, with the rise of the prosumer (producer and consumer) model, which is progressively replacing the traditional consumer. This has resulted in exponential growth of "active" resources connected to the grid.

The risk is linked to difficulties in maintaining observability of the grid in terms of injections and withdrawals of energy. This is having an impact on the ability to forecast residual demand (before self-consumption) and, as a result, on the correct management of generating resources that are able to provide flexible services.

Terna mitigates the risks associated with the management of renewable sources and the "real-time" observability of resources by **using advanced forecasting and planning tools, a supply of new flexibility resources, and innovative data management and analytics solutions.**





+14%

PUN 2018

-30%

PUN 2008-2018

Electricity cost trends

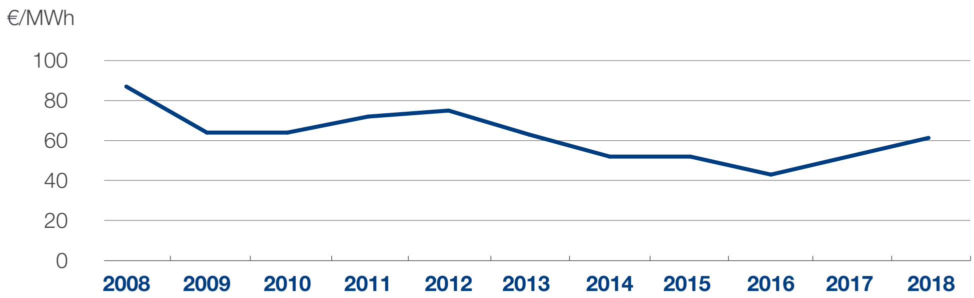
Electricity prices

The average hourly price on the Italian Power Exchange (IPEX[13]/SNP - Single National Price) for 2018 is €61 per MWh, up 14% compared with 2017. The increase reflects rises in demand for electricity (in the Day Ahead Market), and in commodity prices (CO_2 certificates).

The Day Ahead Market, which sets the SNP, is based on supply and demand, although Italy must, by necessity, also take account of its particular geography, with the physical nature of the electricity grid, the widespread nature of its infrastructure and the location of consumption, and the resulting grid congestion. This means that there are a number of "bottlenecks" on the transmission grid, which have made it necessary to identify "market zones" and set transmission limits. Eliminating these bottlenecks is one of Terna's tasks, above all through development of the grid.

The following chart shows **the performance of the SNP from 2008 to 2018, revealing a substantial decline over the period (-30%).**

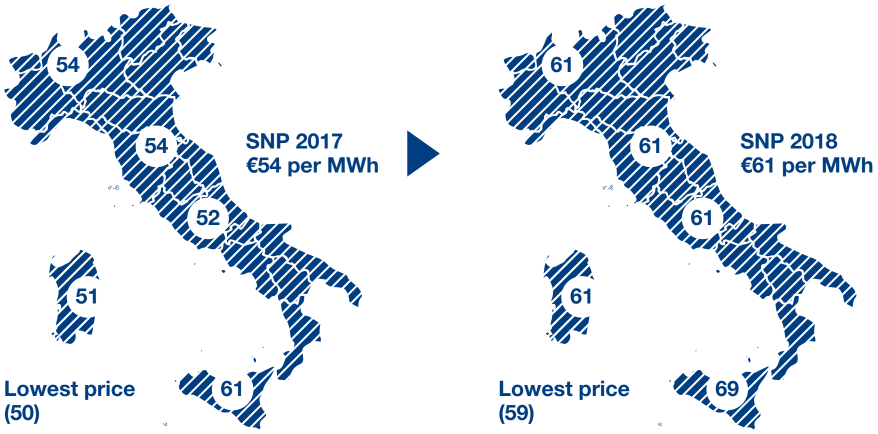
PERFORMANCE OF THE SINGLE NATIONAL PRICE (SNP) FROM 2008



Over the years, prices in the principal zones that make up the Italian electricity market and the Single National Price (SNP) have fallen into line.

[13] IPEX: the Italian Power Exchange.

PERFORMANCE OF ITALY'S SNP AND ZONAL PRICES



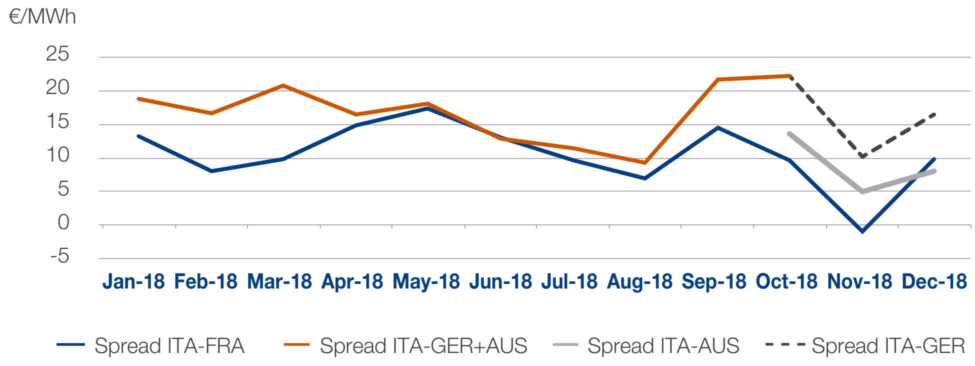
Trade with other countries

Trade with other countries in 2018 resulted in an increase in net imports, which are up 6 TWh on the previous year (up 17% on the previous year).
As usual, during the winter there was a reduction in the quantity of electricity imported, compared with the available transmission capacity in the Northern interconnection. This was primarily due to electrically powered heating systems in northern Europe, and new maintenance work on French nuclear plants.

+6TWh
net imports

Prices on the French (PNX) and Austrian/German (EEX/PHELIX) exchanges, rose in line with the increase in commodity prices (especially CO_2 certificates).

MONTHLY SPREAD FOR ENERGY PRICES COMPARED WITH FRANCE (PNX) AND GERMANY/AUSTRIA (EEX/PHELIX)

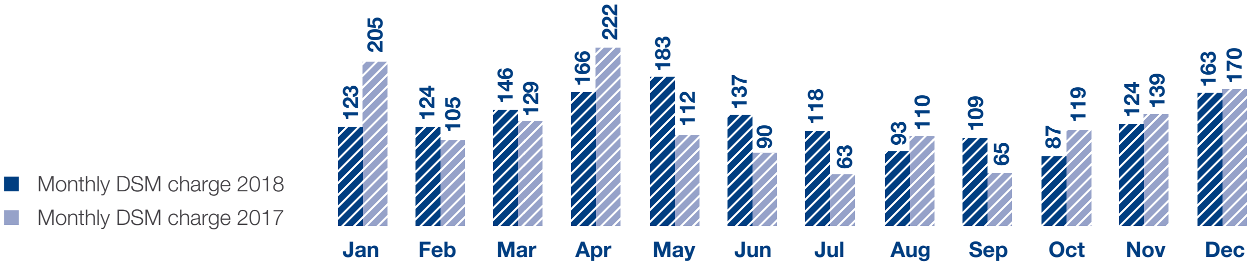


FROM OCTOBER 2018, THE GERMAN AND AUSTRIAN MARKETS WERE DECOUPLED

In particular:

- The Powernext (French price) registered a divergent trend in the cold months of the year during which, traditionally, energy demand in France rises sharply. The average annual price was €50/MWh (up €5/MWh or 12% compared with the previous year).
- Regarding the Phelix (German/Austrian price), it should be noted that, from October 2018, the German/Austrian electricity market has decoupled, and therefore this area no longer has a single price. Consequently, the reference price for trading with Austria is the Austrian one. The average annual price - calculated from January to September as the single price for the Germany/Austria area and from October as the Austrian price - was €46/MWh (up €12 per MWh or 35% compared with the previous year).

ANNUAL AND MONTHLY DSM COSTS (€M)



Dispatching Services Market

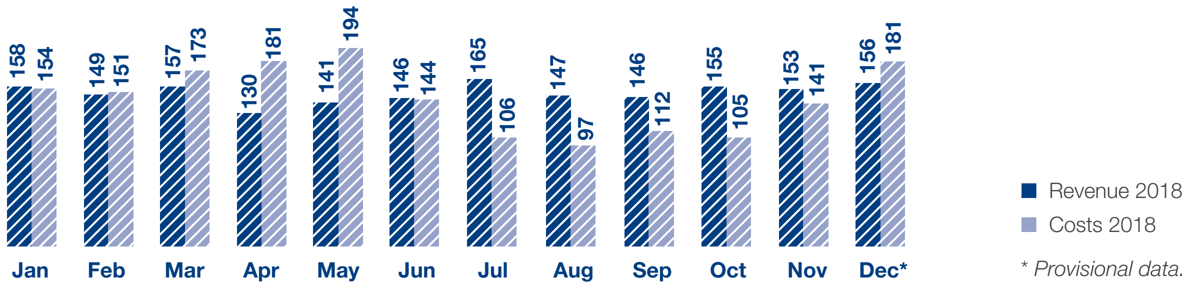
Net DSM charge slightly up in 2018

In 2018, the net charge for using the DSM was €1,573 million, slightly up on the same period of the previous year (€1,528 million). The increase is due above all to:

- an increase in the cost of selection, resulting from the need to meet technical constraints due to a reduction in the number of plants in service as a result of Electricity Market trends;
- a reduction in the cost of managing essential providers of reserve capacity in January compared with the same period in the previous year (in which an increase in selection was registered due to the cold snap in Europe) and in the last three months of the year.

Terna procures dispatching resources on the Dispatching Service Market (MSD) to ensure the security and adequacy of the electricity system.

2018 REVENUE AND UPLIFT COSTS (€M)



** Provisional data.*

Cost of procuring resources on the Dispatching Services Market (uplift)

-14%
the UPLIFT
in 2018

In 2018, the total uplift was €1,741[14] million, down 14% on the same period of the previous year. This was primarily due to a sharp reductions in imbalance costs - in 2018, demand-side and supply-side imbalances generated revenue, compared with an overall cost in 2017 - linked to the impact of new regulations that came into force from September 2017.

Uplift payments are the tool used by the system to recover the net costs deriving from energy-related items from the end user, including the supply of services and energy to cover system imbalances in the DSM, imbalance costs, congestion revenue and the related coverage (CCT, CCC, CCP and DCT[15]) and the cost of the virtual interconnection (the Interconnector).

ARERA Resolution 111/06 (TITLE 4) regulates charges for dispatching services and the connected guarantees. Dispatching charges include the cost of procuring resources on the Dispatching Services Market (known as the uplift), pursuant to article 44, as amended.

The charge is invoiced pro-rata to dispatching users based on energy withdrawn, to cover the expected accrued monthly cost and any prior differences.

[14] The uplift includes the virtual interconnection, amounting to approximately €292 million in 2018 (compared with approximately €256 million in 2017).

[15] These abbreviations, which refer to the Italian terms, have the following meanings:

CCT - Fees for Assignment of Rights of Use of Transmission Capacity

CCC - Contract Covering the Risk of Volatility of the Fee for Assignment of Rights of Use of Transmission Capacity (between zones)

CCP - Contract Covering the Risk of Volatility of the Fee for Assignment of Rights of Use of Transmission Capacity (between industrial centres)

DCT - Contract Covering the Fee for Assignment of Rights of Use of Transmission Capacity on Foreign Interconnections

Operating results of Regulated Activities in Italy

The following table shows a breakdown of the results from the Terna Group's Regulated Activities in 2018 and 2017[16].

(€m)

	2018	2017	Δ
Total regulated revenue in Italy	**1,989.6**	**1,967.2**	**22.4**
Tariff revenue	1,932.2	1,915.5	16.7
- Transmission revenue	*1,789.1*	*1,803.6*	*(14.5)*
- Dispatching, metering and other revenue	*143.1*	*111.9*	*31.2*
Other Regulated revenue	31.9	30.6	1.3
Revenue from construction services performed under concession in Italy	25.5	21.1	4.4
Total cost of Regulated Activities in Italy	**403.1**	**425.5**	**(22.4)**
Personnel expenses	203.4	217.8	(14.4)
External resources	155.5	154.7	0.8
Other	18.7	31.9	(13.2)
Cost of construction services performed under concession in Italy	25.5	21.1	4.4
EBITDA from Regulated Activities in Italy	**1,586.5**	**1,541.7**	**44.8**

EBITDA from Regulated Activities in Italy amounts to €1,586.5 million, an increase of €44.8 million compared with the figure for the previous year. This primarily reflects an increase in tariff revenue relating to dispatching, a reduction in personnel costs resulting from the generational changeover in progress and other charges.

Regulated revenue in Italy is up €22.4 million, reflecting the following:

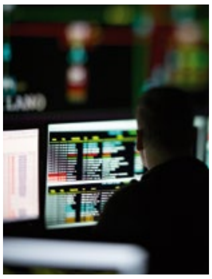
- an increase in **dispatching, metering and other revenue** (up €31.2 million), above all due to the recognition of certain expenses[17] not covered by the dispatching charge;
- a decrease in transmission revenue (down €14.5 million), following a revision of the related tariff to reflect completion, in 2017, of revenue from work in progress and a reduction in the volume of energy transported, offset by an increase in the portion of the NTG owned by Terna. The balance also includes the estimated impact of the revised contribution from international interconnections;
- an increase in **other revenue** (up €1.3 million): above all this reflects higher insurance proceeds (up €5.4 million) after taking into account lower connection service revenue (down €4.2 million).

[16] The Terna Group's operating segments are consistent with the internal control system adopted by the Parent Company, in line with the Strategic Plan for the period 2018-2022.

[17] The regulator, ARERA has decided to allow the recovery of expenses through the uplift mechanism provided for in art.44 of Resolution 111/2006. These expenses regard receivables that are no longer recoverable and relating to the period 2006-2015 (ref. Resolution 218/2018) and increased payments made to fund the regulator for the years 2013-2017.







The **cost of Regulated Activities in Italy** is down €22.4 million, primarily due to a reduction in **personnel expenses** (down €14.4 million), reflecting the higher amount of provisions made in 2017 for early retirement schemes, after taking into account the increase in the average workforce relating to the launch of new initiatives envisaged in the 2018-2022 Strategic Plan, which is mainly focused on investment in the Regulated sector.

Other expenses are down €13.2 million, mainly due to the lower cost of the quality of service (down €5.4 million) and to the favourable outcome of certain disputes that arose in the previous year.

€22.4m

the increase
in revenue from
Regulated Activities

Non-regulated Activities

Using our distinctive competences, we develop value added services as an Energy Solutions Provider for businesses. Our Non-regulated Activities in Italy are designed to support the energy transition, in keeping with our core business.

The main areas in which these activities are developed are:

- **CONNECTIVITY**
- **ENERGY SOLUTIONS**
- **PRIVATE INTERCONNECTORS PURSUANT TO LAW 99/2009**
- **TRANSFORMERS - TAMINI GROUP**

Extraordinary transactions

On 15 February 2018, the acquisition of 70% of **Avvenia The Energy Innovator S.r.l.** was completed, as part of the project to identify and implement new business opportunities for energy efficiency services and initiatives. **Avvenia**, a strategic consulting company classified as an Energy Service Company (Eco) and certified UNI CEI 11352, is a leader in the energy efficiency sector, with one of the highest numbers of efficiency projects completed and operated in Italy, including in the form of EPC (Energy Performance Contract) solutions.

As part of a project to reorganise the Terna Group's non-regulated business, **Terna Energy Solutions S.r.l. (T.E.S.)** was established via the partial demerger of Terna Plus S.r.l. (Terna Plus) which is wholly owned by Terna S.p.A.. The demerger, which was approved by the General Meeting of Terna Plus on 22 May 2018, was completed on 2 August 2018.
As a result of the demerger, T.E.S. was assigned the business unit that is organised and operated to carry out non-regulated business and energy solutions activities in various geographical areas in Italy, or in areas other than South America.


HAEFELY
HAEFELY

CONNECTIVITY

FIBRE

Project description >	The **project for Open Fiber** involves Terna's concession of an IRU (Indefeasible Right of Use) and the provision of ancillary services. The backbones connecting the 13 planned national POPs have been delivered, whilst the 41 regional rings that will connect the regional POPs (Clusters A and B) have been partially delivered. The most significant portion of the fibre optic regional ring requirements have been met by using Terna's overhead power lines, which were also set up during the year, and through the selected acquisition of fibre optic sections from third parties (swap transactions with Retelit and Fastweb).
Benefit for the customer >	The customer will acquire new infrastructure, which performs better than standard underground cables in terms of both reliability (much lower no. of faults per km per year) and quality (low attenuation), with significant savings in terms of length compared with terrestrial connections (> 20% over long distances).
Benefit for the Group >	Extraction of value from Terna's fibre assets via the concession of IRU and the provision of ancillary services.

Project description >	**Fibre IRU project for Fastweb**: dark fibre infrastructure was designed and made available to Fastweb along 760 km of Terna's overhead lines.
Benefit for the customer >	Acquisition of newly built infrastructure which performs better than standard underground cables in terms of both reliability (much lower no. of faults per km per year) and quality (low attenuation), with significant savings in terms of length compared with terrestrial connections (> 20% over long distances).
Benefit for the Group >	Extraction of value from Terna's fibre assets via the concession of IRU and the provision of ancillary services, namely Housing and Maintenance.

Project description >	**Fibre IRU project for RETELIT:** dark fibre infrastructure was designed and made available to Retelit along 1,150 km of Terna's overhead lines.
Benefit for the customer >	The customer will acquire a new infrastructure, which performs better than standard underground cables in terms of both reliability (much lower no. of faults per km per year) and quality (low attenuation), with significant savings in terms of length compared with terrestrial connections (> 20% over long distances).
Benefit for the Group >	Extraction of value from Terna's fibre assets via the concession of IRU and the provision of ancillary services, namely Housing and Maintenance.

CONNECTIVITY - *continued*

SMART TOWERS

< Project description

Smart Tower innovation project: The Smart Tower project aims to extract value from the NTG by expanding its use from an infrastructure exclusively designed for transmitting HV power to an Integrated Monitoring and Environmental Protection System.
The aim of the project is to offer value-added applications and services, exploiting the potential of the IoT (Internet of Things) in various areas of interest, with particular reference to: "environmental protection services", "NTG services" and "connectivity infrastructure".
Implementation of the experimental project to extract value from high voltage pylons by using them for environmental monitoring (smart towers) was completed with installation of the first seven smart tower pylons in Sicily and the acquisition of computer systems that were set up at two substations. Another smart tower has been set up in the province of Belluno to meet the needs of the electricity system, while completion of the four remaining installations in Sicily including the activation of computer systems, as well as the installation of a smart tower in Abruzzo to meet the needs of the electricity system, are expected at the beginning of 2019.

< Benefit for the customer

Start-up scouting activities in progress, with potential customers in the involvement phase (including the public sector).

< Benefit for the Group

Extracting value from the NTG by expanding its uses, moving from being infrastructure aimed exclusively at the transmission of HV power to being an Integrated Monitoring and Environmental Protection System. Assessment of potential benefits for TO and SO requirements.

5G PYLONS

< Project description

Extracting value from pylons by installing antennae in 2018. As part of its Non-regulated business, Terna is developing a commercial strategy aimed at extracting value from its assets, if available, for the provision of services to telecommunications operators. As Terna is not a telecommunications operator, the Company offers its services on the market in a neutral way, merely providing passive infrastructure (rental of space on pylons or in substations, dark fibre).
In particular, negotiations were concluded regarding the installation of antennae on Terna's pylons to cover remote areas (a contract with Open Fiber for FASTWEB 500 pylons in the three-year period 2019-2021). Negotiations with TIM and Fastweb regarding mobile radio solutions have also begun (trialling of 5G solutions). The related contracts are being finalised, in preparation for the conclusion of broader framework agreements.

< Benefit for the customer

By relying on Terna infrastructure (NTG pylons) and taking advantage of its nationwide reach, Open Fiber is able to build Fixed Wireless Access coverage in the rural areas that come within Clusters C and D of the Infratel tenders.

< Benefit for the Group

Extraction of value from the NTG by defining framework agreements regarding the provision of hosting services to support mobile network operators.

ENERGY SOLUTIONS

ENERGY EFFICIENCY

Project description > Design and construction of a **heat recovery plant belonging to Laterlite**, a leading company in the production of light, premixed and insulating expanded clay for the construction industry, in collaboration with Avvenia at the Rubbiano di Solignano plant (Parma).

Benefit for the customer > Optimisation of the qualitative and environmental performance of the production of light expanded clay aggregate (LECA), allowing up to 83% of heat to be reused in the production cycle, with a reduction in the consumption of natural gas and a corresponding reduction in atmospheric emissions of approximately 1,400 tonnes of CO_2 per year.

Benefit for the Group > A replicable, highly innovative project model that has generated an increase in technical and technological knowledge, as well as a contribution to Group revenue of approximately €0.5 million per annum over five years.

Project description > Construction of a **cogeneration plant** for ITS-SISA Detergenti S.r.l., in collaboration with Compendia S.r.l..

Benefit for the customer > Taking advantage of Terna's Energy Solutions know-how to create value for customers in terms of energy and environmental benefits, with savings in consumption and better sustainability performance.

Benefit for the Group > Increasing the Group's presence in the energy efficiency sector.

Project description > Construction by Avvenia and Acciai Speciali Terni of a **heat generator for thermal recovery of fumes** from the walking beam furnace.

Benefit for the customer > Heat recovery to produce superheated steam and preheat demineralised water sent to plant utilities, via a heat recovery steam generator.

Benefit for the Group > Increasing the Group's presence in the energy efficiency sector.

Project description > Design and construction of a **trigeneration system fuelled by natural gas** with a total capacity of approximately 1,560 kWe at the plant belonging to Tratos HV (October 2018).

Benefit for the customer > Taking advantage of Terna's Energy Solutions know-how regarding the transformation of the electricity market towards the use of environmentally-friendly sources of energy.

Benefit for the Group > Increasing the Group's presence in the energy efficiency sector.

Project description > Activation of **an energy assessment drone** promoted and managed within the Innovation Plan.

Benefit for the customer > Carrying out complete assessments in a short space of time to identify complex energy efficiency interventions. The drone will also be able to inspect areas or portions of the plant that are difficult to reach or inspect (e.g. roofs for installation of refrigeration units and photovoltaic panels, piping, etc.).

Benefit for the Group > Saving time in carrying out energy audits, especially in the post-processing phase, by automating the process of reporting and identifying faults and possible related interventions. The opportunity to identify "hidden" interventions that are difficult to detect with normal inspection methods and consequently increase project pipelines. Finally, the possibility of using the diagnostic tool in synergy with other business areas (e.g. for photovoltaic systems and grid infrastructure).

PLANT MAINTENANCE FOR THIRD PARTIES

< Project description

Renegotiation (in October 2018) of **plant maintenance contracts** with RTR.

< Benefit for the customer

Taking advantage of Terna's positioning and know-how regarding O&M activities, ensuring that the services are provided by an authoritative and reliable stakeholder.

< Benefit for the Group

Confirmation of Terna's strong position among the leading O&M players regarding photovoltaic systems, thanks to the use of economic and technical drivers, important optimisation of outsourcing procedures, and the Company's substantial review of the model and contract specifications.

< Project description

Non-regulated Activities Control Centre: Implementation of a platform that gathers and processes data deriving from the assets managed by Terna in the Energy Solutions segment.

< Benefit for the customer

In addition to meeting contractual obligations, the system will enable optimisation of maintenance processes and performance.

< Benefit for the Group

Constant remote monitoring of the status of plants with diagnostics and synthetic KPIs. Possibility to carry out optimised planning of maintenance interventions and implement purpose-built algorithms for predictive maintenance of assets, including an advanced reporting system.

EPC- ENGINEERING, PROCUREMENT AND CONSTRUCTION

< Project description

Design and construction for the customer, Macchiareddu, of the HV/MV **substation and the connection line to the future substation and the National Transmission Grid of the "Cilea" and "Tosti"** photovoltaic plants located in the municipality of Civita Castellana (VT).

< Benefit for the customer

Taking advantage of Terna's positioning and know-how for the construction of the HV/MV substation and the connection line to the future substation and the National Transmission Grid.

< Benefit for the Group

Development of advanced services for renewables.

< Project description

Energisation of an HV/MV substation for connection to the National Transmission Grid of a 27 MW wind power plant for the customer, **AM Energie Rinnovabili**.

< Benefit for the customer

Taking advantage of Terna's positioning and know-how regarding integration of renewables.

< Benefit for the Group

Development of advanced services for renewables.

< Project description

Energisation of an HV/MV substation for connection to the National Transmission Grid of a 42 MW wind farm for the customer, **Eolica Cancellara S.r.l.**.

< Benefit for the customer

Taking advantage of Terna's positioning and know-how regarding integration of renewables.

< Benefit for the Group

Development of advanced services for renewables.

ENERGY SOLUTIONS - *continued*

EPC- ENGINEERING, PROCUREMENT AND CONSTRUCTION (continued)

Project description >

Framework agreement with RFI (December 2018) regarding the "Design, supply, installation, certification and entry into service of metering devices".

Benefit for the customer >

Taking advantage of Terna's positioning and know-how regarding the installation of metering equipment in order to ensure that withdrawals by the FS Group's energy service system are accurately measured (timely certification of consumption) in accordance with current legislation.

Benefit for the Group >

Using the Group's distinctive expertise for the benefit of a strategic partner.

SMART ISLAND

Project description >

The **Giannutri Project Smart Island** built and tested during 2018 is the first real project in Italy that aims to bring about the energy transition from a diesel production system to completely renewable power generation.
The project received awards for "Sustainable Development 2018" and as "Good Practice of the Year 2018 - Environmental Protection".
After the signing of an agreement in 2016 with the **Municipality of Pantelleria** between S.Med.E. Pantelleria (the company that produces and distributes electricity on the island) and Terna Plus, in 2018 preliminary design activities continued regarding the development of renewable power generation on the island and the drawing up of "smart" initiatives to integrate it within the grid.

The activities specifically regarded a photovoltaic plant in an industrial area of approximately 4 MW, including its accumulation system, and an Energy Management System to manage the island's energy resources.
An innovative citizen engagement model was also defined regarding the development of widespread photovoltaic systems on buildings in Pantelleria town.
In accordance with the guidelines set out in the memorandum of understanding signed in 2015 by Terna Plus with the **Municipality of the Island of Giglio**, the Tuscan Archipelago National Park Authority and SIE, the concessionaire for the production and distribution of electricity on the island, all the necessary preparatory activities for the development of renewable power generation were carried out, in accordance with the Ministerial Decree of 14 February 2017, "Meeting the requirements of small islands not interconnected via renewable sources of energy".
Activities were then started to acquire available land for the construction of a 500 kWp plant and a related 2 MW / 1 MWh storage system in Allume. Work is also continuing on the development of an innovative photovoltaic plant at the island's landfill site, which is necessary to achieve the challenging objectives set by the Ministerial Decree of 14 February 2017.
Overall, these initiatives, as well as minimising the impact of traditional power generation on the local population, will enable the island of Giglio to reap all the benefits arising from a transition towards more sustainable forms of energy, while at the same time improving the quality of the electricity service.

Benefit for the customer >

Implementation of sustainable infrastructure projects with very low environmental impact in the interests of the energy transition of small, non-interconnected islands.

Benefit for the Group >

Increased know-how regarding the implementation and operation of hybrid off-grid systems, management of energy flows and development and testing of innovative grid services. Mitigation of technological risks relating to key technologies in the Energy Solutions sector with regard to future projects, and enabling them to have a better technical and economic fit.

In particular, the Giannutri project strengthens Terna's credibility in the field of Energy Solutions vis-à-vis its key stakeholders.

PRIVATE INTERCONNECTORS PURSUANT TO LAW 99/2009

In order to support the development of a single electricity market by expanding the infrastructure needed for interconnections with other countries, EU legislation was introduced, setting out guidelines for the creation of interconnections with other countries by entities other than grid operators.
The European guidelines have been introduced into Italian legislation by **Law 99/2009**, which assigned Terna responsibility for selecting undertakings (the "selected undertakings"), on the basis of public tenders, willing to finance specific interconnectors in exchange for the benefits resulting from a decree granting a third-party access exemption with regard to the transmission capacity provided by the new infrastructure. In particular, the law states that these entities, in exchange for a commitment to finance such projects, are required to commission Terna to build and operate the interconnectors.
A total of five interconnectors are planned for the borders with France, Montenegro (both at an advanced stage of completion), Austria, Switzerland and Slovenia (currently awaiting the necessary consents).

5
cross-border interconnectors built by private investors

Italy-France Interconnector Project

The new "Italy-France" direct current interconnector increases cross-border interconnection capacity by 1200 MW from approximately 3 GW currently to more than 4 GW.
The Group has continued with construction of the private line, in implementation of Law 99/09, on behalf of the company, Piemonte Savoia S.r.l., transferred to the private finance providers on 4 July 2017. On the section not appertaining to Sitaf (*Società Italiana per il traforo autostradale del Frejus*), the civil works and the laying of cable for the entire section were completed at the end of August 2018.
By December 2018, approximately 24.5 km of civil works along the A32 motorway had been completed and 12.8 km of cable laid. In addition, as regards the Middle section, by December 2018, approximately 14 km of cable had been laid and around 21 km of civil works had been completed.
The production of transformers and the converter for the Piossasco Converter, as well as erection of the main buildings, have been completed.

Italy-Montenegro Interconnector Project

The project involves construction of a 500 kV direct current connection, part in submarine cable and part in terrestrial cable, between the substations of Villanova (IT) and Lastva (ME) and covering a distance of approximately 445 km. Entry into service of the first module of the interconnection will result in interconnection capacity of 600 MW by the end of 2019. Of the 600 MW associated with the first module, a portion will be available under exemption to private lenders.

To date, the laying and protection of the first pole of the submarine cable between Italy (Pescara) and Montenegro (Kotor) has been completed, as has the laying of the terrestrial cables. The converters in both Italy and Montenegro are at an advanced stage of completion. On 29 March 2018, the Ministry for Economic Development and the Ministry of the Environment and of the Protection of Land and Sea issued the decree partially transferring the consents from Monita Interconnector S.r.l. to Terna S.p.A., in line with the new scope of the private interconnector. On 19 April 2018, Monita Interconnector S.r.l. submitted a revised application for exemption to the Ministry for Economic Development. On 14 June 2018, ARERA issued clearance for the exemption. Terna is currently awaiting clearance for the exemption from the Ministry for Economic Development.





PRIVATE INTERCONNECTORS PURSUANT TO LAW 99/2009 - *continued*

Italy-Austria Interconnector Project

The Italy-Austria interconnector (the Reschenpass project), which is currently awaiting the necessary consents, involves construction of a new 220-kV AC interconnection between the Glorenza (Italy) and Nauders (Austria) substations. This will consist of 26 km of underground cable and the necessary upgrade of the domestic grid.
The project will increase cross-border interconnection capacity between Italy and Austria by around 300 MW, which will almost double the currently available capacity.

The related consents process on the Italian side is expected to be completed by the end of the first quarter of 2019.On 16 July 2018, the Terna Group set up the special purpose vehicle, Resia Interconnector S.r.l., which, on behalf of the energy-intensive companies selected in accordance with Law 99/09, is to prepare and submit a request for exemption from the right of third parties to access the transport capacity the infrastructure will make available.

Italy-Switzerland Interconnector Project

The project involves the development of new transmission lines between Italy and Switzerland, in part in alternating current and in part in direct current. It will increase interconnection capacity between Italy and Switzerland, raising it by approximately 1 GW.

Italy-Slovenia Interconnector Project

The creation of a direct current line is planned, partly in undersea cable, between the substations of Salgareda (IT) and Bericevo (SL), together with work on upgrading the domestic grids in Italy and in Slovenia. The project is currently awaiting the necessary consents on the Italian side. The expected increase in cross-border capacity of approximately 1 GW will raise the interconnection capacity to more than double the current level.

TRANSFORMERS - TAMINI GROUP

Tamini operates in the electromechanical sector and is a leader in the design, production, commercialisation and repair of power transformers for electricity transmission and distribution grids, of industrial transformers for the steel and metals industry and of special transformers for convertors used in electrochemical production.

With a hundred years of experience, Tamini has a well-established name in Italy and overseas, thanks to its technological and engineering capabilities, combined with the degree of customisation and production flexibility it can offer.

Tamini has six production plants in northern Italy - in Melegnano, Legnano, Ospitaletto, Valdagno, Novara and Rodengo - and two trading companies in the United States and India. The Rodengo plant specialises in services, whilst the Novara production plant continues to manufacture coils, operating as a service centre for all the production sites that manufacture for both the Power and Industrial sectors.

+9%
ORDERS FOR TRANSFORMERS

THE TAMINI GROUP IN 2018

Order book

Tamini received orders for transformers worth approximately €120 million in 2018, a 9% increase on 2017 and in line with expectations.
Service orders amounted to approximately €11 million in 2018, in line with expectations.
Factory order books are up approximately 14% compared with the end of 2017.

2018 results

In 2018, the volume and value of new transformers designed, built and tested rose by around 21%, in line with expectations.
Thanks to the increase in volumes, the gross margin registered a positive figure, and grew strongly compared to 2017.

Vegetable oil transformer

Two 250 MVA transformers using vegetable oil built at the Legnano plant were installed during the year. Tamini also won a contract to produce a 400 MVA vegetable oil transformer.

Operating results of Non-regulated Activities

A breakdown of the Terna Group's results from its Non-regulated Activities for 2018 and 2017 is shown below[18].

(€m)

	2018	2017	Δ
Revenue from Non-regulated Activities	**194.9**	**189.1**	**5.8**
Tamini	103.4	92.6	10.8
Telecommunications	41.7	43.0	(1.3)
Energy Solutions	38.5	29.5	9.0
- EPC	*14.9*	*10.4*	*4.5*
- Energy efficiency	*7.2*	*0.1*	*7.1*
- O&M	*16.4*	*19.0*	*(2.6)*
Italy-France interconnector	9.0	16.0	(7.0)
Other	2.3	8.0	(5.7)
Cost of Non-regulated Activities	**134.4**	**126.7**	**7.7**
EBITDA from Non-regulated Activities	**60.5**	**62.4**	**(1.9)**

EBITDA from Non-regulated Activities amounts to €60.5 million in 2018, registering a slight decrease of €1.9 million, primarily due to accumulated revenue from the private Italy-France interconnector registered in 2017, offset by the higher contribution from the Tamini Group.

€5.8m

the increase in Non-regulated Activities

Revenue from Non-regulated Activities is up €5.8 million, primarily due to the following factors:

- an increase in revenue at the **Tamini Group** (up €10.8 million), primarily due to increased sales of transformers during the year;
- higher revenue in the **Energy Solutions** segment (up €9 million), mainly due to the contribution of energy efficiency activities (up €7.1 million due to the contribution from Avvenia), and new orders (up €4.5 million), offset by a reduction in O&M revenue (down €2.6 million), especially in the photovoltaic sector following the renegotiation of contracts with an operator;
- a reduction in revenue relating to the **private Italy-France interconnector** (down €7 million), due to the higher revenues recognised in 2017, and also to the recovery of the portion of the payment due in relation to the period prior to obtaining the exemption;
- the adjustment in 2017 of the exposure to contractual obligations following the sale of a **photovoltaic project** (down €6.2 million);

The cost of Non-regulated Activities is up €7.7 million, reflecting the above increase in contract work at the Tamini Group (amounting to €103.8 million in 2018, up €4.8 on the previous year), and the contribution of Avvenia (up €4.4 million, mainly due to costs associated with a new energy efficiency contract acquired in 2018), offset by the lower cost of external resources relating to the subsidiaries, Terna Plus S.r.l. and Terna Energy Solutions S.r.l., resulting from a reduction in contract work in progress (down €1.1 million).

[18] The Terna Group's operating segments are consistent with the internal control system adopted by the Parent Company, in line with the Strategic Plan for the period 2019-2023.

International Activities

International markets offer opportunities to leverage the expertise developed in Italy as a TSO, including in the integration of renewables and the development of power lines. We are aware that the radical transformation the world is experiencing is a shared responsibility.

Overseas investment focuses on countries with stable political and regulatory regimes and a need to develop their electricity infrastructure, with a view to diversification with respect to its Italian businesses. This is done partly in collaboration with other energy companies with a consolidated presence in foreign markets.

International markets offer opportunities in terms of the development of transmission plant, driven by growing demand for electricity and the opening up of markets to foreign operators.

Terna's strategic priorities with regard to its overseas operations include:

- **Europe:** to strengthen its presence (assessing and monitoring M&A opportunities and developing merchant interconnector projects);
- **Latin America:** to complete ongoing projects in Brazil, Uruguay and Peru and consolidate its position in the countries of interest, by leveraging the new restructuring;
- **Other geographical areas:** to develop advanced services in order to leverage Terna's technical expertise acquired in Italy. These initiatives are low risk and absorb a limited amount of capital.

Overseas **initiatives** of interest to the Terna Group are:

Concessions: this model envisages the acquisition and operation of transmission systems abroad by taking part in international concession and/or secondary market awards, leveraging the core competencies and experience developed in the international arena;

Technical assistance: this involves the provision of consulting and technical assistance services regarding a TSO's core activities, as well as the definition and implementation of regulatory and market frameworks in the local energy context, with a view to exporting and taking advantage of the distinctive expertise acquired in Italy;

Energy Solutions: this includes all high value-added non-traditional activities aimed at exporting the experience Terna has in Italy in the fields of energy storage and smart solutions;

EPC Management: Engineering, Procurement, Construction Management (EPCM) activities enable leveraging of infrastructure management expertise and implementation of projects overseas.

INITIATIVES IN PROGRESS IN SOUTH AMERICA

Chile

The project was completed with the delivery of the additional works in February 2018, in line with expectations.

Uruguay

During 2018, work continued on the construction of the 213 km Melo-Tacuarembò 500kV transmission line.
The engineering activities were completed and load testing of all types of pylons was successfully completed. The process of receiving and obtaining customs clearance for materials, with a special focus on pylon structures, is still in progress.
As regards construction, civil works are underway on the Melo-Tacuarembó line. At the end of the year more than 60% of the foundations had been completed, and assembly of the pylons began during the second half of the year.
Over 50% of the works have been carried out, with completion expected by the end of 2019.
In October 2018, the status of *Projecto de Inversion* (Investment Project) was obtained, in order to qualify for the related tax benefits.

Brazil

Construction of the lines and substations for the two concessions, Santa Maria Transmissora de Energia (SMTE) in the State of Rio Grande do Sul and Santa Lucia Transmissora de Energia (SLTE) in the State of Mato Grosso, continued in 2018.

Regarding the SMTE concession, construction of the lines and substations has been completed and energisation tests have been successfully carried out.

On 3 October 2018, the concessions' entry into commercial service was formally authorised by ONS (Operador Nacional Do Sistema Eletrico - the Brazilian regulator), and operation and maintenance activities regarding the concessions are in progress.

77% of the line was built using single-pole cable-stayed pylons with a low environmental impact.

Regarding the SMTE concession, 99% of the works have been carried out, with completion expected during the first half of 2019. 75% of the line was built using single-pole cable-stayed pylons with a low environmental impact.

Final checks and the process of obtaining the necessary consents for the project to enter into commercial operation are in progress. The operation and maintenance contract has also been signed.

Peru

Work began in 2017 on construction of 132 km of new 138kV lines between Aguaytìa and Pucallpa
The structural engineering works begun at the end of 2017 were completed in 2018 and the environmental certification process has been launched. This is expected to be completed by the end of the first quarter of 2019.
As far as permits and consents are concerned, the final socio-environmental public hearing with the local population was successfully held, and the documentation relating to the environmental impact study for the authority responsible for issuing the environmental certification (Senace) was completed.
In terms of the acquisition of easements, all the land forming part of the line's buffer zone has been surveyed and recorded, and the process of acquiring easements and land along the route has begun.
Procurement of transmission line materials has also begun.
The project is expected to be completed by the end of 2020.

Operating results of International Activities

A breakdown of the Terna Group's results from International Activities for 2018 and 2017 is shown below[19].

It should be noted that "Revenue from International Activities" directly includes the margin earned on overseas concessions.

(€m)

	2018	2017	Δ
Revenue from International Activities	12.5	6.5	6.0
Cost of International Activities	8.9	6.7	2.2
EBITDA from International Activities	**3.6**	**(0.2)**	**3.8**

EBITDA from International Activities amounts to €3.6 million for 2018, up €3.8 on the previous year, primarily reflecting:

- the effects of activities carried out in **Brazil** (up €12.4 million), offset by the loss recognised on the contract regarding construction of the line in **Uruguay** (down €5.4 million)
- a €2.2 million increase in the **cost of International Activities**, due to higher charges relating to contract work in progress and overseas initiatives.

[19] The Terna Group's operating segments are consistent with the internal control system adopted by the Parent Company, in line with the Strategic Plan for the period 2019-2023.

Focus on Brazil

SANTA MARIA - SANTO ÂNGELO 230KV POWER LINE

160 km of line built
>500 km of cable laid

> 300 pylons mounted
> 300 foundations built

~1,800 tonnes of structure
2 rivers crossed

2 substations built/operated

~500 personnel employed on construction

- 80% of the line was built using single-pole cable-stayed pylons with a low environmental impact.
- Priority lines for the state of Rio Grande do Sul enable integration of energy generated by wind power plants located in southern Brazil into the grid.
- A specific social and productive responsibility and inclusion programme involving 20 indigenous rural households from the Guarani ethnic group has been promoted.

The 230kV line entered service on 3 October 2018, two months ahead of the date agreed with ANEEL.

BRAZIL: CUIABÀ - JAURÙ C2 500KV POWER LINE

355 km of line built
>3,000 km of cable laid

> 700 pylons mounted
> 700 foundations built

~6,000 tonnes of structure
2 rivers crossed

2 substations built/operated

~1,400 personnel employed on construction

- 75% of the line was built using single-pole cable-stayed pylons with a low environmental impact.
- Priority line for the transmission system of the state of Mato Grosso, which serves dispatching of the electricity produced by the large hydroelectric plants in the states of Acre and Rondônia.
- Implementation of the project with respect for the local area (birdlife - tuiuiù specimens identified, natural sites such as the Saranhão cave and the Milton archaeological site).

The 500kV line is expected to enter service during the first half of 2019.

Our people

People are Terna's most important asset, and one of the enabling factors in the Strategic Plan. Each of us brings skills and experience that can help to increase the value of the Company. Trust, passion and responsibility are our values.

No change may take place unless it is understood, promoted and put into practice by people. Our skills and experience help to increase the value of the Company along its growth and development path.

Terna's values system

TRUST

PASSION

RESPONSIBILITY

People at the heart of our business

Investment in training and development, to ensure personal and professional growth

Ongoing initiatives to create a safety and accident prevention culture

Listening to employees by using ways to gauge their opinions

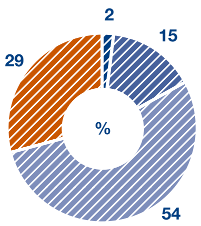
Internal communication aimed at creating a corporate culture in terms of both values and operations

A complex system of **industrial relations based on engagement with the trade unions**

Creation of management and development systems designed to **improve performance and develop individual skills**

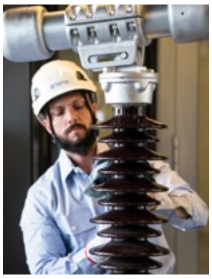
Remuneration and welfare policies that aim to align individual performance with business objectives and generate overall satisfaction and well-being for people.

% COMPOSITION OF THE WORKFORCE



WORKFORCE	AT 31 DECEMBER 2018	AT 31 DECEMBER 2017	CHANGE
Senior managers	**67**	71	(4)
Middle managers	**638**	569	69
Office staff	**2,290**	2,021	269
Blue-collar workers	**1,257**	1,236	21
TOTAL	**4,252**	**3,897**	**355**




The increase in the Terna Group's workforce at 31 December 2018 reflects 468 new hires and 113 people leaving the Group. In addition to the plan for generational turnover launched in 2017, the increase reflects the acquisition of Avvenia S.r.l. and the start-up of new initiatives in accordance with the Strategic Plan, primarily focused on the Investment Plan, development of non-regulated business in Italy and overseas and strengthening of the Group's distinctive expertise.

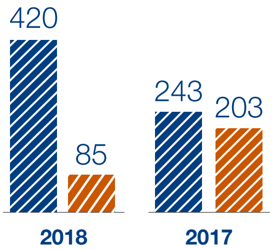
468
new recruits

At 31 December 2018, the number of agency workers employed by the Terna Group totalled 15 (54 in 2017).

The turnover rate[20] of 2.42% was down compared with 2017, as special attention was paid to strengthening distinctive expertise in 2018.

The incidence of voluntary resignations is very low (0.97%).

WORKFORCE TRENDS



■ Employees recruited during the year
■ Employees leaving during the year

COMPOSITION OF THE WORKFORCE	2018	2017	Δ
Permanent employees	**100%**	100%	-
Average age (in years)	**42**	42	-
University and high-school graduates	**94.3%**	93.5%	+0.8%
Women as a % of the total	**13.5%**	12.3%	+1.2%
Women in senior and middle management roles out of total senior and middle managers	**19.7%**	17.5%	+2.2%

The average age of the workforce stood at 42, in line with 2017. University and high-school graduates make up 94.3% of the total workforce, up 0.8% compared with 2017.

42
average age

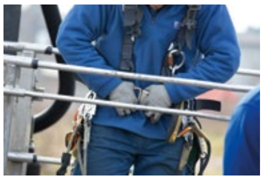
In terms of gender, there has been a **significant increase in women employed (up 1.2%)**, although the majority of the Group's workforce consists of men (accounting for 86.5% in 2018). **The presence of women in the workforce has grown steadily over the years**, rising from 9% in 2005 to 13.5% in 2018. In addition, in 2018, 27% of new recruits, excluding operating personnel, were women, in line with the figures for 2017.

In terms of type of contract, all employees are on permanent contracts.

100%
permanent contracts

[20] The following comments refer to employees of the Terna Group, excluding employees of the Tamini Group (355 HC), Avvenia (16 HC) and Terna Crna Gora d.o.o. (9 HC), as well as the other overseas companies (local staff in Brazil, Uruguay and Peru, respectively 17 HC, 7 HC and 5 HC).




TERNA'S APPROACH

Occupational safety

Safety and accident prevention to guarantee the physical integrity of employees are among the Company's main priorities, The figures for 2018 report no fatal workplace accidents among Group employees.

During September 2018, Terna finalised the analyses required to build a strengthened and more deep-rooted safety culture. This will result in **the launch of the "Zero Accidents" project**, a structured and integrated process which, via a series of wide-ranging initiatives, aims to promote a global approach to safety involving all the Company's staff, as well as people working at Terna's plants in various capacities. Through the definition of improvement and prevention plans, including awareness raising and training initiatives, the two-year project aims to ensure that safety becomes nothing less than a way of life.

The objective is to obtain a significant reduction in accident indicators over the years, in order to achieve and then maintain the target of zero accidents.

In 2018, as in previous years, no fatal workplace accidents were registered among Group employees. A total number of 40 accidents was registered, none of which had an initial prognosis of more than 40 days of estimated recovery time, while 11 accidents had a subsequent ongoing prognosis of more than 40 days, which therefore had not been deemed serious[21] on initial prognosis. Six accidents were also registered with an initial prognosis of less than 3 days of estimated recovery time[22].

OCCUPATION INJURIES SUFFERED BY TERNA EMPLOYEES - GRI-ILO DEFINITIONS	2018	2017
Injury rate	1.28	0.81
Lost day rate	34.40	27.62
Absentee rate	6,937.4	6,239.9
Number of injuries	40	24
- of which serious (initial prognosis > 40 days)	-	1
- of which serious (subsequent ongoing prognosis > 40 days)	11	-
- of which fatal	-	-

The injury rate and the lost day rate are slightly up compared with the previous two-year period. For further details on this matter, reference should be made to the "Sustainability Report".

[21] Since 2018, the criterion for classifying an injury as serious has become more detailed. A serious injury is now defined as resulting in a total absence from work of 40 (forty) days or more, excluding the day of the event, as an initial prognosis or as a subsequent ongoing prognosis accompanied by medical certificates. Previously, only injuries with an initial prognosis of 40 (forty) days or more were registered as being serious, excluding the day of the event.

[22] Since 12 October 2017 (art. 3, paragraph 3-bis of Law Decree 244/2016), companies have an obligation to report to INAIL any injuries resulting in an absence from work of at least one day, excluding the day of the relevant event. Previously, the obligation only applied to absences of over 3 days, excluding the day of the event. Absences of less than 3 days were only registered internally.

Training

Training is continuously provided at Terna throughout employees' working lives. The aim is to create value for people by increasing and diversifying their skills (employability), and to create value for the Company by developing human capital in line with its mission and business strategy. The Campus is where all the different kinds of training are provided. Its mission is to transfer the specialist know-how of the most experienced staff (faculty) and of external contributors (universities and business schools).

Employees received 55 hours of training per capita. This is in line with the figure for the period 2016-17 (an average of 55.5 over the two years), influenced by the strong commitment to supporting generational turnover and the resulting recruitment of large numbers of technical personnel.

The figure is extremely positive when set against the average for the 40 companies listed in the FTSE-MIB, which in 2016 (the latest figure available) was 25.8 hours per capita.

55 hours
of training per capita
(compared with an average of 25.8 for FTSE-MIB companies)

Approximately **203,000 hours of training had been provided at 31 December 2018, primarily focused on professional and technical and operational skills** and ensuring compliance with HSE, GDPR and statutory 231 requirements, in addition to the integration of newly hired personnel, and the development of new professional skills and new technical roles such as multiskilled ones.

In addition to training initiatives aimed at managerial and personnel development, the Company implemented a training programme to develop and consolidate project management skills and PMP and SME certification for a selection of staff who operate in the international and engineering fields.

"Terna 4.0 Go Digital", a programme of initiatives, online tips and workshops aimed at strengthening digital aptitudes and an innovation-oriented mindset, was launched.

Development of human capital

In support of human resources development policies, **Terna uses the Professional System as a basic architecture to manage roles, skills and development paths within the organisation**, enhancing competencies and crafts ("professional families") identified on the basis of core business and corporate processes.

As part of human capital development initiatives, work on the design of a new Performance Management System was completed in the first half of 2018. The system is used to define and communicate objectives, outcomes and expected organisational behaviours, as well as to promote a culture of appraisal and feedback as a way for managers to develop and coach members of their teams.

An initial pilot project, "People for Performance", was launched in the second half of 2018. This involved approximately 600 people, with the aim of gradually extending the project to all the workforce from 2019.

Further details of remuneration and incentive schemes are provided in Terna S.p.A.'s annual Remuneration Report, which is published on the Company's website (www.terna.it).

TERNA'S APPROACH *(continued)*

Recruitment and selection

Staff recruited on the external labour market are university graduates - especially engineers - and graduates from technical colleges, most of whom have specialised in electrical engineering. Once hired, new recruits acquire the specific knowledge and skills they need via dedicated training courses. The preferred channel for collecting candidates' applications is the "Work with us" section of the Company's website.

In April 2018, with the aim of spreading greater cultural awareness among the younger generation and trying out original recruitment and selection methods, Terna organised an innovative recruitment day at the Teatro Eliseo Theatre in Rome, which provided **a growth and learning opportunity to 100 engineering and economics graduates**. As an outcome of this recruitment day, Terna was able to identify a pool of valuable resources and to hire **18 new staff**.

2018 also saw an increase in the recruitment of specialist and middle manager profiles, needed to acquire new expertise and professional skills.

Terna also manages relations with schools, universities and job centres in order to support the process of recruiting new staff and to sustain a virtuous circle of sharing between the Company and the outside world. In this connection, during 2018, the **second edition of *Trasmettere il Sapere***, Terna's work experience scheme, took place. The scheme involved 13 vocational training institutes from all over Italy and approximately 600 4th- and 5th-year students.

In the last quarter of 2018, **planning began for the third edition of the *Trasmettere il Sapere* project**, which will feature a more active format (project work, digital contests, tutoring) and will involve 15 vocational training institutes and approximately 750 4th- and 5th-year students.

Thirteen recruiting events **were also held at high schools** to present the Company and start the selection process with graduates. In 2018, Terna **entered into 17 sponsorships and partnerships with prestigious** universities (Stanford, Luiss, Polytechnic University of Milan, Polytechnic University of Turin, Rome's La Sapienza University, etc.) and accredited master's degree programmes, as well as signing more than 40 agreements. The Company also activated 29 apprenticeships and internships and took part in 17 career days.

In order to **attract, select and enhance** Terna's talented people, **two structured recruitment processes, called onboarding, have been designed**. The first is aimed at approximately 1,000 colleagues hired in the last 36 months (university and high school graduates), while the second is aimed at future new recruits.

Training for these colleagues began in November 2018 (the first 9 courses have been completed).

The onboarding course provides for job shadowing experiences, training for university and high school graduates in mixed classrooms, and counselling activities using the buddy system.

Company welfare

Following the signing of specific agreements with the labour unions in 2018, the **Terna Welfare initiative, which allows Group employees to allocate part of their performance bonus for the purchase of welfare goods and services and supplementary pension schemes, was launched**. The amount chosen is tax-free and increased by 12%, thanks to an additional supplement paid for by the Company. In defining the management service for the welfare plan, special attention was paid to the "Family" category. Indeed, employees allocated a significant portion of their bonuses to reimbursement of this type of expenditure, especially school expenses relating to tuition fees, study holidays, books and taxes.

In addition, in order to facilitate work-life balance, on 1 July 2018 a **smart working** trial was launched lasting throughout the second half of 2018, involving approximately 100 employees from organisational departments at offices in Rome. A specific labour union agreement - signed in June 2018 - regulated the initiative during the trial period. In view of the outcomes of the trial, smart working will be gradually extended in 2019, also involving employees based in other large cities.

The Group's new organisational structure

The Group's new organisational structure, in place from 1 July 2018, aims to support Terna's central role in the integrated electricity system, with the aim of:

Optimising and integrating real-time dispatching activities and long-term planning	Optimising the management of tangible assets and maximising operational excellence in their design, construction, operation and maintenance

With regard to the above purposes, the following two organisational units now report directly to the Chief Executive Officer:

- **"Strategy, Development and Dispatching"**, which includes system strategy, grid planning, dispatching, regulatory affairs and energy & research insights;
- **"National Transmission Grid"**, which includes asset management and plant design, construction, operation and maintenance, as well as procurement and ICT.

The new organisational structure also **strengthens the Group's innovation and digital capabilities** through the creation of a new department reporting directly to the Chief Executive Officer, called "Innovation, Digital and Energy Solutions".
Finally, **the "External Relations and Sustainability"** function has been revisited in view of the Group's growing role at international and European level in the development of energy strategies.

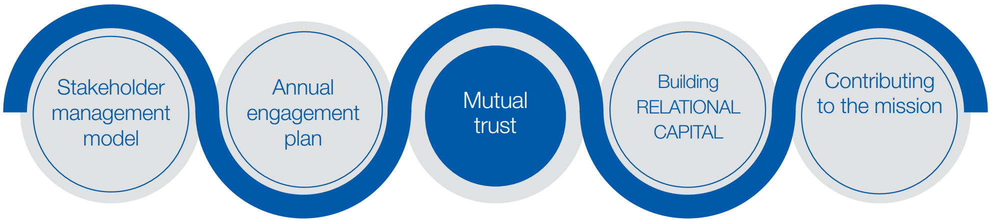
At a local level, moreover, the new Genoa Infrastructure Unit was opened on 9 April 2018. This innovative, environmentally sustainable building, which uses cutting-edge energy efficiency technology and has been built to the very highest environmental standards, is designed to meet the Company's requirements in terms of the quality of the working environment. The investment of around €2 million has involved:

- the modernisation and improvement of approximately 13,500 square metres of office space, services and other premises;
- construction of an 11-kW photovoltaic plant has also been built to power the building's internal and external LED lighting, thereby maximising energy savings;
- the installation of an underground retarding basin with capacity of 500 cubic metres, which releases rainwater at a constant, linear rate, limiting the risk of water courses overflowing, in accordance with the Municipality of Genoa's new Urban Plan.

Local stakeholders

Engagement with local communities is a key part of our Grid Development Plan. This allows us to create the conditions in which together we can build an increasingly sustainable national grid.

A favourable social environment, coinciding with the availability of sufficient relational capital, is essential to Terna's ability to carry out the investments envisaged in the Grid Development Plan within the established time-scale and to exploit available opportunities for its Non-regulated business, in Italy and overseas.



To build and maintain good stakeholder relations, Terna has developed a number of tools and procedures within its "Stakeholder Engagement Model" designed to engage with and monitor public opinion, with the aim of avoiding the risk of failing to identify any problems in good time.

A specific engagement programme is conducted each year to identify the actions to be taken in order to bring the Group's relations into line with best practices and to ensure that stakeholders are listened to on a regular basis.

17
'Terna Incontra' meetings held in 2018 in 8 regions

SUSTAINABILITY INITIATIVES

Stakeholder

Local communities: more engagement and consultation

Terna has, since 2002, adopted a voluntary approach designed to foster the prior involvement of local government (regional and local authorities, park authorities, etc.). Since 2015, this has been extended to include people from the communities directly affected by Terna's plans through public meetings called "**Terna incontra**". These events focus on listening to local concerns, sharing design ideas and on dialogue, with the aim of ensuring a secure, efficient and sustainable grid.

17 such meetings were held during the year in eight Italian regions: at Avigliana (TO) in Piedmont; at a Vellezzo Bellini (PV) in Lombardy; at Auronzo di Cadore (BL) in Veneto; at Piombino (LI), San Vincenzo (LI) and Suvereto (LI) in Tuscany; at Codrongianos (SS) and Santa Teresa di Gallura (OT - 2 meetings) in Sardinia; at Bisaccia (AV), Lacedonia (AV), Naples and Sorrento (NA) in Campania; at Alberona (FG), Deliceto (FG) and Troia (FG) in Puglia; and at Cortale (CZ) in Calabria.

The main effects of these initiatives have resulted in:

- **the memorandum signed with Veneto Regional Authority** designed to bring development and innovation to the area at no cost to local people (the most important commitment regards the plan to rationalise the grid between Venice and Padua).
- the plan to modernise **the grid in Naples** and improve the level of security;
- the **"Green Corridors"** project, the first large-scale plan in Italy and Europe to reduce the risks linked to tall trees growing close to power lines.

Environmental organisations: strengthening partnerships

Terna's commitment to the environment and biodiversity led, in 2009, to the conclusion of partnership agreements with critical stakeholders, such as leading environmental organisations, with the aim of arriving at shared solutions designed to boost the environmental sustainability of the National Transmission Grid (NTG). Growing concerns over the impact of climate change, and the accompanying focus on energy transition initiatives, has led to further cooperation between Terna and these organisations. In particular, in 2016, Terna renewed and expanded its partnerships with Legambiente, the WWF and Greenpeace.

Investors: a growing request for transparency regarding environmental, social and governance aspects

Approaches to climate change and the energy transition, within the context of this specific sector, have **widened calls from numerous institutional investors** for major companies to conduct an informed and full assessment of the business risks linked to ESG (environmental, social and governance) issues. Moreover, with the adoption, by European countries, of Directive 2014/95/EU on non-financial disclosures (in Italy with Legislative Decree 254/2016), large companies are now required to publish an annual non-financial statement. Of particular importance, in terms of transparency and reporting, are the recommendations from the Task Force on Climate-related Financial Disclosures (the so-called Bloomberg Task Force) regarding the publication of information on the implications of climate change for business strategies, in terms of risks and opportunities. This is considered of central importance, with regard to both the best possible allocation of investment and efforts to combat climate change. Terna has for some time now implemented these recommendations (an examination of the emerging risks has also been included this year in the section "Dispatching of electricity").

Terna and innovation

Innovation and digital transformation are essential in an increasingly complex energy sector. Decisions regarding future development focus on the technology trends most relevant to our business.

The current **energy transition** process requires a new systemic and organic approach to innovation, based around a strategic acceleration of a portfolio of effective Research, Development and Innovation initiatives in keeping with the Group's strategies.

Terna decided to further speed up innovation in 2018, adopting a centralised, coordinated vision in order to encourage and coordinate research and the development of ideas, with the aim of creating a synergistic innovation ecosystem within the Company, capable of **enabling the transition to a new TSO 2.0 model**. The transition requires a new, smarter approach to managing the electricity system, which should be increasingly intelligent and flexible both at the level of the grid, thanks to the use of Industry 4.0 enabling technologies, above all the Internet of Things or IoT (advanced sensors, big data, advanced analytics), and in terms of the market. This will require the extensive digitalisation of processes and assets. It will entail an unprecedented revolution that will rapidly result in the integration of distributed generation resources, storage and market demand for services, and the Europe-wide integration of national markets.

The steps taken in this regard include implementation of an **Open Innovation process** and the creation of a structured Innovation Plan. Today's form of innovation calls for an approach capable of opening up new possibilities for development and cooperation with the outside world and the creation of dynamic interactions, including close attention to start-ups, which offer Terna the chance to invest in technological initiatives capable of creating more value for the Company and for Italy's electricity and energy system.

The Innovation Plan organises the innovation flow in a consistent manner, from the birth of new ideas through to development of the projects emerging from the R&D process.

New initiatives, which may be driven by requirements within the Company or by the Open Innovation process, are classified within a coherent framework, based on the principal new technologies earmarked by Terna as being capable of influencing both current and future innovation:

1. **Internet of Things**: Industrial IoT, distributed sensors and wearables;
2. **Energy Tech**: technologies linked to the new Energy Resources (Storage, Demand Side Response, E-mobility) and Smart Grids;
3. **Advanced Materials**: nanotechnologies, biomimicry and smart dust.

Factories

The main strategic project streams relating to **Transmission Operator (TO)** and **System Operator (SO)** activities have been identified and the related innovation factories set up: the **TO Innovation Factory** and the **SO Innovation Factory**, each responsible for carrying out their assigned innovation projects.

The TO Innovation Factory includes projects relating to **Transmission Technologies** and is specifically linked to Asset Management, Engineering and Infrastructure Development processes, supporting technology scouting initiatives, the identification and implementation of technologies, innovative processes and solutions for use in operating the Transmission Grid, with the aim of making continuous improvements to it.

The SO Innovation Factory, on the other hand, covers two areas: the **Dispatching and Control Systems** process, which includes engineering, supervision, control, scheduling and monitoring of the national electricity system in order to ensure that the transmission service is fit for purpose and its security, cost-effectiveness, continuity, quality and efficiency in accordance with pre-determined, measurable standards; and **System Engineering**, which deals with the upgrade and management of the National Electricity System, the preparation of defence and restart plans, and activates the procedures involved in the start-up of plants for dispatching purposes. The latter is also responsible for the process of analysing and calculating the grid, for calibration and protection systems, for the assessment and statistical analysis of disruptions, functional requirements and systems innovation.

Specifically, R&D and Innovation activities regarding TO activities are guided by the Development Plan. In this regard, priorities are focused on HVDC issues, new cable laying technologies, the optimisation of overhead lines and asset management technologies.

The focus in relation to SO activities is on enabling the market participation of distributed generation resources and demand for electric power and storage, with the aim of encouraging the penetration and integration of non-programmable renewable sources within the National Electricity and Energy System. The priority innovation project streams in this sector, therefore, relate to the flexibility of the Electricity System (e.g. vehicle-to-grid projects, demand-side response, etc.) and the secure management of the Electricity System (e.g. R&D activities regarding the resilience of the Electricity System, pilot projects on improved observability of distributed resources, etc.).

Digital transformation is the main enabling tool for innovation

Digital transformation is the main enabling tool for innovation and, in general, the current energy transition, to be implemented via projects in the following areas: connectivity (e.g. IoT technologies for asset management and dynamic network management), synchronous data management (e.g. advanced forecasting technologies for data management and electricity market processes), asynchronous data management (e.g. big data technologies and machine learning for use in data analytics and the exploitation of historical data).

Innovation in the Company is supported and promoted via multiple tools:

- **Systems and processes to support the enhancement of assets and internal expertise:** this includes tools for enhancing intellectual capital and sharing corporate know-how, as well as portfolio management tools.
- **Open innovation:** this encourages openness towards new areas for development within and beyond the Company, through dynamic interactions with universities and research centres, partnerships with peers and large industrial players, as well as access to start-ups and small and medium enterprises.
- **Access to incentive and soft financing mechanisms:** this promotes access to incentives (e.g. tax relief for companies investing in research and development activities, and patent box provisions) and specific funding programmes for both international and national R&D projects.

OPERATIONS RISK MANAGEMENT

Information and Cyber Risk

For some time, Terna has had an Information Security Governance Model, which enables it to identify the most significant cyber risks. It is based on policies and procedures, combined with a coordinated Information Risk Management ("IRM") operating programme, led and coordinated by the Group's CISO (Chief Information Security Officer. During 2018, the framework for the security measures used to mitigate this risk was updated to Revision 5 of the NIST 800.53 standard, this ensuring alignment with best international practices.
A pilot project involving Cyber Risk Quantitative Analysis was also completed. This was used to survey the market prices quoted by insurance brokers for Cyber Risk
Assurance policies for certain forms of cyber risk.
In addition, Terna's Computer Emergency Readiness Team (CERT) was sued to implement a structured process for identifying and rapidly containing security breaches, minimising any data loss and working to restore the affected services.

OPEN INNOVATION IN THE DEVELOPMENT PLAN

Sector	Description
Peers energy sector and infrastructures	The signature of agreements and partnerships with energy businesses who are not competitors (TSOs, DSOs, utilities, etc.). Membership of and active participation in leading associations and international bodies involved in the electricity sector and innovation. *Examples: RTE, ENI, RFI, ENTSO-E, EASE*
Universities and research centres	Collaborations to promote and coordinate studies and research with national universities and research centres of excellence in areas of strategic interest, in order to contribute to the preparation of expert researchers in this field and to promote and encourage initiatives aimed at teaching and training in the energy sector. *Examples: RSE, Ensiel*
Large companies and industries	The signature of agreements and partnerships with suppliers or companies who may be competitors, regarding areas of common interest in the electricity sector or applications aimed at ensuring greater sustainability, cost-effectiveness and security in the management of grids.
Start-ups, SMEs and venture capital	The scouting of start-ups and mature enterprises in order to grasp opportunities for the development of specific initiatives of interest to Terna and/or business partnerships. *Examples: the Next Energy programme*

MAIN RESEARCH AND DEVELOPMENT INITIATIVES

Description	Projects and programmes
Terna and the Cariplo Foundation ran the **third edition (2018-2019)** of the initiative, using the same proven structure for the three calls: the "Call for Talent", "Call for Ideas" and "Call for Growth". The third edition of Next Energy relates to the theme "Interaction between electricity infrastructure and local areas", focusing on environmental sustainability, and includes: • **Call for Talent:** 10 internships lasting 6 months for talented young engineers, economists, mathematicians, physicists and statisticians; • **Call for Ideas:** the selection of 10 early-stage start-ups with a medium to low level of technology readiness (a TRL of 2-5). The chosen start-ups will have access to incubators selected by the Cariplo Factory and the winner will receive a €50,000 voucher to be exchanged for services; • **Call for Growth:** the selection of up to 5 mature start-ups with medium to high levels of technology readiness (a TRL of 5-8), chosen on the basis of specific requirements identified by Terna with the aim of developing pilot projects.	NEXT ENERGY programme and the start-up ecosystem
Terna has entered into partnership with the start-up accelerator, Digital Magics, an incubation program founded in 2004 specialising in digital start-ups which, in the energy sector, works in partnership with **Compendia**, an innovative energy services company. The first call, which was completed on 20 November, resulted in the selection of Wisense, a start-up based in the Marche region of Italy founded by three Ancona University students. The company is using Artificial Intelligence and Machine Learning technologies to develop a system capable of recording and analysing data on seismic wave propagation, for potential use in projects that Terna is developing as part of efforts to boost the resilience of the electricity system.	Monitower Call
In connection with its research and innovation activities, in 2017, Terna joined the research programme launched in October 2016 by the Precourt Institute of Energy at Stanford University (one of 30 research centres at this Californian university that specialises in engineering). The programme, called Bits & Watts as a reminder of the strong correlation between electricity grids and digital transformation, aims to identify solutions to facilitate and accelerate the current transition in the electricity sector, by combining university and industry expertise to develop innovative projects and solutions. The initiative's strategic value lies in its integrated approach to research focusing on three key areas, ranging from the coordinated management of electricity transmission and distribution grids, to the active integration of consumers within the electricity system and the use of data analysis in the development of new automated energy management tools. Following the memorandum of understanding signed with **Ensiel** (a consortium set up by the main Italian universities operating in the power systems sector), and the adoption of the innovative contractual format with the direct award of contracts for research and development services, in 2018, Terna launched 11 projects involving 9 Italian universities from among those most active in the electricity and energy systems sector.	Academy

Financial resources

Our management approach aims to maximise efficiency and achieve and maintain a solid financial structure, taking a highly prudent stance towards mitigation of the potential risks.

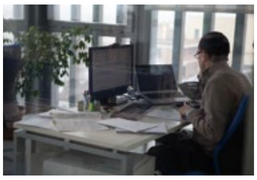
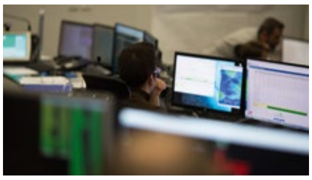
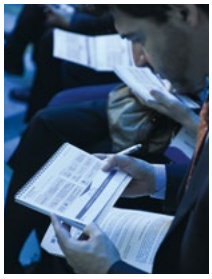
The key aspects of the resulting financial strategy are:

- **diversification** of the sources of financing, raising funds on both the capital markets and in the form of borrowings from major banks and supranational financial institutions;
- a **balance** between short and medium-term instruments, in keeping with the composition of assets;
- the **proactive management** of debt in order to take advantage of the opportunities offered by the capital markets;
- a commitment to maintaining **high credit ratings**, based on a strong financial position;
- **active management of the financial risks** to which the Company is exposed, as set out in more detail in the section, "Risk management".

Fully in line with Terna's strategy, which aims to combine investment and sustainability to drive growth and value creation, it is **Terna's ambition to play a leading role in the sustainable finance market**.

This strategy was implemented during 2018 through the €750 million *green bond issue* launched in July (the issue was subsequently increased to €1 billion in January 2019), and again confirmed with the signature, in September 2018, of a €900 million ***Revolving Credit Facility*** **linked to sustainability indicators** (increased to up to €1.15 billion in November 2018).

As further confirmation of our commitment to playing an active role in the development of sustainable finance, **on 15 January 2019, Terna joined the Corporate Forum for Sustainable Finance**, a network of 16 major European companies committed to developing sustainable finance as a way of combatting climate change and promoting a more sustainable and responsible society.


Fully in line with Terna's strategy, which aims to combine investment and sustainability to drive growth and value creation, it is Terna's ambition to play a leading role in the sustainable finance market. This strategy was implemented during 2018 **through the €750 million green bond issue launched in July**, with the proceeds to be used to finance or refinance "Eligible Green Projects". These are projects producing environmental benefits that meet certain criteria (the use of the issue proceeds, the process of selecting and assessing projects, management of the issue proceeds and reporting) listed in the "Green Bond Framework", published by Terna in compliance with the "Green Bond Principles 2018" drawn up by the ICMA (International Capital Market Association). Specifically, the net proceeds from the issues will be sued to finance:

- projects that aim to increase renewable energy production - for example, infrastructure enabling renewable energy plants to be connected to the national grid or that allow for a larger volume of renewable energy to be injected into the grid;
- projects designed to cut carbon emissions by reducing grid losses - for example, infrastructure designed to boost the efficiency of the electricity transmission gird;
- projects that aim to reduce soil use and protect biodiversity.

In September, moreover, the Company **signed its first revolving credit facility**, amounting to €900 million, that uses a mechanism based on a series of bonuses and penalties linked to the achievement of specific environmental, social and governance ("ESG") objectives. The facility was then increased to €1.15 billion in November.

In 2019, Terna has confirmed its commitment to the development of sustainable finance with the issue, in January, of a new **Green Bond** in the form of a private placement, reopening the earlier issue in July 2018.

In April 2019, moreover, was launched a **Green Bond** amounting to €500m, intended to institutional investors. In line with the previous green emissions, the net proceeds from the issuance will be used to finance the company's eligible green projects of the Company.

A few days later, the Company joined the "Forum on Sustainable Finance", together with other major European companies committed to developing sustainable finance as a way of combatting climate change and promoting a more sustainable and responsible society.

Focus on sustainable finance

The conditions obtained make Terna's bonds the highest yielding corporate issue in 2018 at national level

Debt is described in detail in the section, "Financial review".

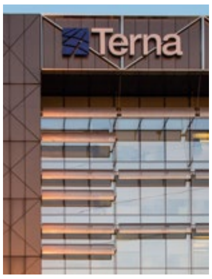
STRATEGY AND FINANCIAL RISK MANAGEMENT

Market, liquidity and credit risk

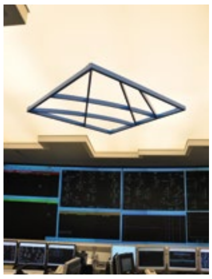
Terna adopts a dynamic approach to managing the various forms of financial risk, including market risk (interest rate, exchange rate and inflation risk), liquidity risk and credit risk. This approach includes constant monitoring of the financial markets, in order to carry out planned hedging operations under favourable market conditions, but also to take advantage of opportunities to improve existing hedges, when changes in market conditions or the hedged items make previous hedges unsuitable or excessively costly.
Further details are provided in the notes to the consolidated financial statements and to the Parent Company's separate financial statements.

Key events relating to finance during the year and in early 2019 are described below:

- On **3 April 2019** TERNA S.p.A. launched a green bond addressed to institutional investors. The issuance is made under Terna's Euro 8,000,000,000 Medium Term Notes Programme (EMTN), which has been rated "BBB+" by Standard & Poor's, "(P)Baa2" by Moody's and "BBB+" by Fitch for an aggregate amount of 500 million Euro. The green bond has been issued with a tenor of 7 years and a maturity date falling on 10 April 2026, will pay a coupon of 1.000%, with an issue price equal to 99.886%, a spread of 78 basis points over the midswap and an indicative spread of approximately 100 basis points lower than the Italian BTP having same maturity. The actual cost for Terna, in respect of such issuance, is therefore equal to 1.02% as opposed to the aggregate average cost of the consolidated debt equal to 1.6% over the new Strategic Plan period. The net proceeds from the issuance will be used to finance the company's eligible green projects of the Company.
- On **10 January 2019**, Terna launched a fixed-rate green bond issue in the form of a private placement, amounting to €250 million, reopening the bond issue of 23 July 2018. The bonds form part of the Company's €8 billion Euro Medium Term Notes programme. The securities, maturing on 23 July 2023, will pay a coupon of 1.000% and will be issued at a price equal to 99.787%, with a spread of 90 basis points with respect to the midswap rate and a yield of 1.05%, slightly below that of the July 2018 issue. The proceeds will be used to finance the Company's eligible green projects.
- On **16 November 2018**, Terna S.p.A. signed an agreement amending the ESG-linked back-up Revolving Credit Facility obtained on 24 September 2018 from a pool of banks made up of Banca IMI, Banco BPM, BNP Paribas and UniCredit as Joint Mandated Lead Arrangers, with the aim of increasing the total amount of the facility from €900 million to €1,150 million, following the inclusion of Mediobanca - Banca di Credito Finanziario in the transaction as a new lender. All the other terms and conditions in the agreement signed on 24 September 2018 continue to apply.








- Shortly after achieving the highest ranking among the world's electric utilities in the Dow Jones Sustainability Index 2018, on **24 September 2018**, Terna entered into a committed ESG-linked back-up Revolving Credit Facility, with a value of €900 million, with a pool of banks made up of Banca IMI, Banco BPM, BNP Paribas and UniCredit as Joint Mandated Lead Arrangers. BNP Paribas worked in partnership with Terna in the role of Sustainability Coordinator. At the same time, the Company cancelled a €750 million line of credit expiring on 11 December 2019. The new revolving credit facility introduces elements relating to sustainability through a series of bonuses and penalties linked to the achievement of specific environmental, social and governance ("ESG") objectives. The facility is for a period of 5 years and will be used to fund the Company's day-to-day operations. The interest rate is linked to EURIBOR plus an initial spread of 0.65% (variable between a minimum of 0.6% and a maximum of 1.45% depending on Terna's rating). The transaction means that Terna can count on adequate liquidity in respect of its current rating, and confirms the Group's strong commitment to introducing a model aimed at reinforcing the role of sustainability as a strategic lever in the creation of value for all its stakeholders.
- On **16 July 2018**, Terna successfully launched a fixed-rate green bond issue amounting to €750 million under its €8 billion Euro Medium Term Notes (EMTN) Programme. The bonds have a term to maturity of 5 years and pay coupon interest of 1%, with a yield of 1.08% (mid-swap + 80bps). The cost of the borrowing is below the overall average cost envisaged in the Strategic Plan, given that the transaction marked the reopening of the corporate bond market after a number of months of inactivity caused by rising yields. This is undoubtedly a positive development, not only for Terna but for the sector as a whole. The issue was six times oversubscribed, leading to the issue being increased from €500 million to €750 million when the bonds started trading.
- On **15 March 2018**, the Project Finance agreement worth US$81 million, signed on 14 July 2017 and to be used to fund construction of a 500-kV transmission line in Uruguay, was awarded the prize for "Latin America Transmission/Distribution deal of the year", organised by IJ Global's Project Finance and Infrastructure Journal (one of the leading infrastructure publications in the world, focusing on the energy market). The journal is owned by Euromoney, recognised as one of the world's most authoritative sources of financial market information.

RATINGS

	SHORT-TERM	MEDIUM/ LONG-TERM	OUTLOOK	LATEST REVIEW
Terna S.p.A.				
Standard & Poor's	A-2	BBB+	Negative	29 October 2018
Moody's	Prime-2	Baa2	Stable	23 October 2018
Fitch	F2	BBB+	Stable	9 November 2018
Italian state				
Standard & Poor's	A-2	BBB	Negative	26 October 2018
Moody's	Prime-3	Baa3	Stable	19 October 2018
Fitch	F2	BBB	Negative	22 February 2019

"As a major transmission and dispatching operator, we invest in skills, technology and innovation to ensure that we are well equipped to plan, develop and maintain the grid (Transmission Operator), and guarantee an electricity service that is balanced, secure and high quality (System Operator). Italy and Terna are at the centre of a system that includes 25 interconnections with neighbouring countries: this gives us a leading role to play in energy integration in Europe and the Mediterranean area. This know-how is, naturally, also applied in our Non-regulated and International activities."

+2.9%
EBITDA IN 2018

+5.5%
CAPEX IN 2018

+2.5%
TERNA'S SHARE PRICE IN 2018

4 Performance

Financial review 2018

Introduction

The Annual Report for 2018 has been prepared in accordance with the requirements of art. 154-*ter* of Legislative Decree 58/98 introduced by Legislative Decree 195 of 6 November 2007 (the "Transparency Decree"), as amended by Legislative Decree 27 of 27 January 2010.

As required by Legislative Decree 38 of 28 February 2005 and EEC Regulation 1606/2002, the financial statements of the parent company Terna S.p.A. and the consolidated financial statements of the Terna Group for the year ended 31 December 2018 were prepared in compliance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board and endorsed by the European Commission (hereinafter "EU-IFRS").

In compliance with the provisions of art. 2364 of the Italian Civil Code and art. 9.2 of the Company's Articles of Association, the Board of Directors, has decided to call an Annual General Meeting of shareholders within 180 days of the end of the annual reporting period, given that Terna S.p.A. is a company required to prepare consolidated financial statements.

Basis of presentation

The measurement and recognition criteria applied in this Annual Report are consistent with those adopted in the consolidated financial statements for the year ended 31 December 2017, with the exception of the application of the new accounting standards, *IFRS 9 - Financial Instruments* and *IFRS 15 - Revenue from Contracts with Customers*, effective from 1 January 2018. These standards have been applied retrospectively, recognising the immaterial cumulative effect of initial application as an adjustment to the opening balance of retained earnings.

In order to present the performance of the Terna Group and Terna S.p.A. and to analyse the financial positions, separate reclassified statements have been prepared. These differ from the statements required by the EU-IFRS adopted and described in the consolidated and separate financial statements for the year ended 31 December 2018.

These reclassified statements contain alternative performance indicators, which differ from those resulting directly from the separate and consolidated financial statements. Management considers these indicators to be useful in assessing the performances of the Group and of Terna S.p.A. and representative of the business's operating results and financial position.
In line with the guidance provided by ESMA/2015/1415, the criteria used in constructing these indicators are described in specific notes, reconciling them with the amounts presented in the consolidated and separate financial statements. The notes are contained in an annex to this Integrated Report.

In addition, a number of comparative amounts in the income statement have been reclassified in order to improve presentation, without changing the comparative result. These amounts include those relating to the margin earned on overseas concessions, recognised in International revenue, and the classification of revenue from construction services performed under concession in Italy in Regulated Activities in Italy.

The Terna Group

Scope of consolidation

The following changes in the structure of the Group have taken place with respect to 31 December 2017:

- part of the process of identifying and acting on new commercial opportunities for the provision of energy efficiency services and projects, on 15 February 2018, the acquisition of a 70% interest in **Avvenia The Energy Innovator S.r.l.** was completed;
- **Resia Interconnector S.r.l.** was established on 16 July 2018 in relation to the construction of the private Italy-Austria interconnection, for which the authorisation process regarding the Passo Resia-Glorenza cable section is in progress and is expected to be completed in 2019;
- The partial demerger of Terna Plus S.r.l. (a wholly-owned subsidiary of the parent, Terna S.p.A.), and the transfer of the demerged assets to a newly-established company named **Terna Energy Solutions S.r.l.**, became effective on 2 August 2018. The demerged business is focused on Non-regulated Activities and on the energy solutions activities already carried out by Terna Plus. Following the demerger, the latter company has assumed responsibility for the activities in South America. The demerger also resulted in the transfer, to Terna Energy Solutions, of the investments in companies that carry out Non-regulated Activities in Italy: Tamini Trasformatori S.r.l., Rete Verde 17 S.r.l., Rete Verde 18 S.r.l., Rete Verde 19 S.r.l., Rete Verde 20 S.r.l. and Avvenia The Energy Innovator S.r.l. (acquired on 15 February 2018).

The Group's reclassified income statement

The Terna Group's operating results for the year ended 31 December 2018, compared with those for the previous year, are summarised in the following reclassified income statement, obtained by reclassifying amounts in the statutory consolidated income statement.

(€m)

	2018	2017	CHANGE	% CHANGE
TOTAL REVENUE	**2,197.0**	**2,162.8**	**34.2**	**1.6**
- Regulated revenue in Italy	1,989.6	1,967.2	22.4	1.1
of which Revenue from construction services performed under concession	*25.5*	*21.1*	*4.4*	*20.9*
- Non-Regulated revenue	194.9	189.1	5.8	3.1
- International revenue*	12.5	6.5	6.0	92.3
TOTAL OPERATING COSTS	**546.4**	**558.9**	**(12.5)**	**(2.2)**
- Personnel expenses	238.8	252.6	(13.8)	(5.5)
- Cost of services, leases and rentals	176.5	170.4	6.1	3.6
- Materials	77.9	69.4	8.5	12.2
- Other costs	22.6	34.9	(12.3)	(35.2)
- Quality of service	5.1	10.5	(5.4)	(51.4)
- Cost of construction services performed under concession	25.5	21.1	4.4	20.9
GROSS OPERATING PROFIT (EBITDA)	**1,650.6**	**1,603.9**	**46.7**	**2.9**
- Amortisation, depreciation and impairment losses	554.1	526.5	27.6	5.2
OPERATING PROFIT (EBIT)	**1,096.5**	**1,077.4**	**19.1**	**1.8**
- Net financial income/(expenses)	(88.8)	(88.8)	-	-
PROFIT/(LOSS) BEFORE TAX	**1,007.7**	**988.6**	**19.1**	**1.9**
- Income tax expense for the period	296.1	294.4	1.7	0.6
PROFIT FOR THE YEAR	**711.6**	**694.2**	**17.4**	**2.5**
Profit/(Loss) attributable to non-controlling interests	5.0	5.9	(0.9)	(15.3)
PROFIT FOR THE PERIOD ATTRIBUTABLE TO OWNERS OF THE PARENT	**706.6**	**688.3**	**18.3**	**2.7**

(€m)

EBITDA BY OPERATING SEGMENT	2018	2017	CHANGE
Regulated Activities in Italy	1,586.5	1,541.7	44.8
Non-regulated Activities	60.5	62.4	(1.9)
International Activities	3.6	(0.2)	3.8
EBITDA	**1,650.6**	**1,603.9**	**46.7**

Gross operating profit (EBITDA) for the year amounts to **€1,650.6 million**, up €46.7 million compared with the €1,603.9 million of 2017. This primarily reflects the improved result from Regulated Activities in Italy.

Revenue

(€m)

REGULATED ACTIVITIES IN ITALY	2018	2017	CHANGE
Tariff revenue	**1,932.2**	**1,915.5**	**16.7**
Other regulated revenue	31.9	30.6	1.3
Revenue from construction services performed under concession in Italy	**25.5**	**21.1**	**4.4**
TOTAL	**1,989.6**	**1,967.2**	**22.4**

Regulated revenue in Italy is up €22.4 million, primarily due to ARERA's recognition of certain expenses not covered by the dispatching charge after revision of the transmission charge, reflecting the different performances of revenue from work in progress, including the impact of the revised contribution from international interconnections.

(€m)

NON-REGULATED ACTIVITIES	2018	2017	CHANGE
Tamini	103.4	92.6	10.8
Services for third parties (telecommunications. energy solutions. other)	82.5	80.5	2.0
Italy-France interconnector	9.0	16.0	(7.0)
TOTAL	194.9	189.1	5.8

The increase in **Non-Regulated revenue**, totalling €5.8 million, reflects revenue growth at the **Tamini Group**, after a reduction in revenue linked to the **private Italy-France interconnector** project (reflecting one-off proceeds booked in 2017).

(€m)

INTERNATIONAL ACTIVITIES	2018	2017	CHANGE
Latin America	10.9	4.0	6.9
Other	1.6	2.5	(0.9)
TOTAL	12.5	6.5	6.0

International revenue is up €6 million, reflecting revenue generated by investment in assets held under concession in **Brazil** (up €12.4 million), after the loss recognised on the contract for construction of the power line in **Uruguay** (down €5.4 million).

Costs

Operating costs are down €12.5 million compared with the previous year. Without taking into account the increase in the cost of work carried out under concession, this reflects the following:

- **Personnel expenses**: down €13.8 million, primarily due to due to net provisions for the early retirement scheme launched in 2017 (down €19.6 million), after the significant increase in the average workforce as a result of the launch of the new initiatives envisaged in the Strategic Plan;
- **Services, leases and rentals:** up €6.1 million, primarily due to revised right-of-way fees in certain regions of Italy and external services, after the reduction in external costs on contract work;
- **Materials:** up €8.5 million, primarily due to an increase in contract work at Tamini and Avvenia;
- **Quality of service:** down €5.4 million, primarily due to the higher costs incurred in 2017 in relation to certain major events in central and southern Italy, with respect to outages in 2018 essentially due to events in northern Italy in October;
- **Other operating costs:** down €12.3 million, broadly due to the adjustment to the Group's provisions for risks and charges.

Amortisation, depreciation and impairment losses for the year amount to €554.1 million, up €27.6 million compared with 2017, primarily due to the entry into service of new plant.

Operating profit (**EBIT**), after amortisation, depreciation and impairment losses, amounts to **€1,096.5 million**, compared with €1,077.4 million for 2017 (up 1.8%).

Net financial expenses for the year total €88.8 million, primarily attributable to the Parent Company (€84.0 million), and are in line with the previous year.

After net financial expenses, **profit before tax** amounts to **€1,007.7 million**, up €19.1 million compared with the previous year (up 1.9%).

Income tax expense for the year totals €296.1 million, an increase of €1.7 million (0.6%) compared with the previous year, essentially due to the improved profit before tax. The tax rate for the year is 29.4%, broadly in line with the 29.8% of 2017.

Profit for the year amounts to **€711.6 million**, an increase of €17.4 million (2.5%) compared with the €694.2 million of 2017.

Profit for the year attributable to owners of the Parent (after excluding the share attributable to non-controlling interests) amounts to **€706.6 million**, up €18.3 million (2.7%) compared with the €688.3 million of 2017.

Cash flow

The above performance, combined with non-cash items and other cash flows from and for operating activities, has resulted in a cash inflow of €1,474.5 million, enabling the Group to finance a large part of its investing activities (€1,091.1 million) and provide a return on equity (€486.4 million, including €451.1 million in the form of dividends paid to shareholders). The balance is financed by net debt, which totals €7,899.4 million, compared with €7,796.4 million at the end of 2017 (up €103 million).

(€m)

	CASH FLOW 2018	CASH FLOW 2017
- Profit for the year	711.6	694.2
- Amortisation, depreciation and impairment losses	554.1	526.5
- Net change in provisions	(48.3)	(28.8)
- Net losses/(gains) on sale of assets	(3.5)	(2.1)
Operating cash flow	**1,213.9**	**1,189.8**
- Change in net working capital	336.6	408.3
- Other changes in property, plant and equipment and intangible assets	36.0	137.5
- Change in investments	1.7	(2.7)
- Change in financial assets	(113.7)	(98.7)
Cash flow from operating activities	**1,474.5**	**1,634.2**
- Total capital expenditure	(1,091.1)	(1,033.9)
Free cash flow	**383.4**	**600.3**
- Dividends paid to the Parent Company's shareholders	(451.1)	(418.4)
- Cash flow hedge reserve after taxation and other movements in equity attributable to owners of the Parent	(39.6)	(2.0)
- Other movements in equity attributable to non-controlling interests	4.3	-
Change in net debt	**(103.0)**	**179.9**

The Group's reclassified statement of financial position

The Terna Group's financial position at 31 December 2018 and 31 December 2017 is summarised below in the reclassified statement of financial position, obtained by reclassifying amounts in the statutory consolidated statement of financial position.

(€m)

	AT 31 DECEMBER 2018	AT 31 DECEMBER 2017	CHANGE
Total net non-current assets	**14,083.6**	**13,466.4**	**617.2**
- Intangible assets and goodwill	519.4	505.7	13.7
- Property, plant and equipment	13,244.3	12,752.8	491.5
- Financial assets	319.9	207.9	112.0
Total net working capital	**(1,822.5)**	**(1,485.2)**	**(337.3)**
- Net energy-related pass-through payables	(777.6)	(852.7)	75.1
- Net receivables resulting from Regulated Activities	313.9	335.1	(21.2)
- Net trade payables	(860.7)	(714.4)	(146.3)
- Net tax assets	50.9	105.9	(55.0)
- Other net liabilities	(549.0)	(359.1)	(189.9)
Gross invested capital	**12,261.1**	**11,981.2**	**279.9**
Sundry provisions	(307.5)	(355.8)	48.3
NET INVESTED CAPITAL	**11,953.6**	**11,625.4**	**328.2**
Equity attributable to owners of the Parent	**4,019.2**	**3,803.3**	**215.9**
Equity attributable to non-controlling interests	**35.0**	**25.7**	**9.3**
Net debt	**7,899.4**	**7,796.4**	**103.0**
TOTAL	**11,953.6**	**11,625.4**	**328.2**

The €617.2 million increase in **net non-current assets** compared with 31 December 2017 primarily reflects a combination of the following:

- an increase of €112.0 million in financial assets, mainly due to construction services performed under concession in Brazil during the period (up €94.3 million) and an increase in the Interconnector Guarantee Fund, set up to fund investment in interconnections by art. 32 of Law 99/09 (up €18.9 million);
- total capital expenditure of €1,091.1 million, as described below;
- amortisation and depreciation for the year, totalling €540.0 million;
- other movements during the year, resulting in a reduction of €41.3 million, including grants related to assets (primarily in relation to projects financed by the Ministry for Economic Development and the EU and to the re-routing of power lines at the request of third parties); disposals and impairment losses, resulting in a reduction of €22.6 million.

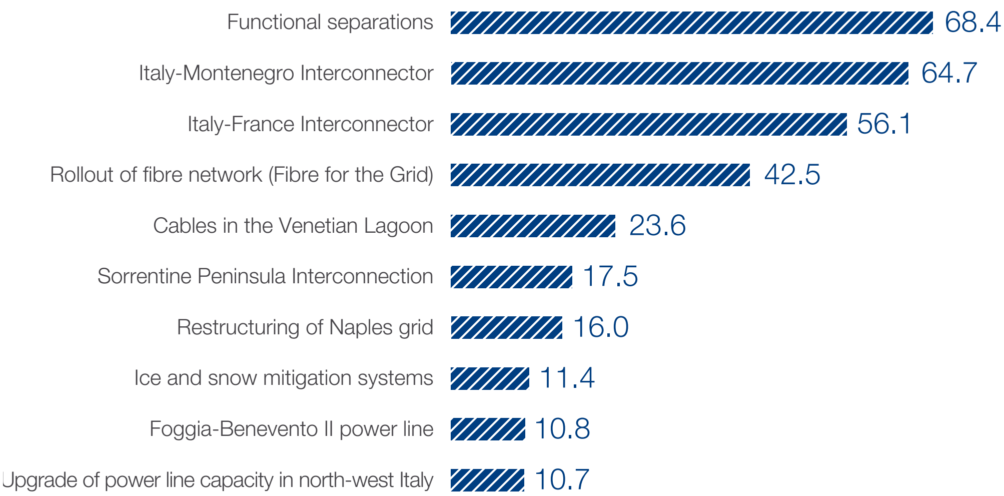
The change during the period also reflects the contribution from the acquisition of Avvenia the Energy Innovator S.r.l. (€17.6 million, primarily reflecting the company's order book).

The Group's **capital expenditure** totalled **€1,091.1 million** in 2018, up **5.5%** on the €1,033.9 million of 2017. Of this amount, investment incentives amounted to **€99.5 million**, compared with €122.8 million in 2017.

Investment in non-regulated assets, amounting to €87.4 million, primarily regards the private part of the Italy-France interconnector.

The following chart shows key capital expenditure on the NTG RTN in 2018:

KEY CAPITAL EXPENDITURE* (€m)



** Amounts include financial expenses.*

A total of 159 km of power lines entered service in 2018 (Bono-Buddusò, Villanova-Cepagatti, Benevento II-Benevento III, Messina-Riviera-Villafranca, Ciminna-Casuzze, Sacca Fisola-Fusina and the connections between the San Salvo, the Main Naples and the Naples Levante substations), alongside the San Severo, Quartu-Quartucciu, Santa Teresa, San Salvo, Portella Pero, Siculiana, Ravenna Industrial Park and Canino substations.

Net working capital (net current liabilities) of €1,822.5 million generated cash of €337.3 million during the year compared with 2017. This reflects the combined effect of:

Cash inflows

- an increase of €146.3 million in **net trade payables**, largely due to the increase in capital expenditure towards the end of the year;
- a reduction of €21.2 million in **net energy-related pass-through receivables**, primarily reflecting payment by the Fund for Energy and Environmental Services (*Cassa per i Servizi Energetici e Ambientali-CSEA*) of the RENS bonus for the quality of service provided in 2016 (€25.6 million);
- an increase of €189.9 million in **other net liabilities**, primarily due to increases in payments on account received from the entities financing the Italy-France Interconnector (up €106.1 million), in the provision for the Interconnector Guarantee Fund set up by Terna S.p.A. following the issue of the 2016 Stability Law (up €21.9 million) and in government grants received during the year (€61.6 million, primarily from the Ministry for Economic Development).

Cash outflows

- an increase in **net energy-related pass-through payables** of €75.1 million, primarily reflecting the combined effect of:
  - a reduction in net payables resulting from transactions on the Dispatching Services Market (€24.4 million) and from imbalances (€99.7 million); these changes in DSM and imbalance costs are reflected in the amount receivable for procuring resources on the Dispatching Services Market (the uplift), which is down €68.9 million compared with the end of 2017;
  - a reduction in net payables linked to plants that are essential for the security of the electricity system - *UESS* (€127.2 million), reflecting increased payments approved by ARERA compared with the previous year;
  - an increase in amounts due from the from the Fund for Energy and Environmental Services (*Cassa per i Servizi Energetici e Ambientali* - CSEA) linked to the interruptibility service (€10.6 million);
  - an increase in payables relating to capacity payments (€125.4 million), resulting from items collected after payments made in 2018;
- a reduction in **net tax assets** of €55 million, primarily reflecting a decrease in the Group's refundable VAT (down €32.7 million), due to higher payments on account in the previous year as a result of the Ministerial Decree of 27 June 2017, after refundable VAT accruing on the increased volume of purchases made by subsidiaries towards the end of the year. The change also reflects a reduction in net income tax assets (down €22.7 million), essentially due to higher payments on account made in the previous year (determined on the basis of a higher rate of IRES applied in 2016) and an increase in tax payable for the period (essentially due to the increase in pre-tax profit).

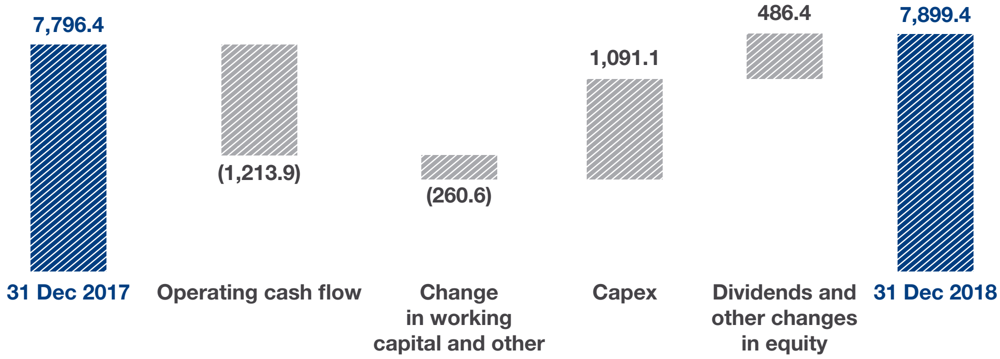
Gross invested capital thus amounts to €12,261.1 million, marking an increase of €279.9 million compared with the end of the previous year.

Sundry provisions are down €48.3 million, primarily due to:

- the adjustment to provisions for employee benefits (down €11.3 million), with particular regard to agreements relating to the energy discounts granted to pensioners), uses during the year in relation to the existing plan for generational turnover (down €9.6 million), the higher value of provisions made in the previous year for urban and environmental redevelopment schemes (down €7.3 million), favourable outcomes to a number of disputes arising in previous years (down €4.9 million) and the payment, by ARERA, of expenses not covered by the transmission and dispatching charges (down €6.6 million);
- provisions for net deferred tax liabilities (down €11.9 million), primarily due to the effect on taxation of amortisation and depreciation and uses of provisions for risks and charges.

Net invested capital of €11,953.6 million is up €328.2 million compared with 31 December 2017 and is financed by equity attributable to owners of the Parent, totalling €4,019.2 million (compared with €3,803.3 million at 31 December 2017), equity attributable to non-controlling interests of €35 million (€25.7 million at 31 December 2017) and net debt of €7,899.4 million (up €103 million compared with the €7,796.4 million of 31 December 2017).

CHANGE IN NET DEBT (€m)

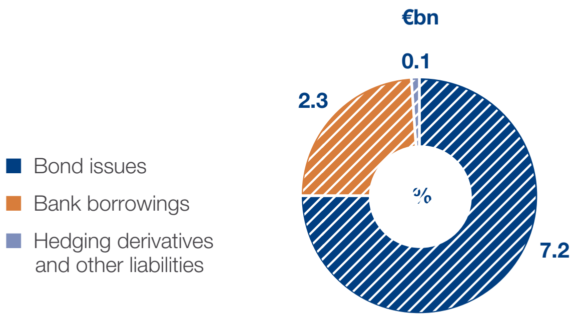


Debt

The Group's financial policy and gross debt

The key aspects of the Group's financial policy are diversification of the sources of funding, a balance between short- and medium/long-term forms of debt and the proactive management of debt.

Gross debt at 31 December 2018 amounts to approximately **€9.6 billion**, consisting of €7.2 billion in the form of bond issues and €2.3 billion in bank borrowings. The average term to maturity of debt, which is almost all fixed rate, is approximately 5.2 years.



Fixed/ variable rate	Maturity	Cost of debt
~100% fixed *as proportion of gross debt*	5.2 years	1.3%

Bonds have been issued in the form of both public and private placements under the €8 billion Euro Medium Term Notes (EMTN) Programme (in which a large number of Italian and overseas banks participate), in addition to a stand-alone issue of €800 million dating back to 2004. Focused specifically on qualified investors and listed on the Luxembourg Stock Exchange, Terna's bonds have a very diverse investor base, in terms of both sector and geographical profile.

The main provider of Terna's bank loans is the European Investment Bank (EIB). Total borrowings from the EIB at 31 December 2018 amount to almost €2.2 billion (including €46 million yet to be drawn on). Thanks to its strong credit ratings, Terna is able to obtain financing from banks on extremely good terms, as shown by the refinancing of the Revolving Credit Facility expiring in 2019 with a new revolving facility of €900 million, obtained in September and increased by a further €250 million in November. The Group currently has three committed, revolving credit facilities, amounting to €2.5 billion.

Net debt

The Group's net debt at 31 December 2018 amounts to €7,899.4 million, an increase of €103 million compared with 31 December 2017.

(€m)

NET DEBT (BY TERM TO MATURITY)	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Total medium/long-term debt	**8,286.8**	**8,677.8**	**(391.0)**
- Bond issues	6,563.2	6,541.9	21.3
- Borrowings*	1,664.4	2,125.4	(461.0)
- Derivative financial instruments	59.2	10.5	48.7
Total short-term debt/ (funds)	**(387.4)**	**(881.4)**	**494.0**
- Bond issues (current portions)	616.7	749.9	(133.2)
- Short-term borrowings	25.0	118.0	(93.0)
- Borrowings (current portions)	616.7	134.4	479.5
- Other current financial liabilities, net	89.8	105.5	(15.7)
- Financial assets	(403.9)	-	(403.9)
- Cash and cash equivalents	(1,328.9)	(1,989.2)	660.3
Total net debt	**7,899.4**	**7,796.4**	**103.0**
NET DEBT (BY TYPE OF INSTRUMENT)			
- Bond issues	7,179.9	7,291.8	(111.9)
- Borrowings*	2,278.3	2,259.8	18.5
- Short-term borrowings	25.0	118.0	(93.0)
- Derivative financial instruments	59.2	10.5	48.7
- Other financial liabilities	89.8	105.5	(15.7)
GROSS DEBT	**9,632.2**	**9,785.6**	**(153.4)**
- Financial assets	(403.9)	-	(403.9)
- Cash and cash equivalents	(1,328.9)	(1,989.2)	660.3
Total net debt	**7,899.4**	**7,796.4**	**103.0**

** This item includes fees on credit facilities.*

Changes in the **Group's net debt** are as follows:

- reduction in bond issues (down €111.9 million), resulting from repayment, in February, of bonds issued in 2012, totalling €750.0 million, the green bond issue of 23 July 2018 (€750 million) and the adjustment to these instruments to reflect their amortised cost;
- an increase in borrowings (up €18.5 million), primarily due to new borrowings €154.2 million, after repayments during the period (down €134.5 million);
- a decrease in short-term borrowings and other financial liabilities (down €108.7 million), primarily due to the Parent Company's repayment of short-term credit facilities and the settlement of interest on borrowings and the related hedges;
- an increase in derivate financial instruments (up €48.7 million), primarily due to the movement in market interest rates and the change in the notional value of the derivatives portfolio;
- an increase in financial assets (up €403,9 million) following the purchase of government securities maturing in December 2019 and having a notional value of €400 million;
- a reduction in cash and cash equivalents (€660.3 million). Cash amounts to €1,328.9 million at 31 December 2018, including €751.5 million invested in short-term, readily convertible deposits and €577.2 million deposited in bank current accounts.

Reconciliation of the Group's profit for the year and equity with the corresponding amounts for the Parent Company

The reconciliation of consolidated equity and consolidated profit for the year and the corresponding amounts for the Parent Company is shown below.

(€m)

	PROFIT FOR FY 2018	EQUITY AT 31 DECEMBER 2018
Parent Company's financial statements	**661.3**	**3,850.9**
Profit and equity contributed by Group companies:		
- Group companies - Regulated Activities	62.4	116.4
- Group companies - Non-Regulated Activities	(9.5)	70.5
- Group companies - International Activities	(4.1)	(15.3)
Companies accounted for using the equity method	1.5	31.7
Total consolidated financial statements	**711.6**	**4,054.2**
Share attributable to non-controlling interests - Non-Regulated Activities	5.0	35.0
Terna Group's consolidated financial statements	**706.6**	**4,019.2**

Terna's shares

+191%

the capital gain since the date of the IPO

Terna and the financial markets

Terna S.p.A. has been listed on Borsa Italiana's screen-based trading system (*Mercato Telematico Azionario*) since 23 June 2004. **From the date of floatation to the end of 2018, the share price has risen 191% (a capital gain)**, providing a Total Shareholder Return (TSR[23]) of 559%, ahead of both the Italian market (FTSE Mib +28%) and the relevant European sector index (DJ Stoxx Utilities), which is up 154%.

Europe's leading stock markets recorded negative performances in 2018, held back by fears of a global economic slowdown. Milan lost 16.1% over the year, with Frankfurt and Paris losing 20.6% and 11%, respectively, and London down 12.5% and Madrid off 15%.

Performance of Terna's shares

Terna's shares, in contrast, ended 2018 in positive territory after an annual increase of 2.25% to €4.953 per share, outperforming the Company's principal peers and the relevant sector index for Europe (the DJ Stoxx Utilities was down 2.1%). The average daily volume traded during the year amounted to approximately 6.6 million shares per day. The ex-dividend date for the interim dividend for 2018, amounting to 7.87 euro cents per share, was 19 November.

KEY INDICATORS PER SHARE

	2018	2017	2016	2015	2014	2013
Number of shares (in millions)	2,010	2,010	2,010	2,010	2,010	2,010
Price at year end (€ per share)	4.95	4.84	4.35	4.76	3.76	3.63
Market capitalisation* (€m)	9.507	9.668	9.367	8.482	7.718	6.713
Average price for year (€ per share)	4.73	4.81	4.66	4.22	3.84	3.34
Earnings per share (€)	0.352	0.339	0.315	0.296	0.271	0.256
Dividend per share (€)	0.233	0.220	0.206	0.200	0.200	0.200
Payout ratio	70.88%	66.63%	77.32%	76.30%	89.30%	88.40%
Dividend yield**	4.7%	4.5%	4.7%	4.2%	5.3%	5.5%
Total shareholder return	7.3%	15.90%	-4.3%	32.5%	8.9%	27.6%

* *Based on the average price for the year.*
** *Dividend per share for the year as a percentage of the share price at year end.*

WEIGHTING OF TERNA'S SHARES	2018	2017
> on the FTSE MIB	2.42%	1.94%

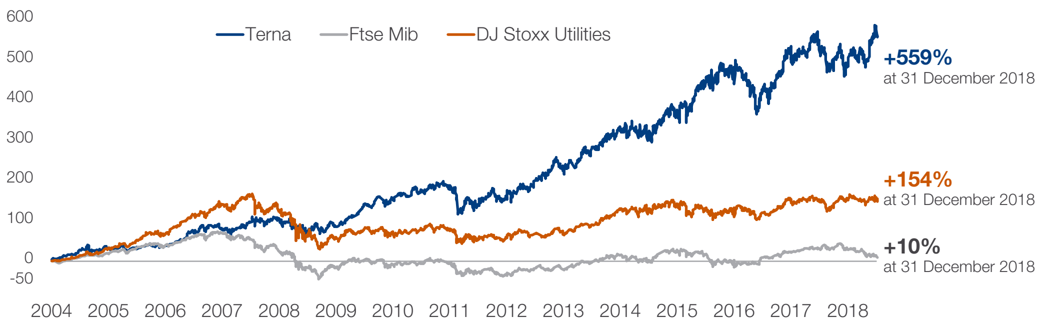
Source: Borsa Italiana.

[23] Total Shareholder Return (TSR): total return on an equity investment, calculated as the sum of:
I. the capital gain: the change in the share price (difference between the price at the end and at the beginning of the relevant period) as a percentage of the price at the beginning of the period;
II. reinvested dividends: the ratio between dividends per share paid out during the period and the share price at the beginning of the period. Dividends are assumed to have been reinvested in the shares.

PERFORMANCE OF TERNA'S SHARES - *Price (2018)*

Source: Bloomberg

PERFORMANCE OF TERNA'S SHARES – Total Shareholder Return (from their floatation to the end of 2018) (%)



Source: Bloomberg

Inclusion in stock exchange sustainability indices

Terna's commitment to measuring and improving its ESG (Environmental, Social and Governance) performance is reflected positively in the sustainability ratings.

Terna's inclusion in all the leading international stock exchange sustainability indices was confirmed in 2018. In September, on the occasion of the annual review conducted by the Swiss sustainability rating agency, RobecoSAM, Terna's presence in the Dow Jones Sustainability Index (World and Europe) was confirmed, and the Company was named **Industry Leader in the Electric Utilities sector**.

INDEX	TERNA
BLOOMBERG GENDER EQUALITY INDEX	Included since January 2019
DOW JONES SUSTAINABILITY INDEX	Included since 2009
ECPI	Included since 2007
ETHIBEL SUSTAINABILITY INDEX (ESI)	Included since 2009
EURONEXT VIGEO	Included in the World 120, Eurozone 120 and Europe 120 baskets since 2012
FTSE ECPI	Included since 2010
FTSE4Good	Included in the index (Global and Europe baskets) every year since 2005
MSCI GLOBAL SUSTAINABILITY	Included regularly in the index since 2007
STOXX® ESG	Included in the index since 2011
STOXX® LOW CARBON	Included in the index since February 2016, the date the index was launched
UNITED NATIONS GLOBAL COMPACT ("GC100")	Included in the index since 2013

In recognition of its ranking as "Industry Leader", Terna was included in the Gold Class in RobecoSAM's "Sustainability Yearbook 2019", published in January 2019.

Terna S.p.A.

A review of the operating performance and financial position of the Parent Company, Terna S.p.A., is provided below.

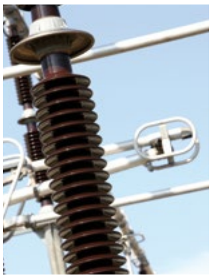
Terna S.p.A.'s reclassified income statement

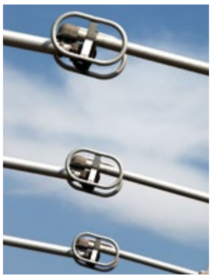
Terna S.p.A.'s operating results for the years 2018 and 2017 are summarised in the following reclassified income statement, obtained by reclassifying amounts in the statutory income statement.

(€m)

	2018	2017	CHANGE
TOTAL REVENUE	**1,967.6**	**1,951.5**	**16.1**
- Tariff revenue	1,800.6	1,786.4	14.2
of which transmission revenue	*1,657.5*	*1,674.5*	*(17.0)*
of which dispatching, metering and other revenue	*143.1*	*111.9*	*31.2*
- Other operating income	141.5	144.0	(2.5)
- Revenue from construction services performed under concession*	25.5	21.1	4.4
TOTAL OPERATING COSTS	**452.0**	**464.9**	**(12.9)**
- Personnel expenses	63.6	65.7	(2.1)
- Cost of services, leases and rentals	343.8	332.1	11.7
- Materials	0.9	7.0	(6.1)
- Other costs	13.1	28.5	(15.4)
- Quality of service	5.1	10.5	(5.4)
- Cost of construction services performed under concession*	25.5	21.1	4.4
GROSS OPERATING PROFIT (EBITDA)	**1,515.6**	**1,486.6**	**29.0**
- Amortisation, depreciation and impairment losses	517.9	495.2	22.7
OPERATING PROFIT/(LOSS) (EBIT)	**997.7**	**991.4**	**6.3**
- Net financial income/(expenses)	(78.5)	(89.8)	11.3
PROFIT/(LOSS) BEFORE TAX	**919.2**	**901.6**	**17.6**
- Income tax expense	257.9	261.6	(3.7)
PROFIT FOR THE YEAR	**661.3**	**640.0**	**21.3**

Gross operating profit (EBITDA) for 2018 amounts to €1,515.6 million, an increase of €29.0 million compared with the previous year. This primarily reflects the overall increase in tariff revenue and a reduction in costs as a result of the favourable outcomes to a number of disputes arising in previous years.




The increase in **revenue** (equal to €16.1 million) primarily reflects growth in dispatching, metering and other revenue (up €31.2 million), above all due to the recognition of certain expenses[24] not covered by the dispatching charge. This was partially offset by the reduction in the transmission charge (down €17.0 million), following a revision of the related tariff to reflect completion, in 2017, of revenue from work in progress and a reduction in the volume of energy transported, offset by an increase in the portion of the NTG owned by Terna. The balance also includes the estimated impact of the revised contribution from international interconnections.

Operating costs are down €12.9 million, primarily due to reductions in other operating costs (down €15.4 million), broadly reflecting the favourable outcomes to a number of disputes arising in previous years, in the cost of materials (down €6.1 million, mainly in relation to the telecommunications business) and in costs incurred for the quality of service (down €5.4 million). These reductions were partially offset by increases in service costs and lease expense (up €11.7 million), primarily relating to intercompany services rendered under specific intercompany contracts and revised right-of-way fees in certain regions of Italy.

Amortisation, depreciation and impairment losses for the year amount to €517.9 million, up €22.7 million compared with 2017, primarily due to the entry into service of new plant.

Operating profit (**EBIT**) thus amounts to €997.7 million, up €6.3 million on the figure for 2017.

Net financial expenses for the year total €78.5 million, a reduction of €11.3 million compared with the €89.8 million of 2017. This primarily reflects an increase in interest income due to an increase in liquidity invested during the year and the improved return on that liquidity, as well as an increase in capitalised financial expenses linked to an increase in the Company's capital expenditure during the year.

Income tax expense for the year amounts to €257.9 million, a reduction of €3.7 million compared with the previous year, essentially due to non-recurring items.

Profit for the year thus amounts to €661.3 million, up €21.3 million on the profit for 2017.

[24] The regulator, ARERA has decided to allow the recovery of expenses through the uplift mechanism provided for in art.44 of Resolution 111/2006. These expenses regard receivables that are no longer recoverable and relating to the period 2006-2015 (ref. Resolution 218/2018) and increased payments made to fund the regulator for the years 2013-2017.

Cash flow

Cash flows in 2018 and pro forma 2017[25] are shown below.

The above performance, combined with non-cash items and other cash flows from and for operating activities, has resulted in a cash inflow of €1,316.5 million, enabling the Parent Company to finance a large part of its investing activities (€886.1 million) and provide a return on equity (€485.7 million, including €451.1 million in the form of dividends paid to shareholders). The balance is financed by net debt, which totals €8,101.8 million, compared with €8,046.5 million at the end of 2017 (up €55.3 million).

(€m)

	CASH FLOW FY 2018	CASH FLOW FY 2017 PRO FORMA
- Profit for the year	661.3	640.0
- Amortisation, depreciation and impairment losses	517.9	495.2
- Net change in provisions	(66.1)	(18.5)
- Net losses/(gains) on sale of assets	(3.0)	(1.7)
Operating cash flow	**1.110.1**	**1.115.0**
- Change in net working capital	243.0	287.3
- Change in investments	(55.7)	(30.0)
- Other movements in property, plant and equipment and intangible assets	38.7	120.1
- Change in financial assets	(19.6)	(24.8)
Cash flow from operating activities	**1.316.5**	**1.467.6**
- Total capital expenditure	(886.1)	(851.9)
Free cash flow	**430.4**	**615.7**
- Dividends paid to shareholders	(451.1)	(418.4)
- Cash flow hedge reserve after taxation and other movements in equity	(34.6)	5.9
Change in net debt	**(55.3)**	**203.2**

[25] The comparative "2017 pro forma" column, previously published last year, takes into account the impact of the merger with and into Terna S.p.A. of the wholly owned subsidiaries of Terna Storage S.r.l. and Terna Rete Italia S.r.l. in the previous year. The merger was effective for accounting and tax purposes from 1 January 2017.

Terna S.p.A.'s reclassified statement of financial position

Terna S.p.A.'s financial position at 31 December 2018 and 2017 is summarised in the following statement, obtained by reclassifying amounts in the statutory statement of financial position.

(€m)

	AT 31 DECEMBER 2018	AT 31 DECEMBER 2017	CHANGE
Total net non-current assets	**13,548.1**	**13,139.6**	**408.5**
- Intangible assets and goodwill	427.7	424.3	3.4
- Property, plant and equipment	12,035.0	11,705.2	329.8
- Financial assets	1,085.4	1,010.1	75.3
Total net current liabilities	**(1,388.0)**	**(1,144.3)**	**(243.7)**
- Net energy-related pass-through payables	(799.7)	(874.4)	74.7
- Net receivables resulting from regulated activities	313.9	335.1	(21.2)
- Net trade payables	(537.6)	(424.5)	(113.1)
- Net tax assets	(14.2)	106.8	(121.0)
- Other liabilities, net	(350.4)	(287.3)	(63.1)
Gross invested capital	**12,160.1**	**11,995.3**	**164.8**
Sundry provisions	(207.4)	(273.5)	66.1
NET INVESTED CAPITAL	**11,952.7**	**11,721.8**	**230.9**
Equity	**3,850.9**	**3,675.3**	**175.6**
Net debt	**8,101.8**	**8,046.5**	**55.3**
TOTAL	**11,952.7**	**11,721.8**	**230.9**

The principal changes with respect to 31 December 2017 are described below.

Net invested capital amounts to €11,952.7 million at 31 December 2018, an increase of €230.9 million compared with the previous year. This reflects an increase in **net non-current assets** (€408.5 million), the cash generated by **net working capital** (down €243.7 million) and a reduction in sundry provisions (€66.1 million).

The change in **net working capital**, represented by a reduction of €243.7 million, is primarily due to an increase in amounts payable to the subsidiary, Terna Rete Italia S.p.A., as a result of the greater volume of capital expenditure carried out towards the end of the year, compared with the same period of 2017, an increase in VAT and income tax payable and an increase in prepayments from third parties (primarily the Ministry for Economic Development) and from the Interconnector Guarantee Fund.

Net non-current assets are up €408.5 million, primarily due to capital expenditure during the year (€886.1 million), after grants deducted directly from the carrying amount of the related assets (€40.5 million, primarily in relation to projects financed by the Ministry for Economic Development), amortisation and depreciation for the year (€503.8 million) and disposals and impairment losses (€15.2 million). The change also reflects the subscription for newly issued shares in the subsidiary, Terna Crna Gora d.o.o. (€59.0 million) and the Interconnector Guarantee Fund, set up by art. 32 of Law 99/09 to fund investment in interconnections (up €18.9 million).

Sundry provisions are down €66.1 million, primarily due to provisions for net deferred tax liabilities (down €35.5 million), mainly due to the effect on taxation of amortisation and depreciation and movements in provisions for risks and charges, uses during the year in relation to the existing plan for generational turnover (down €9.6 million), the higher value of provisions made in the previous year for urban and environmental redevelopment schemes (down €7.3 million), favourable outcomes to a number of disputes arising in previous years (down €5.1 million) and the payment, by ARERA, of expenses not covered by the transmission and dispatching charges (down €6.6 million).

Net debt of €8,101.8 million is up €55.3 million.

(€m)

NET DEBT (BY TYPE OF INSTRUMENT)	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
- Bond issues	7,179.9	7,291.8	(111.9)
- Borrowings*	2,221.8	2,227.5	(5.7)
- Short-term borrowings and other financial liabilities	89.5	195.5	(106.0)
- Derivative financial instruments	59.1	9.9	49.2
Gross debt	**9,550.3**	**9,724.7**	**(174.4)**
- Long- and short-term loans to subsidiaries	(99.5)	-	(99.5)
- Financial assets	(403.9)	-	(403.9)
- Cash and cash equivalents (including the net balance on intercompany current accounts)	(945.1)	(1,678.2)	733.1
Total net debt	**8,101.8**	**8,046.5**	**55.3**

** This item includes fees on credit facilities.*

In addition to the information provided above, the increase in net debt also reflects the loans granted in 2018 to the Latin American subsidiaries (up e€99.5 million).

Proposal

for the Annual General Meeting regarding the distribution of Terna S.p.A.'s profit for the year

Proposal for appropriation of profit for the year

Terna S.p.A.'s Board of Directors proposes to pay a total dividend of €468,730,134.40 for 2018, equal to €0.2332 per share, of which €0.0787 per share was declared in the form of an interim dividend on 9 November 2018.

The Board of Directors thus proposes to appropriate Terna S.p.A.'s profit for 2018, amounting to €661,291,201.83, as follows:

- €158,186,370.40 to cover payment of the interim dividend payable from 21 November 2018;
- €310,543,764.00 to pay a final dividend of €0.1545 to the holders of each of the 2,009,992,000 ordinary shares outstanding at the date of this Board of Directors' meeting. The final dividend will be payable on 26 June 2019, with an ex-dividend date for coupon 30 of 24 June 2019 and a record date (as defined by art.83-terdecies of Legislative Decree 58 of 24 February 1998, the Consolidated Law on Finance of 25 June 2019);
- €192,561,067.43 to be taken to retained earnings.

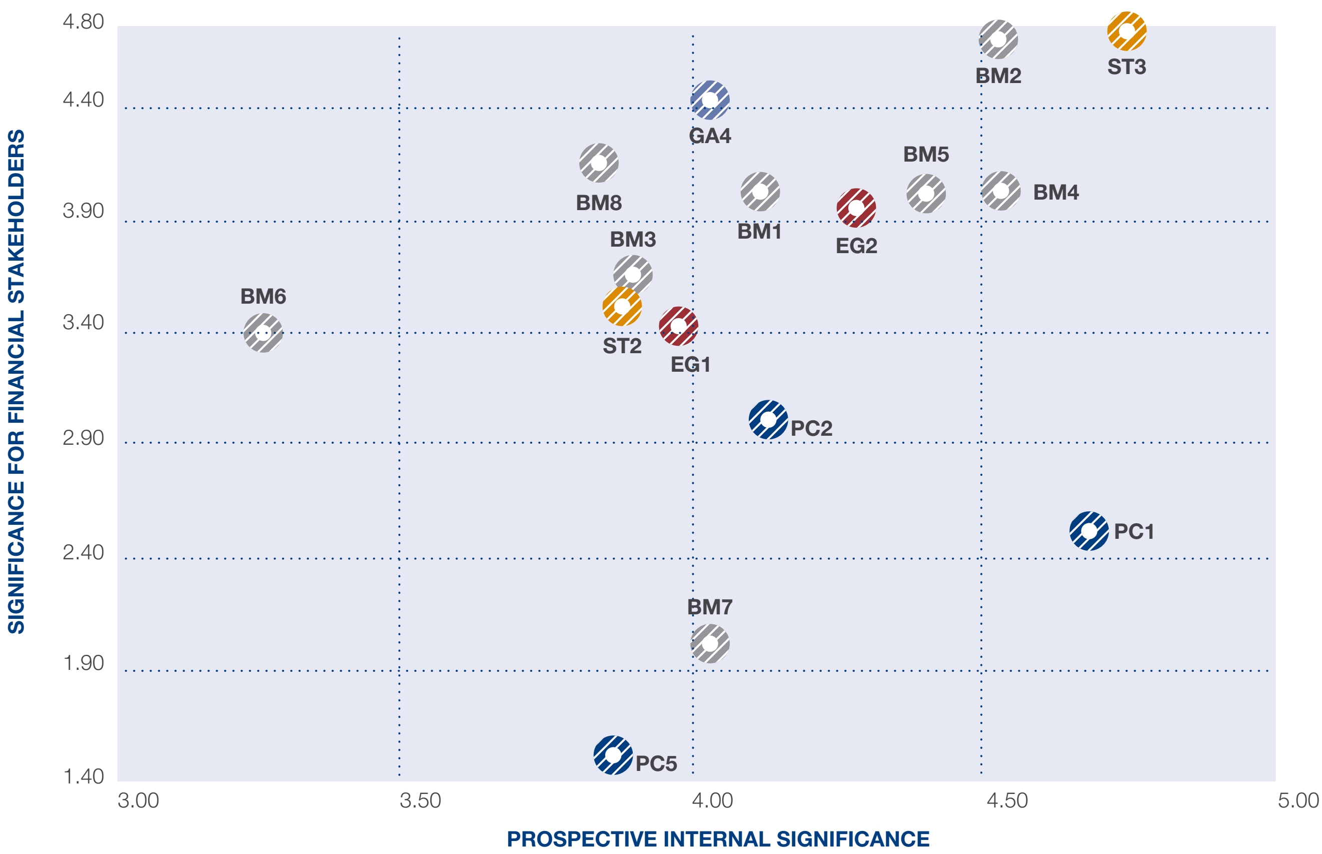
> “We have less than twelve years to deliver on the commitments made by the international community at the Paris climate talks and keep global warming to within the 1.5°C above pre-industrial levels. The Intergovernmental Panel on Climate Change (IPCC) has already reported that the temperature of the Earth has already risen by between 0.8 and 1.2 degrees. Fossil fuels still account for over 80% of global primary energy consumption. This is the reason why decarbonisation is a shared goal throughout the world and is the driving force behind our commitment to do all we can to improve our planet.”

5

Annexes

Materiality analysis

PROSPECTIVE MATERIALITY MATRIX



Ethics and governance model

EG1: Alignment with best governance practices

EG2: Business integrity

Transmission service

ST2: Electricity market integration

ST3: Quality, security and service continuity

People and community

PC1: Health and safety and correct labour practices

PC2: HR development

PC5: Social responsibility and positive impact on local communities

Business management

BM1: Strategic approach to stakeholder management

BM2: Compliance with financial targets

BM3: Prudent risk management

BM4: Choice of investments and conformity with plan

BM5: Engagement with local stakeholders

BM6: Business and development and diversification

BM7: Monitoring of environmental and social aspects of the supply chain

BM8: Innovation and research

Management of environmental impacts

GA4: Reduction of the Group's environmental footprint

In the preparation of its Integrated Report for 2018, Terna has taken into account the guiding principles in the Integrated Reporting Framework developed by the IIRC-International Integrated Reporting Council. One of these principles is materiality, which requires entities to consider, when selecting the matters to cover and the related KPIs, their effective relevance in terms of their role in value creation.

The matters covered in the Integrated Report for 2018 are consistent with the materiality matrix on the previous pages. Construction of the matrix also played a part in the materiality analysis carried out during preparation of the Sustainability Report, which from last year also has the role of "Non-financial statement", now obligatory in accordance with Legislative Decree 254/2016 and also based on the materiality principle.

Key steps in this process are the following:

- **selection of the main topics** for which to determine their significance for Terna and for stakeholders. The selection was conducted in 2016 on the basis of an in-depth analysis of internal and external documents. 23 topics, belonging to 5 areas, were identified: ethics and the governance model; the transmission service; the management of environmental impacts; business management; people and communities;
- **determination of significance for Terna**. The selected topics have been classified according to their importance for Terna. The analysis looked at the degree of active management (the presence of policies, procedures, monitoring, objectives, etc.) of each topic. The Strategic Plan 2018-2022 and the "Sustainability initiatives and KPIs for the Strategic Plan 2019-2023" are the main sources used in assessing materiality in 2018. The analysis also took into account the results of the internal survey on materiality conducted last year, involving second-level heads of department and validated by senior management;
- **determination of significance for stakeholders**. Each topic was ranked by combining the significance of the topic for each category of stakeholder with the weighting assigned to that category in Terna's stakeholder map. In particular, the significance of each topic for a given category of stakeholder was assessed on the basis of a) the analysis of documents, b) the results of specific surveys (e.g. engagement surveys of personnel, questionnaires completed by customers of the Group's non-regulated business) and c) management's perception of the significance of topics for stakeholders with whom they have direct contact.

Further details are provided in the section on materiality in the Sustainability Report-Non-financial Statement.

The materiality matrix used for the Integrated Report differs from the one used for the Sustainability Report-Non-financial Statement as regards the following key aspects:

- the determination of significance for Terna was based on the prospective significance, with reference to the five-year period covered by the Business Plan for 2018-2022: starting from the current level of active management, the need for investment - in boosting management capabilities - in order to achieve the objectives in the Plan was assessed for each topic;
- in determining significance for stakeholders, and again in line with IIRC principles, only the opinions of those belonging to the financial category, meaning "shareholders" (including financial analysts and institutional investors) and "credit providers" (e.g. banks), were taken into account;
- the topics placed in the matrix (16) are those for which, in the set of sources analysed, it was possible to identify the information of significance to financial stakeholders.

In the matrix, the most significant topics are those furthest away from the origin, for both axes.

Regulatory framework and other information

Summary of the principal legislative measures

A brief description is provided below of the principal legislation of interest to the Group issued during 2018 and, subsequently, up to the date of preparation of this Annual Report.

- **Law 205 of 27 December 2017, containing the Budget Law for the 2018 financial year and the long-term budget for the three-year period 2018-2020, published in the Official Gazette of 29 December 2017**
  The 2018 Budget Law extended the option of applying super depreciation and hyper depreciation to capital assets purchased in 2019 and the tax breaks on expenditure on Industry 4.0 training. The law has also introduced contributions holidays for new hires and the option, during the three-year period 2018-2020, to apply for early retirement, up to 7 years before reaching the statutory retirement age, provided there is agreement between the employer and workers regarding the payment of contributions.

- **Law Decree 87 of 12 July 2018, containing urgent measures regarding the dignity of workers and enterprises, converted into Law 96 on 9 August 2018, published in Official Gazette no. 186 of 11 August 2018**
  The Law Decree has amended the legislation on hyper depreciation, with the benefits no longer available for assets transferred overseas, and on the tax relief on additional spending on research and development, excluding intangible assets purchased from companies in the same group from the relief. The legislation also makes access to state aid dependent on jobs and production remaining in Italy. It also places tighter restrictions on the renewal of fixed term contracts and has introduced an increase in the contributions payable on these types of employment relationship.

- **Legislative Decree 107 of 10 August 2018, containing amendments to Italian legislation in order to bring it into line with the provisions of EU Regulation 596/2014 on market abuse, and which has abrogated EU Directive 2003/6/CE and Directives 2003/124/EU, 2003/125/EC and 2004/72/EC, published in the Official Gazette of 14 September 2018**
  The decree has amended Italian legislation on market abuse in line with EU Regulation 596/2014 and requires the issuers of financial instruments to disclose price sensitive information. It has introduced sanctions for so-called "tipping", when a person discloses inside information outside the normal exercise of their employment, profession or duties.

- **Law Decree 119 of 23 October 2018, containing urgent measures on tax and finance, converted into law 136 of 17 December 2018, published in Official Gazette no. 293 of 18 December 2018**
  This Decree contains measures regarding electronic invoicing and the settlement of VAT, extending the "reverse charge" procedure until 2022.

- **Law Decree 135 of 14 December 2018, containing urgent measures on support and simplification for enterprises and the public administration, published in Official Gazette no. 290 of 14 December 2018**
  The Law Decree has abrogated the legislation requiring businesses to keep single electronic records from January and has revised the provisions of the Tenders Code relating to the reasons for the exclusion of economic operators.

- **Law 145 of 30 December 2018, containing the Budget Law for the 2019 financial year and the long-term budget for the three-year period 2019-2021, published in Official Gazette no. 302 of 31 December 2018**
  The 2019 Budget Law has extended the option of applying hyper depreciation to 2019, capping eligible expenditure at €20 million and making the applicable rates of depreciation progressive; it has also extended the tax breaks on expenditure on Industry 4.0 training and the contributions holiday for new hires, above all for young people who have recently graduated from university with a first-class degree and people who have recently completed a doctorate. The law has reduced the deductible portion of additional spending on research and development to 25%, of relating to cost items such as personnel expenses for staff not on permanent contracts and contracts with innovative start-ups and SMEs not belonging the same group. It has also abolished ACE tax relief, which permitted companies to deduct a notional return on new equity from taxable income. Finally, the legislation has increased the tax-deductible portion of council tax from 20% to 40% and permits companies to apply an IRES rate reduced to 15% on profits reinvested in capital assets and in increased personnel expenses for permanent workers.

Resolutions of the Italian Regulatory Authority for Energy, Networks and the Environment

A summary is provided below of the principal resolutions adopted by Italy's Regulatory Authority for Energy, Networks and the Environment (ARERA) during 2018 and, subsequently, up to the date of preparation of this Annual Report.

- **Resolution 44/2018/R/eel:** Adjustments to the payments for volumes accepted in the balancing market in place of the volumes accepted during the planning phase for the ex-ante dispatching services market, in order to supply the secondary reserve service.
- **Resolution 129/2018/R/eel:** Urgent measures regarding output-based incentive mechanisms for transmission services. Changes to the rules governing the recognition of incentives for high-risk projects.
- **Resolution 261/2018/R/eel:** Changes and additions to the criteria and conditions governing capacity payments.
- **Resolution 290/2018/R/eel:** Approval of the proposed division of regional costs for intraday coupling close to Italy's borders pursuant to article 80 of EU Regulation 2015/1222 (CACM).
- **Resolution 292/2018/R/eel:** Audit of contractual compliance by Terna S.p.A. and Gestore dei Mercati Energetici S.p.A. with regard to the launch of intraday coupling.
- **Resolution 338/2018/I/eel:** Revision of the regulator's opinion 701/2016/I/eel granting an exemption for a portion of the "Italy-Montenegro" direct current interconnection.
- **Resolution 363/2018/R/eel:** Downward revision of the charge covering the costs of paying for the load interruptibility service and the charge to cover downward revision of the fee covering the not-recoverable costs incurred by the safeguard operators for the default of non-detachable end users with effect from 1 July 2018.
- **Resolution 383/2018/R/eel:** Approval of the regulation, drawn up by Terna S.p.A. in accordance with the regulator's Resolution 300/2017/R/eel, regarding the pilot project for participation in the dispatching services market (DSM) for relevant production units for which enablement is not obligatory.
- **Resolution 402/2018/R/eel:** Approval of the regulation, drawn up by Terna S.p.A. in accordance with the regulator's Resolution 300/2017/R/eel, regarding the pilot project for provisions of the primary frequency response service via relevant production units integrated with the storage system.
- **Resolution 386/2018/R/eel:** Measures regarding subdivision of the relevant grid into zones, following completion of the review process carried out in accordance with EU Regulation 2015/1222 (CACM).
- **Resolution 422/2018/R/eel:** Approval of the regulation, drawn up by Terna S.p.A. in accordance with the regulator's Resolution 300/2017/R/eel, regarding the pilot project for the participation of mixed virtual units in the dispatching services market (DSM). Amendment of the regulator's Resolution 300/2017/R/eel.

- **Resolution 534/2018/R/eel:** Determinations regarding essential plants. Changes and additions to the related regulations.
- **Resolution 535/2018/R/eel:** Approval of the proposed terms and conditions for balancing, presented pursuant to EU Regulation 2017/2195 (the Balancing Regulation) and assessment of the compliance of the proposed changes to the transmission, dispatching, development and grid security code.
- **Resolution 592/2018/R/eel:** Approval of changes to the transmission, dispatching, development and grid security code drawn up by Terna S.p.A. for the purposes of implementing EU Regulation 2016/631. Addition to the Integrated Text on Active Connections.
- **Resolution 628/2018/R/eel:** launch of the procedure for implementing the regulation governing the exchange of data between Terna S.p.A., electricity distribution companies and significant grid users in order to guarantee the security of the national electricity system.
- **Resolution 668/2018/R/eel:** Financial incentives for initiatives designed to boost the resilience of electricity distribution systems.
- **Resolution 670/2018/R/eel:** Revision of tariffs for provision of the electricity transmission service in 2019 and decisions regarding applications for incentives for specific high-risk projects.
- **Opinion 674/2018/R/eel:** Assessment of the draft 2018 Ten-year Plan for Development of the National Transmission Grid.
- **Resolution 675/2018/R/eel:** Approval of the regulation drawn up by Terna for the provision of resources to be made available for use in voltage regulation in the Brindisi area. Further provisions and pilot projects relating to voltage regulation.
- **Resolution 692/2018/R/eel:** Changes to the regulator's Resolution 627/2016/R/eel and provisions regarding planning for development of the electricity transmission grid.
- **Resolution 698/2018/R/eel:** Determination of the criteria and objectives of output incentive mechanisms for the transmission service in order to build interzonal transmission capacity.
- **Resolution 699/2018/R/eel:** Output incentive mechanisms for projects designed to boost the efficiency of the dispatching service.
- **Resolution 705/2018/R/eel:** Review of dispatching charges for 2019.

Further details of the above resolutions, and information of further resolutions adopted by the regulator (ARERA), can be found on the regulator's website www.arera.it.

Other information

Additional information is presented below in accordance with specific statutory or industry requirements.

Treasury shares

The Parent Company does not directly or indirectly hold any of its own shares or the shares of CDP Reti S.p.A. or Cassa Depositi e Prestiti S.p.A., nor has it purchased or sold any such shares during the reporting period.

Related party transactions

Related party transactions entered into by the Terna Group in 2018 primarily regard services forming part of its ordinary activities and provided under normal market conditions, as described in greater detail in the consolidated financial statements for the year ended 31 December 2018[26].

The Parent Company's Corporate Governance rules ensure that such transactions are conducted in accordance with the rules governing procedural and substantial correctness and on an arm's length basis, and in keeping with the regulations for transparent reporting to the market.

No material transactions[27] were carried out in 2018, nor were any transactions subject to the reporting requirements applicable in the event of exemptions applied in accordance with the relevant regulations[28].

Information on ownership structures

The disclosures required by art. 123-*bis* "Information on ownership structures" of the Consolidated Law on Financial Intermediation (Legislative Decree 58 of 24 February 1998) are provided in a separate document approved by Terna's Board of Directors ("Report on Corporate Governance and Ownership Structures" for 2018, available on Terna S.p.A.'s website (www.terna.it - in the section "Investor Relations").

[26] Relations with members of the Parent Company's Board of Statutory Auditors, with particular regard to their remuneration, are described in the notes to the item, "Services" in the notes to the consolidated and separate financial statements for the year ended 31 December 2017. In addition, in implementation of CONSOB Resolution 18049 of 23 December 2011, disclosures regarding the remuneration of "*members of management and supervisory bodies and general managers*", and their shareholdings in the Company and those of the other persons referred to in the above article, are included in the annual Remuneration Report published in accordance with the law.

[27] These are related party transactions classified in compliance with Annex 3 to the "Regulations on related party transactions" (adopted with CONSOB Resolution 17221 of 12 March 2010, as amended by CONSOB Resolution 17389 of 23 June 2010).

[28] As *"transactions falling within the scope of the ordinary activities of the Company or its subsidiaries or associates or of financing activities related thereto, provided that the transactions are conducted on equivalent to market or standard terms and conditions"*.

Attestations pursuant to article 2.6.2, paragraphs 7 and 8 of the Regulations for the markets organised and managed by Borsa Italiana S.p.A., relating to the conditions described in articles 15 and 16 of the CONSOB's Markets Regulation (no. 20249 of 28 December 2017 in Official Gazette no.1 of 2 January 2018)

With reference to article 36 of the Regulation implementing the provisions of Legislative Decree 58 of 24 February 1998 regarding markets, adopted with Resolution 16191/2007, and the amended provisions of art. 15 of the above new Regulations adopted with CONSOB resolution no. 20249 of 28 December 2017 (the "CONSOB Markets Regulation"), Terna S.p.A. does not hold any significant controlling interests, as defined in the above regulations, in companies incorporated and regulated under the laws of countries not belonging to the European Union.

With regard to the provisions of article 37 of the same CONSOB Markets Regulation, and to the amended provisions of article 16 of the new Regulations mentioned above, Terna S.p.A. is subject to the de facto control of Cassa Depositi e Prestiti S.p.A., exercised through CDP Reti S.p.A. (a joint-stock company controlled by Cassa Depositi e Prestiti S.p.A.), which holds a 29.851% interest in the Parent Company. The checks, providing confirmation of the above situation of control, were conducted by Cassa Depositi e Prestiti and notified to the Company and the CONSOB with effect from 19 April 2007 and, subsequently, by letter dated 30 October 2014 and 2 December 2014. At this time, there are no formal arrangements for the management and coordination of the Company, nor have any such rights been exercised. Terna S.p.A. conducts its business either directly or through its subsidiaries in conditions of operational and contractual independence.

Participation in the regulatory simplification process introduced by CONSOB Resolution 18079 of 20 January 2012

Pursuant to art. 3 of CONSOB Resolution 18079 of 20 January 2012, Terna has elected to adopt the simplified regime provided for in articles 70, paragraph 8, and 71, paragraph 1-bis of CONSOB Regulation 11971 of 14 May 1999, as amended (the CONSOB Regulations for Issuers). As a result, Terna exercises the exemption from disclosure requirements provided for in the above Regulations in respect of transactions of a significant nature involving mergers, spin-offs, capital increases involving contributions in kind, acquisitions and disposals.

Changes

in the dimensions of the NTG

Below are details of changes in the dimensions of the infrastructure available for use and in service with respect to the situation at 31 December 2017.

DETAILS OF ELECTRICITY SUBSTATIONS OWNED BY THE TERNA GROUP*

(AT 31 DECEMBER)	UNIT OF MEASUREMENT	2018	2017	CHANGE	% CHANGE
380 kV					
Substations	no.	164	164	0	0.00
Power transformed	MVA	115,258	114,008	1,250	1.10
220 kV					
Substations	no.	150	150	0	0.00
Power transformed	MVA	31,417	31,317	100	0.32
Lower voltages (≤150 kV)					
Substations	no.	567	557	10	1.80
Power transformed	MVA	3,914	3,890	24	0.62
Total					
Substations	no.	881	871	10	1.15
Power transformed	MVA	150,589	149,215	1,374	0.92

** MVA are calculated to three decimal places and rounded to the nearest whole number. Percentages are calculated to five decimal places and rounded to two decimal places.*

DETAILS OF POWER LINES OWNED BY THE TERNA GROUP*

(AT 31 DECEMBER)		UNIT OF MEASUREMENT	2018	2017	Δ	Δ %
380 kV						
Length of circuits		km	12,496	12,487	9	0.07
Length of lines		km	11,315	11,305	10	0.09
220 kV						
Length of circuits		km	11,915	11,915	(0)	0.00
Length of lines		km	9,549	9,549	1	0.01
Lower voltages (≤150 kV)						
Length of circuits		km	50,031	50,123	(92)	(0.18)
Length of lines		km	46,806	46,852	(46)	(0.10)
Total						
Length of circuits		km	74,442	74,525	(83)	(0.11)
overhead		km	71,043	71,182	(139)	(0.20)
underground cables		km	1,945	1,880	65	3.47
submarine cables		km	1,454	1,463	(9)	(0.61)
Length of circuits		km	67,671	67,706	(35)	(0.05)
overhead		km	64,271	64,363	(91)	(0.14)
underground cables		km	1,945	1,880	65	3.47
submarine cables		km	1,454	1,463	(9)	(0.61)
Incidence of direct current connections (200 - 380 - 500 kV)						
Circuits		km	2,077	2,077		
	% of total	%	2.79	2.79		
Lines		km	1,757	1,757		
	% of total	%	2.60	2.60		

* *Km are calculated to three decimal places and rounded to the nearest whole number. Percentages are calculated to five decimal places.*

PRINCIPAL CHANGES IN THE SIZE OF THE TERNA GROUP'S INFRASTRUCTURE

Substations

New infrastructure:

The following substations have **entered service**:

- switching substation at Santa Teresa di Gallura [SS] (5 150kV bays);
- switching substation at Canino 150 [VT] (3 150kV bays);
- switching substation at San Salvo [CH] (6 132kV bays);
- switching substation at Ravenna Industrial Park [RA] (3 132kV bays);
- transformer substation at La Rosa 2 [LI] (1 132kV bay);

and the following were **acquisitions**:

- switching substation at Bussento [SA] (5 150 kV bays);
- switching substation at Tanagro [SA] (5 150kV bays);
- switching substation at Portella Pero [PA] (4 150kV bays);
- switching substation at Siculiana [PA] (3 150kV bays);

The substation at Stornarella [FG] was also included in the Group's assets and the future Belcastro 380 [CZ] substation was **commissioned in its provisional setup**.

Existing infrastructure:

- **reconstruction in armoured form** of the San Antonio [BZ] substation (6 220kV bays)
- **commissioning** of 18 new line bays for the substations at Villanova (2 380kV bays), Benevento III (1 380kV bay and 2 150kV bays), Cassano 380, Cassano d'Adda and Castelluccia (1 220kV bay each), Vaglio (2 150kV bays), Aprilia 150, Butera, Rumianca and San Severo (1 150kV bay each), BAS Bergamo, Bistagno, Cornegliano and Tavazzano (1 132kV bay each);
- **commissioning** of 10 new machine and/or power factor correction bays in the substations of Redipuglia (1 380kV bay and 1 220kV bay), Benevento III and San Severo (1 380kV bay and 1 150kV bay each), Brindisi Sud and Erchie (1 380kV bay each), Cassano 380 (1 220kV bay), Porto Tolle (1 132kV bay);
- **commissioning** of 1 new 150kV parallel bay at the San Severo substation;
- **demolition and/or decommissioning** of 6 bays at the substations of Benevento II (2 150kV bays), San Rocco (2 132kV bays), Diano Marina (2 66kV bays).

Transformers

The following transformers **entered service**:

- 1 new 380/220kV 600 MVA autotransformer for the Redipuglia substation;
- 1 new 380/150kV 400 MVA autotransformer for the Benevento III substation;
- 1 new 380/150kV 250 MVA autotransformer for the San Severo substation;
- 1 new 380/132kV 250 MVA autotransformer for the Travagliato substation;
- 1 new 220/60kV 100 MVA transformer for the San Antonio substation;
- 1 new 132/15kV 40 MVA transformer for the Savona substation;
- 1 new 132/15kV 16 MVA transformer and the concomitant commissioning of the new La Rosa 2 substation;

and the following **further changes** occurred:

- demolition of 1 380/132kV 300 MVA autotransformer at the Travagliato substation;
- demolition of 1 132/15 kV 32 MVA transformer at the Savona substation;
- replacement of 1 132/66 kV 25 MVA transformer with another identical transformer at the Cuneo RT substation.

Power lines

- **construction** of 10 new lines amounting to a total of 52.0 km of circuit: Villanova - Cepagatti Conversion 1 \ 2 380kV (2 lines amounting to 4.0 km in cable), Gadio - Ricevitrice Ovest 220 kV (6.0 km in cable), Main Naples primary substation - Naples Levante 220kV (3.9 km in cable), Villafranca - Messina Riviera primary substations (new) 150kV (8.9 km of overhead line and 2.7 km in cable), Quartu - Quartucciu 150kV (5.9 km in cable), Tavazzano - Cornegliano 132kV (5.9 km in cable), Malpensata - BAS Bergamo 132kV (3.3 km in cable), cables in the lagoon: Cavallino - Sacca Serenella 132kV (14.2 km in cable) and Fusina 2 - Saccafisola primary substation 132 kV (5.9 km in cable);
- **construction** of 4 short connections between adjacent infrastructure, amounting to 1.4 km of circuit, including: 1 220kV line (0.2 km in cable), 2 150kV lines (0.7 km of overhead line and 0.4 km in cable) and 1 132kV line (0.2 km in cable);
- **acquisition from third parties** of 4 lines amounting to 48.7 km of circuit, including 1 150kV line (18.2 km of overhead line), 2 132kV lines (0.7 km of overhead line), and 1 60kV line (29.8 km of overhead line);
- **construction** of 12 in-out derivations on lines in operation, with an overall increase of the same number of circuits and 13.8 km of circuit, including: 1 line of 2.2 km at 380kV, 6 lines of 10.6 km at 150kV, 5 lines of 1.1 km at 132kV;
- **construction of variants, rigid derivations, re-routings and/or changes to grid distribution** with a total reduction of 3 lines amounting to 83.0 km of circuit, including: 3.2 km more at 380kV, 1 line with 6.9 km less at 220kV, 1 line with 28.4 km less at 150kV, 1 line with 50.9 km less at 132kV, 2 66kV lines less;
- **demolition** of 12 lines and/or parts of lines amounting to 79.2 km of circuit, including: 5.1 km at 220kV, 26.0 km at 150kV, 3.0 km at 132kV, 8.4 km at 60kV, 36.7 km at 50kV;
- **sale to third parties** of a portion of 220kV overhead line amounting to 0.8 km of circuit.

Alternative performance measures (APMs)

In accordance with the guidelines in ESMA/2015/1415, the alternative performance indicators used in this Integrated Report are described below.

MEASURE	DESCRIPTION
OPERATING RESULTS	
Operating profit/(loss) - EBIT	is an indicator of operating performance obtained by adding **Net financial income/(expenses)** to **Profit/(Loss) before tax.**
Gross operating profit/(loss) - EBITDA	is an indicator of operating performance obtained by adding **Amortisation, depreciation and impairment losses to Operating profit/(loss) (EBIT).**
Tax rate	is the amount of tax paid as a proportion of pre-tax profit and is based on the ratio of **Income tax expense to Profit/(Loss) before tax.**
FINANCIAL POSITION	
Net working capital	is an indicator of financial position, showing the entity's liquidity position; it is based on the difference between **Current assets** and **Current liabilities** of a non-financial nature, as presented in the statement of financial position
Gross invested capital	is an indicator of financial position, showing the entity's total assets and is obtained by adding **Net non-current assets** and **Net working capital**.
Net invested capital	is calculated by deducting **Sundry provisions** from **Gross invested capital**
CASH FLOW	
Net debt	is an indicator of the entity's financial structure and is obtained by deducting **Cash and cash equivalents** and **Financial assets from Short- and long-term financial liabilities** and the related **derivative instruments**
Free cash flow	is the cash generated by operating activities less capital expenditure and is the difference between **Cash flow from operating activities** and **Cash flow for investing activities**

Reconciliations

In accordance with the guidelines in ESMA/2015/1415, reconciliations of the reclassified income statement and statement of financial position and of net debt and cash flow of the Terna Group and Terna S.p.A. with the related statutory income statement and statement of financial position are shown below.

RECONCILIATION OF THE TERNA GROUP'S RECLASSIFIED INCOME STATEMENT AND STATEMENT OF FINANCIAL POSITION AND NET DEBT

THE GROUP'S RECLASSIFIED INCOME STATEMENT	€M	CONSOLIDATED INCOME STATEMENT
Regulated revenue in Italy	1,989.6	"Revenue from sales and services", totalling €2,272.5 million, "Other revenue and income", totalling €46.6 million, after the cost of International Activities: "Personnel expenses", totalling €0.6 million, " Raw and consumable materials used", totalling €119.2 million, "Services", totalling €1.2 million, and "Other operating costs" of €1.1 million
Non-Regulated revenue	194.9	
Revenue from International Activities	12.5	
Personnel expenses	238.8	"Personnel expenses" after the cost of construction services performed under concession in Italy in accordance with IFRIC 12 (€4.7 million) and the cost of International Activities (€0.6 million)
Cost of services, leases and rentals	176.5	"Services" after the cost of construction services performed under concession in Italy in accordance with IFRIC 12 (13.5 million) and the cost of International Activities (€1.2 million)
Materials	77.9	"Raw and consumable materials used" after the cost of construction services performed under concession in Italy in accordance with IFRIC 12 (€7.3 million) and the cost of International Activities (€119.2 million)
Other costs	22.6	Other operating costs after the cost of International Activities (€1.1 million)
Quality of service	5.1	
Cost of construction services performed under concession	4.7	"Personnel expenses"
	13.5	"Services"
	7.3	"Raw and consumable materials used"
Net financial income/ (expenses)	(88.8)	Points 1, 2 and 3 of letter C - "Financial income and expenses"

(Continued)

(Continued)

THE GROUP'S RECLASSIFIED STATEMENT OF FINANCIAL POSITION	€M	CONSOLIDATED STATEMENT OF FINANCIAL POSITION
Financial assets	319.9	"Investment accounted for using the equity method", "Other non-current assets" and "Non-current financial assets"
Net energy-related pass-through payables	(777.6)	"Trade receivables" relating to the value of energy-related pass-through receivables (€715 million) and "Trade payables" relating to the value of energy-related pass-through payables (€1,492.6 million)
Net receivables resulting from Regulated Activities	313.9	"Trade receivables" relating to the value of receivables resulting from Regulated Activities (€339.4 million) and "Trade payables" relating to the value of payables resulting from Regulated Activities (€25.5 million)
Net trade payables	(860.7)	"Trade payables" after the value of energy-related pass-through payables (€1,492.6 million) and payables resulting from Regulated Activities (€25.5 million) and "Trade receivables" after the value of energy-related pass-through receivables (€715 million) and the value of receivables resulting from Regulated Activities (€339.4 million)
Net tax assets	50.9	"Tax assets", "Other current assets" relating to the value of other tax assets (€44.1 million), "Other current liabilities" relating to the value of other tax liabilities (€7.4 million) and "Tax liabilities"
Other liabilities, net	(549.0)	"Other non-current liabilities", "Other current liabilities" after other tax liabilities (€7.4 million), "Inventories" and "Other current assets" after other tax assets (€44.1 million)
Sundry provisions	(307.5)	"Employee benefits", "Provisions for risks and charges" and "Deferred tax assets"
Net debt	7,899.4	"Long-term borrowings", "Current portion of long-term borrowings", "Non-current financial liabilities", "Short-term borrowings", "Cash and cash equivalents", "Current financial assets" and "Current financial liabilities"

THE GROUP'S ANALYSIS OF NET DEBT	€M	CONSOLIDATED STATEMENT OF FINANCIAL POSITION
"Bond issues" and "Borrowings"	9,458.2	Corresponds with "Long-term borrowings" and "Current portions of long-term borrowings"
"Derivative financial instruments" - medium/long-term	59.2	Corresponds with "Non-current financial liabilities"
Other current financial liabilities, net	89.8	Corresponds with "Current financial assets" relating to the value of accrued financial income (€0.6 million) and "Current financial liabilities".
Financial assets	(403.9)	Corresponds with "Current financial assets" relating to the value of government securities (€402.6 million) and cash flow hedges (€1.3 million).

RECONCILIATION OF THE TERNA GROUP'S CASH FLOW

(€m)

	CASH FLOW 2018	RECONCILIATION WITH FINANCIAL STATEMENTS	PRO FORMA CASH FLOW 2017	RECONCILIATION WITH FINANCIAL STATEMENTS
- Profit for the year	711.6		694.2	
- Amortisation, depreciation and impairment losses	554.1		526.5	
- Net change in provisions	(48.3)		(28.8)	
Employee benefits		*(11.3)*		*(23.4)*
Provisions for risks and charges		*(25.1)*		*27.9*
Deferred tax assets		*(3.3)*		
Deferred tax liabilities		*(8.6)*		*(33.3)*
- Net losses/(gains) on sale of assets(1)	(3.5)		(2.1)	
Operating cash flow	**1,213.9**		**1,189.8**	
- Change in net working capital:	336.6		408.3	
Inventories		*(0.4)*		*(4.8)*
Trade receivables		*75.5*		*176.0*
Income tax assets		*17.6*		*(17.2)*
Other current assets		*53.1*		*(71.6)*
Trade payables		*16.2*		*217.2*
Tax liabilities		*5.1*		*(8.1)*
Other liabilities		*169.5*		*116.8*
- Other changes in non-current assets	(76.0)		36.1	
Intangible assets(2)		*(9.3)*		-
Property, plant and equipment(3)		*45.3*		*137.5*
Non-current financial assets		*(113.2)*		*(98.3)*
Other non-current assets		*(0.6)*		*(0.4)*
Investments accounted for using the equity method		*1.8*		*(2.7)*
Cash flow from operating activities	**1,474.5**		**1,634.2**	
Capital expenditure				
- Total Capital expenditure	(1,091.1)		(1,033.9)	
Property, plant and equipment(3)		*(1,034.7)*		*(993.8)*
Intangible assets(2)		*(56.4)*		*(40.1)*
Total cash flow from (for) investing activities	**(1,091.1)**		**(1,033.9)**	
Free cash flow	**383.4**		**600.3**	
- Cash flow hedge reserve after taxation and other movements in equity attributable to owners of the Parent(4)	(39.6)		(2.0)	
- Other movements in equity attributable to non-controlling interests	4.3		-	
- Dividends paid to Parent Company's shareholders(4)	(451.1)		(418.4)	
Change in net debt	**(103.0)**		**179.9**	
- Change in borrowings	**(557.3)**		**673.6**	
Non-current financial assets		*4.3*		*325.7*
Current financial assets		*(404.3)*		*26.0*
Non-current financial liabilities		*48.7*		*(2.3)*
Long-term borrowings		*(444.0)*		*267.2*
Short-term borrowings		*(93.0)*		*97.9*
Current portion of long-term borrowings		*346.3*		*(20.2)*
Current financial liabilities		*(15.3)*		*(20.7)*
- Change in cash and cash equivalents	**(660.3)**		**853.5**	

(1) Included in "Other revenue and income" and "Other operating costs" in the consolidated financial statements.
(2) See note 14 to the financial statements.
(3) See note 12 to the financial statements.
(4) See the consolidated statement of changes in equity.

RECONCILIATION OF THE TERNA S.P.A.'S RECLASSIFIED INCOME STATEMENT AND STATEMENT OF FINANCIAL POSITION AND NET DEBT

TERNA'S RECLASSIFIED INCOME STATEMENT	€M	INCOME STATEMENT
Tariff revenue	1,800.6	"Revenue from sales and services"
Revenue from construction services performed under concession	25.5	"Revenue from sales and services"
Other operating income	141.5	"Revenue from sales and services", totalling €66.8 million, and "Other revenue and income"
Personnel expenses	63.6	"Personnel expenses" after the cost of construction services performed under concession in accordance with IFRIC 12 (€0.3 million)
Cost of services. leases and rentals	343.8	"Services" after the cost of construction services performed under concession in accordance with IFRIC 12 (€20.8 million)
Materials	0.9	"Raw and consumable materials used" after the cost of construction services performed under concession in accordance with IFRIC 12 (€4.4 million)
Other costs	13.1	Other operating costs
Quality of service	5.1	
Cost of construction services performed under concession	0.3	"Personnel expenses"
	20.8	"Services"
	4.4	"Raw and consumable materials used"
Net financial income/ (expenses)	(78.5)	Points 1 and 2 of letter C - "Financial income and expenses"

TERNA'S RECLASSIFIED STATEMENT OF FINANCIAL POSITION	€M	STATEMENT OF FINANCIAL POSITION
Financial assets	1,085.4	"Non-current financial assets" after loans to subsidiaries (€10 million) and "Other non-current assets"
Net energy-related pass-through payables	(799.7)	"Trade receivables" relating to the value of energy-related pass-through receivables (€715 million) and "Trade payables" relating to the value of energy-related pass-through payables (€1,514.7 million)
Net receivables resulting from Regulated Activities	313.9	"Trade receivables" relating to the value of receivables resulting from Regulated Activities (€339.4 million) and "Trade payables" relating to the value of payables resulting from Regulated Activities (€25.5 million)
Net trade payables	(537.6)	"Trade payables" after the value of energy-related pass-through payables (€1,514.7 million) and payables resulting from Regulated Activities (€25.5 million) and "Trade receivables" after the value of energy-related pass-through receivables (€715 million) and the value of receivables resulting from regulated activities (€339.4 million))
Net tax assets	(14.2)	"Tax assets", "Other current assets" relating to the value of other tax assets (€4.8 million), "Other current liabilities" relating to the value of other tax liabilities (€26.9 million) and "Tax liabilities"
Other liabilities, net	(350.4)	"Other non-current liabilities", "Other current liabilities" after other tax liabilities (€26.9 million), "Inventories" and "Other current assets" after other tax assets (€4.8 million)
Sundry provisions	(207.4)	"Employee benefits", "Provisions for risks and charges" and "Deferred tax assets"
Net debt	8,101.8	"Long-term borrowings", "Current portion of long-term borrowings", "Non-current financial liabilities", "Short-term borrowings", "Cash and cash equivalents", "Non-current financial assets" relating to the value of loans to subsidiaries (€10 million), "Current financial assets" and "Current financial liabilities"

TERNA'S ANALYSIS OF NET DEBT	€M	STATEMENT OF FINANCIAL POSITION
"Bond issues" and "Borrowings"	9,401.7	Corresponds with "Long-term borrowings" and "Current portions of long-term borrowings"
"Derivative financial instruments"	59.1	Corresponds with "Non-current financial liabilities"
"Short-term borrowings and other financial liabilities"	89.5	Corresponds with "Short-term borrowings", "Current financial liabilities" and "Current financial assets" relating to the value of accrued financial income (€0.6 million)
"Cash and cash equivalents (including the net balance on intercompany current accounts)"	(945.1)	Corresponds with "Cash and cash equivalents"
"Long- and short-term loans to subsidiaries"	(99.5)	Corresponds with "Non-current financial assets", totalling €10 million, and "Current financial assets", totalling €89.5 million
"Financial assets"	(403.9)	Corresponds with "Current financial assets" relating to the value of government securities (€402.6 million) and cash flow hedges (€1.3 million).

RECONCILIATION OF THE TERNA S.P.A.'S CASH FLOW

(€m)

	CASH FLOW 2018	RECONCILIATION WITH FINANCIAL STATEMENTS	PRO FORMA CASH FLOW FY2017	RECONCILIATION WITH FINANCIAL STATEMENTS
- Profit for the year	661.3		640.0	
- Amortisation, depreciation and impairment losses	517.9		495.2	
- Net change in provisions	(66.1)		(18.5)	
Employee benefits		*(0.9)*		*(17.0)*
Provisions for risks and charges		*(29.7)*		*29.8*
Deferred tax assets		*(18.2)*		
Deferred tax liabilities		*(17.3)*		*(31.3)*
- Net losses/(gains) on sale of assets(1)	(3.0)		(1.7)	
Operating cash flow	**1,110.1**		**1,115.0**	
- Change in net working capital:	243.0		287.3	
Inventories		*5.3*		*(5.4)*
Trade receivables		*51.9*		*231.6*
Income tax assets		*41.9*		*(43.8)*
Other current assets		*42.7*		*(20.7)*
Trade payables		*7.0*		*143.8*
Tax liabilities		*8.1*		*(5.3)*
Other liabilities		*86.1*		*(12.9)*
- Other changes in non-current assets	(36.6)		65.3	
Property. plant and equipment(2)		36.8		120.1
Intangible assets(3)		1.9		
Non-current financial assets		(74.6)		(54.8)
Other non-current assets		(0.7)		-
Cash flow from operating activities	**1,316.5**		**1,467.6**	
Capital expenditure				
- Total Capital expenditure	(886.1)		(851.9)	
Property, plant and equipment(2)		(834.3)		(813.4)
Intangible assets(3)		(51.8)		(38.5)
Total cash flow from (for) investing activities	**(886.1)**		**(851.9)**	
Free cash flow	**430.4**		**615.7**	
- Dividends(4)	(451.1)		(418.4)	
- Cash flow hedge reserve after taxation and other movements in equity(4)	(34.6)		5.9	
Change in net debt	**(55.3)**		**203.2**	
- Change in borrowings	(677.8)		673.2	
Current financial assets		*(492.5)*		*65.1*
Non-current financial assets		*(6.8)*		*326.8*
Non-current financial liabilities		*47.9*		*(2.8)*
Long-term borrowings		*(466.6)*		*234.8*
Short-term borrowings		*(90.0)*		*90.0*
Current portion of long-term borrowings		*345.8*		*(20.0)*
Current financial liabilities		*(15.6)*		*(20.7)*
- Change in cash and cash equivalents	(733.1)		876.4	

(1) Included in "Other revenue" and "Other operating costs" in the financial statements.
(2) See note 10 to the financial statements.
(3) See note 12 to the financial statements.
(4) See the statement of changes in equity.

CONSOLIDATED FINANCIAL STATEMENTS

Contents

Consolidated financial statements

Consolidated income statement

(€m)

	NOTE	2018	2017
A – REVENUE			
1. Revenue from sales and services	1	2,272.5	2,184.0
of which: related parties		*1,603.6*	*1,593.3*
2. Other revenue and income	2	46.6	64.0
of which: related parties		*16.1*	*6.7*
Total revenue		**2,319.1**	**2,248.0**
B – OPERATING COSTS			
1. Raw and consumable materials used	3	204.4	158.1
of which: related parties		*0.2*	*0.1*
2. Services	4	191.2	182.4
of which: related parties		*19.7*	*25.7*
3. Personnel expenses	5	244.1	257.2
- gross personnel expenses		*312.3*	*321.0*
- capitalised personnel expenses		*(68.2)*	*(63.8)*
of which: related parties		*2.9*	*2.6*
4. Amortisation. depreciation and impairment losses	6	554.1	526.5
5. Other operating costs	7	28.8	46.4
of which: related parties		*0.1*	*0.2*
Total costs		**1,222.6**	**1,170.6**
A - B OPERATING PROFIT/(LOSS)		**1,096.5**	**1,077.4**
C – FINANCIAL INCOME/(EXPENSES)			
1. Financial income	8	6.9	3.9
2. Financial expenses	8	(98.3)	(96.5)
of which: related parties		*(3.1)*	*(3.8)*
3. Share of profit/(loss) of investees accounted for using the equity method	9	2.6	3.8
D – PROFIT/(LOSS) BEFORE TAX		**1,007.7**	**988.6**
E – INCOME TAX EXPENSE	**10**	**296.1**	**294.4**
F – PROFIT FOR THE YEAR		**711.6**	**694.2**
Profit attributable to owners of the Parent		***706.6***	***688.3***
Profit attributable to non-controlling interests		***5.0***	***5.9***
Earnings per share	**11**		
Basic earnings per share		0.352	0.342
Diluted earnings per share		0.352	0.342

Consolidated statement of comprehensive income

(€m)

	NOTE	2018	2017
PROFIT FOR THE YEAR		**711.6**	**694.2**
Other comprehensive income for the year reclassifiable to profit or loss			
- Cash flow hedges, after taxation	23	(32.1)	5.5
- Financial assets at fair value through other comprehensive income, after taxation	23	1.1	
- Gains/(Losses) from translation of financial statements in currencies other than the euro	23	(4.8)	(6.9)
- Cost of hedges, after taxation	23	(1.8)	-
Other comprehensive income for the year not reclassifiable to profit or loss			
- Actuarial gains/(losses) on provisions for employee benefits, after taxation	23	0.9	(0.4)
COMPREHENSIVE INCOME FOR THE YEAR		**674.9**	**692.4**
COMPREHENSIVE INCOME FOR THE YEAR ATTRIBUTABLE TO:			
Owners of the Parent		*669.9*	*686.5*
Non-controlling interests		*5.0*	*5.9*

Consolidated statement of financial position

(€m)

	NOTE	31 DECEMBER 2018	31 DECEMBER 2017
A – NON-CURRENT ASSETS			
1. Property, plant and equipment	12	13.244,3	12.752,8
of which: related parties		*40.9*	*26,2*
2. Goodwill	13	230,1	230,1
3. Intangible assets	14	289,3	275,6
4. Deferred tax assets	15	3,3	-
5. Investments accounted for using the equity method	16	76,1	77,9
6. Non-current financial assets	17	229,0	120,1
of which: related parties		-	*0,3*
7. Other non-current assets	18	14,8	14,2
Total non-current assets		**14.086,9**	**13.470,7**
B – CURRENT ASSETS			
1. Inventories	19	15,2	14,8
2. Trade receivables	20	1.189,7	1.265,9
of which: related parties		*409,7*	*407,1*
3. Current financial assets	17	404,5	0,2
4. Cash and cash equivalents	21	1.328,9	1.989,2
of which: related parties		*0,1*	*0,1*
5. Income tax assets	22	19,3	36,9
6. Other current assets	18	86,0	139,1
of which: related parties		*3,3*	-
Total current assets		**3.043,6**	**3.446,1**
TOTAL ASSETS		**17.130,5**	**16.916,8**

(continues)

(continued)

(€m)

	NOTE	31 DECEMBER 2018	31 DECEMBER 2017
C – EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT			
1. Share capital		442.2	442.2
2. Other reserves		788.5	820.4
3. Retained earnings/(accumulated losses)		2,240.1	2,001.7
4. Interim dividend		(158.2)	(149.3)
5. Profit for the year		706.6	688.3
Total equity attributable to owners of the Parent	**23**	**4,019.2**	**3,803.3**
D – EQUITY ATTRIBUTABLE TO NON-CONTROLLING INTERESTS	**23**	**35.0**	**25.7**
Total equity attributable to owners of the Parent and non-controlling interests		**4,054.2**	**3,829.0**
E – NON-CURRENT LIABILITIES			
1. Long-term borrowings	24	8,227.6	8,671.6
of which: related parties		-	*500.0*
2. Employee benefits	25	69.4	80.7
3. Provisions for risks and charges	26	241.4	266.5
4. Deferred tax liabilities	15	-	8.6
5. Non-current financial liabilities	24	59.2	10.5
6. Other non-current liabilities	27	373.8	251.0
Total non-current liabilities		**8,971.4**	**9,288.9**
F – CURRENT LIABILITIES			
1. Short-term borrowings	24	25.0	118.0
2. Current portion of long-term borrowings	24	1,230.6	884.3
of which: related parties		*500.0*	-
3. Trade payables	28	2,514.1	2,497.9
of which: related parties		*66.7*	*46.1*
4. Tax expense	28	5.1	-
5. Current financial liabilities	24	90.4	105.7
of which: related parties		*0.5*	*0.5*
6. Other current liabilities	28	239.7	193.0
of which: related parties		*14.7*	*5.6*
Total current liabilities		**4,104.9**	**3,798.9**
TOTAL LIABILITIES AND EQUITY		**17,130.5**	**16,916.8**

Consolidated statement of changes in equity

31 DECEMBER 2017 - 31 DECEMBER 2018
GROUP'S SHARE CAPITAL AND RESERVES

	SHARE CAPITAL	LEGAL RESERVE	SHARE PREMIUM RESERVE	CASH FLOW HEDGE RESERVE
EQUITY AT 31 DECEMBER 2017	442.2	88.4	20.0	(12.7)
Change in accounting standards	-	-	-	-
RESTATED EQUITY AT 1 JANUARY 2018	442.2	88.4	20.0	(12.7)
PROFIT FOR THE YEAR				
OTHER COMPREHENSIVE INCOME:				
- Change in fair value of cash flow hedges, after taxation				(32.1)
- Actuarial gains/(losses) on employee benefits, after taxation				
- Gains/(Losses) from translation of financial statements in currencies other than the euro				
- Financial assets at fair value through other comprehensive income, after taxation				
- Cost of hedges, after taxation				(1.8)
Total other comprehensive income	-	-	-	(33.9)
COMPREHENSIVE INCOME	-	-	-	(33.9)
TRANSACTIONS WITH SHAREHOLDERS:				
- Appropriation of profit for 2017:				
Retained earnings				
Dividends				
- Interim dividend 2018				
Total transactions with shareholders	-	-	-	-
Contribution of newly acquired companies				
Other changes				
Total other changes	-	-	-	-
EQUITY AT 31 DECEMBER 2018	442.2	88.4	20.0	(46.6)

31 DECEMBER 2016 - 31 DECEMBER 2017
GROUP'S SHARE CAPITAL AND RESERVES

	SHARE CAPITAL	LEGAL RESERVE	SHARE PREMIUM RESERVE	CASH FLOW HEDGE RESERVE
EQUITY AT 31 DECEMBER 2016	442.2	88.4	20.0	(18.2)
PROFIT FOR THE YEAR				
OTHER COMPREHENSIVE INCOME:				
- Change in fair value of cash flow hedges, after taxation				5.5
- Actuarial gains/(losses) on employee benefits, after taxation				
- Gains/(Losses) from translation of financial statements in currencies other than the euro				
Total other comprehensive income	-	-	-	5.5
COMPREHENSIVE INCOME	-	-	-	5.5
TRANSACTIONS WITH SHAREHOLDERS:				
- Appropriation of profit for 2016:				
Retained earnings				
Dividends				
- Interim dividend 2017				
Total transactions with shareholders	-	-	-	-
Other changes				
Total other changes	-	-	-	-
EQUITY AT 31 DECEMBER 2017	442.2	88.4	20.0	(12.7)

(€m)

OTHER RESERVES	RETAINED EARNINGS/ (ACCUMULATED LOSSES)	INTERIM DIVIDEND	PROFIT FOR THE YEAR	EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT	EQUITY ATTRIBUTABLE TO NON-CONTROLLING INTERESTS	EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT AND NON-CONTROLLING INTERESTS
724.7	2,001.7	(149.3)	688.3	3,803.3	25.7	3,829.0
	(3.0)	-	-	(3.0)	(0.6)	(3.6)
724.7	1,998.7	(149.3)	688.3	3,800.3	25.1	3,825.4
			706.6	706.6	5.0	711.6
				(32.1)		(32.1)
0.9				0.9		0.9
	(4.8)			(4.8)		(4.8)
1.1				1.1		1.1
				(1.8)		(1.8)
2.0	(4.8)	-	-	(36.7)	-	(36.7)
2.0	(4.8)	-	706.6	669.9	5.0	674.9
	246.1		*(246.1)*	-		-
	-	*149.3*	*(442.2)*	*(292.9)*		*(292.9)*
		(158.2)		(158.2)		(158.2)
-	246.1	(8.9)	(688.3)	(451.1)	-	(451.1)
					4.9	4.9
	0.1			0.1		0.1
-	0.1	-	-	0.1	4.9	5.0
726.7	2,240.1	(158.2)	706.6	4,019.2	35.0	4,054.2

(€m)

OTHER RESERVES	RETAINED EARNINGS/ (ACCUMULATED LOSSES)	INTERIM DIVIDEND	PROFIT FOR THE YEAR	EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT	EQUITY ATTRIBUTABLE TO NON-CONTROLLING INTERESTS	EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT AND NON-CONTROLLING INTERESTS
725.1	1,789.7	(144.9)	633.1	3,535.4	19.8	3,555.2
			688.3	688.3	5.9	694.2
				5.5		5.5
(0.4)				(0.4)		(0.4)
	(6.9)			(6.9)		(6.9)
(0.4)	(6.9)	-	-	(1.8)	-	(1.8)
(0.4)	(6.9)	-	688.3	686.5	5.9	692.4
	219.1		*(219.1)*	-		
		144.9	*(414.0)*	*(269.1)*		*(269.1)*
		(149.3)		(149.3)		(149.3)
-	219.1	(4.4)	(633.1)	(418.4)	-	(418.4)
	(0.2)			(0.2)		(0.2)
-	(0.2)	-	-	(0.2)	-	(0.2)
724.7	2,001.7	(149.3)	688.3	3,803.3	25.7	3,829.0

Consolidated statement of cash flows

(€m)

	2018	2017
PROFIT FOR THE YEAR	**711.6**	**694.2**
ADJUSTED BY:		
Amortisation, depreciation and impairment losses /(reversals of impairment losses) on non-current property, plant and equipment and intangible assets *	545.0	516.4
Accruals to provisions (including provisions for employee benefits) and impairment losses	43.2	74.1
(Gains)/Losses on sale of property, plant and equipment	(3.5)	(2.1)
Financial (income)/expense	91.5	82.8
Income tax expense	296.1	294.4
CASH FLOW FROM OPERATING ACTIVITIES BEFORE CHANGES IN NET WORKING CAPITAL	**1,683.9**	**1,659.8**
Increase/(decrease) in provisions (including provisions for employee benefits and taxation)	(54.5)	(69.2)
(Increase)/decrease in inventories	(0.4)	(4.8)
(Increase)/decrease in trade receivables and other current assets	129.2	89.7
Increase/(decrease) in trade payables and other current liabilities	62.7	200.2
Increase/(decrease) in other non-current liabilities	128.0	135.2
(Increase)/decrease in other non-current assets	(115.0)	(98.7)
Interest income and other financial income received	5.0	352.0
Interest expense and other financial expenses paid	(230.0)	(228.7)
Income tax paid	(302.3)	(343.8)
CASH FLOW FROM OPERATING ACTIVITIES [A]	**1,306.6**	**1,691.7**
- of which: related parties	*24.1*	*(138.0)*
Investments in non-current property. plant and equipment after grants received	(992.5)	(864.9)
Revenue from sale of non-current property, plant and equipment and intangible assets and other movements	12.7	9.4
Capitalised financial expenses	15.1	12.8
Investments in non-current intangible assets after grants received	(56.4)	(40.1)
Recognition of intangible assets and property, plant and equipment from new acquisitions	(17.6)	-
(Increase)/decrease in investments in associates	1.8	(2.7)
CASH FLOW FOR INVESTING ACTIVITIES [B]	**(1,036.9)**	**(885.5)**
- of which: related parties	*(14.7)*	*9.6*
Increase/(decrease) in retained earnings and accumulated losses	(2.9)	-
Dividends paid	(451.1)	(418.4)
Movements in short- and medium/long-term financial liabilities (including short-term portion)**	(78.8)	465.7
Movements in short-term financial investments	(401.5)	-
Recognition of non-controlling interests in equity of newly acquired companies	4.9	-
Increase/(decrease) in equity attributable to non-controlling interests	(0.6)	-
CASH FLOW FROM FINANCING ACTIVITIES [C]	**(930.0)**	**47.3**
INCREASE/(DECREASE) IN CASH AND EQUIVALENTS [A+B+C]	**(660.3)**	**853.5**
Cash and cash equivalents at beginning of year	1,989.2	1,135.7
Cash and cash equivalents at end of year	1,328.9	1,989.2

* *After grants related to assets recognised in the income statement for the year.*
** *After derivatives and impact of fair value adjustments.*

Notes

A. Accounting policies and measurement criteria

Introduction

Terna S.p.A.'s registered office is at Viale Egidio Galbani 70, Rome, Italy. The consolidated financial statements at and for the year ended 31 December 2018 include the Company's financial statements and those of its subsidiaries (the "Group"). The subsidiaries included within the scope of consolidation are listed below.
These consolidated financial statements were authorised for publication by the Board of Directors on 20 March 2019.
The consolidated financial statements at and for the year ended 31 December 2018 are available for inspection on request at Terna S.p.A.'s registered office at Viale Egidio Galbani 70, Rome, or on the Company's website at www.terna.it.
The Board of Directors has also authorised the Chairwoman and the Chief Executive Officer to make any alterations to the form of the consolidated financial statements and any additions and adjustments to the sections concerning significant subsequent events.

The Terna Group is the largest independent transmission system operator in Europe and one of the leading operators in the world in terms of kilometres of line managed (more than 72 thousand km).
It is responsible for the transmission and management of power flows on the high-voltage (HV) and very high-voltage (VHV) grid throughout Italy, in order to guarantee a balance between demand and supply for energy (dispatching). It is also responsible for the planning, construction and maintenance of the grid. It acts as the Italian TSO (Transmission System Operator), having been granted a monopoly under a government concession, and is subject to regulation by Italy's Regulatory Authority for Energy, Networks and the Environment (ARERA) and the guidelines established by the Ministry for Economic Development. It ensures the security, quality and cost-effectiveness of the national electricity system and has the task of developing the grid and integrating it with the European grid. It ensures equal access for all grid users.

Compliance with IAS/IFRS

The consolidated financial statements at and for the year ended 31 December 2018 have been prepared in accordance with International Financial Reporting Standards (IFRS), International Accounting Standards (IAS) issued by the International Accounting Standards Board (IASB) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and the Standing Interpretations Committee (SIC), as endorsed by the European Commission ("EU-IFRS").

This document has also been prepared taking into account the provisions of Legislative Decree 38 of 28 February 2005, of the Italian Civil Code and CONSOB Resolutions 15519 ("Provisions governing financial statements in implementation of art. 9, paragraph 3 of Legislative Decree 38/2005") and 15520 ("Amendments to the implementing rules for Legislative Decree 58/1998"), as well as CONSOB Communication DEM/6064293 ("Disclosure requirements for listed issuers and issuers of financial instruments that are widely held among the public pursuant to art. 116 of the Consolidated Law on Finance").

Basis of presentation

The consolidated financial statements consist of the statement of financial position, the income statement, the statement of comprehensive income, the statement of cash flows, the statement of changes in equity and the notes thereto.

In the statement of financial position, assets and liabilities are classified on a "current/non-current" basis, with separate reporting of assets and liabilities held for sale. Current assets, which include cash and cash equivalents, are those held for realisation, sale or consumption in the Group's normal operating cycle; current liabilities are those expected to be settled in the Group's normal operating cycle or within one year of the end of the financial year.
The income statement is classified on the basis of the nature of costs. The income statement is presented as two statements, the first of which (the income statement) presents revenue and expense items for the year; the second (the statement of comprehensive income) starts with the result for the year and then presents the revenue and expense items (including reclassification adjustments) that are recognised in equity rather than profit or loss for the year.
The statement of cash flows has been prepared using the indirect method.
The consolidated financial statements are accompanied by the Integrated Report for Terna S.p.A. and the Group, which as from financial year 2008 has been prepared as a single document, exercising the option granted by Legislative Decree 32 of 2 February 2007, which amended art. 40 (Integrated Report) of Legislative Decree 127 of 9 April 1991.
These consolidated financial statements are presented in millions of euros, and all amounts are shown in millions of euros, unless otherwise indicated.
It should be noted that, for the purposes of comparison, certain amounts in the financial statements for the year ended 31 December 2017 have been restated, without, however, altering amounts in equity at 31 December 2017 or those in the income statement and the statement of comprehensive income for 2017.

Use of estimates

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

Impairment losses

Property, plant and equipment and intangible assets with finite useful lives are tested at least once a year to check for evidence of impairment. If there is evidence that an asset may be impaired, its recoverable amount is estimated.
The recoverable amount of goodwill and intangible assets with indefinite useful lives, where present, as well as intangible assets not yet available for use, is estimated at least annually. The recoverable amount is equal

to the greater of the fair value less costs to sell and value in use. Value in use is measured by discounting estimated future cash flows considering information available at the time of estimate and on the basis of estimates of the performance of future variables, such as prices, costs, demand growth rates, production profiles, and discounted at a pre-tax rate that reflects current market assessments of the time value of money for the investment period and risks specific to the asset. If the intangible asset does not generate cash inflows, the asset's recoverable amount is calculated as part of the Cash Generating Unit ("CGU") to which it belongs.
An impairment loss is recognised in the income statement when the asset's carrying amount, or the net invested capital of the CGU to which it belongs, is greater than its recoverable amount.
Impairment losses on CGUs are first taken as a reduction in the carrying amount of any allocated goodwill and then as a reduction in other assets allocated to the CGU on a pro rata basis. Except for goodwill, impairment losses may be reversed up to the recoverable amount or the original cost of the asset if there is an indication that the impairment loss no longer exists or when there is a change in the methods used to measure the recoverable amount.

Allowance for doubtful accounts

Trade receivables are initially recognised at fair value net of any losses relating to sums considered non-recoverable, for which specific provisions have been made in the allowance for doubtful accounts. The new accounting standard, IFRS 9, adopted from 1 January 2018, has introduced the application of a model based on expected credit losses. This requires the Group to assess expected credit losses, and the related changes, at each reporting date, superseding the approach used in IAS 39. It is, therefore, no longer necessary for a trigger event to occur before the recognition of losses on receivables.
Specifically, the Group has applied the simplified approach permitted by IFRS 9 to trade receivables, finance lease receivables and assets deriving from contracts with customers, in order to measure the allowance for doubtful accounts based on expected losses over the life of the receivable. The Group has thus determined the amount of expected credit losses using a provisioning matrix, based on information regarding historical credit losses for similar past due exposures, adjusted to take into account current conditions and forward-looking elements.

Provisions for risks and charges

Provisions for risks and charges are allocated when a disbursement of cash, for an amount which can be reliably estimated, will be necessary to fulfil a legal or constructive obligation arising as a result of a past event. Where the time value of money is significant, provisions are discounted, using a rate that the Group believes to be appropriate (a rate is used that reflects current market conditions and the specific risks connected with the liability). After initial recognition, the value of the provisions for risks and charges is updated to reflect the passage of time and any changes in the estimate following alterations to the amounts forecast, the timing and the discount rates used. Any increase in provisions associated with the passage of time is recognised in the income statement under "Financial expenses".
Liabilities that can be associated with legal and tax disputes and liabilities associated with urban and environmental restoration projects are estimated by the Group. The measurement of provisions for legal disputes is based on the probability of incurring an expense, including through the use of external legal advisors supporting the Group companies; the estimate of provisions to be set aside for urban and environmental restoration projects, the "offsets" aimed at compensating for the environmental impact of the construction of new plant, is based on an analysis of the agreements entered into with the local authorities concerned and the progress of work on construction of the new plant.

Employee benefits

The liability for employee benefits paid upon or following termination of employment in relation to defined benefit plans or other long-term benefits is recognised net of any plan assets and is measured on the basis of actuarial assumptions, estimating the amount of future benefits that employees have vested at the reporting date. The actuarial valuations used to quantify employee benefits (of all plans except termination benefits [*TFR - Trattamento di Fine Rapporto*]) were based on "vested benefits", applying the projected unit credit method. These valuations are based on economic and demographic assumptions: the discount rate (used to determine the current value of the obligation, determined considering returns on high quality bonds in line with the duration of the group of workers measured), the inflation rate, the rate at which future salary levels are expected to rise, the rate of increase for average health reimbursements, rate of increase for electricity prices and demographic factors, such as mortality and invalidity, retirement, resignation, advances and household composition.

Subsidiaries and scope of consolidation

The scope of consolidation includes the Parent Company, Terna S.p.A., and the companies over which it has the power to directly or indirectly exercise control. Control exists when the Parent Company has the power or the ability to influence the relevant activities (having a substantial impact on the Parent Company's results), and is exposed to or has the right to variable returns from its involvement with the investee, and the ability to use its power over the subsidiaries to affect the amount of the investor's returns. The financial statements of subsidiaries are consolidated on a line-by-line basis from the date when the Parent Company gains control until the date when such control ceases. The companies included within the scope of consolidation are listed below:

NAME	REGISTERED OFFICE	CURRENCY	SHARE CAPITAL	% INTEREST	METHOD OF CONSOLIDATION
SUBSIDIARIES CONTROILLED DIRECTLY BY TERNA S.P.A.					
Terna Rete Italia S.p.A.	Rome	Euro	120,000	100%	Line-by-line
Business	Design, construction, management, development, operation and maintenance of power lines and grid infrastructure and other grid-related infrastructure, plant and equipment used in the above electricity transmission and dispatching activities and in similar, related and connected sectors.				
Terna Crna Gora d.o.o.	Podgorica (Montenegro)	Euro	173,000,000	100%	Line-by-line
Business	Authorisation, construction and operation of the transmission infrastructure forming the Italy-Montenegro interconnector on Montenegrin territory.				
Terna Plus S.r.l.	Rome	Euro	16,050,000	100%	Line-by-line
Business	Design, construction, management, development, operation and maintenance of plant, equipment and infrastructure for grids and systems, including distributed storage and pumping and/or storage systems.				
Terna Interconnector S.r.l.	Rome	Euro	10,000	65%*	Line-by-line
Business	Responsible for construction and operation of the private section of the Italy-France interconnector and civil works on the public section.				
Monita Interconnector S.r.l.	Rome	Euro	10,000	95%**	Line-by-line
Business	Responsible for construction and operation of the private section of the Italy-Montenegro interconnector.				
Rete S.r.l.	Rome	Euro	387,267,082	100%	Line-by-line
Business	Design, construction, management, development, operation and maintenance of high-voltage power lines.				
Difebal S.A.	Montevideo (Uruguay)	Uruguayan peso	140,000	100%	Line-by-line
Business	Design, construction and maintenance of electricity infrastructure in Uruguay.				
Terna Energy Solutions S.r.l.	Rome	Euro	2,000,000	100%	Line-by-line
Business	Design, construction, management, development, operation and maintenance of distributed energy storage systems, pumping and/or storage systems, plant, equipment and infrastructure, including grids; research, consultancy and assistance in matters relating to the core business; any other activity capable of improving the use and development of plant, resources and expertise.				
Resia Interconnector S.r.l.	Rome	Euro	10,000	100%	Line-by-line
Business	Design, construction, management, development, operation and maintenance, including on behalf of third parties, of power lines and grid infrastructure and other infrastructure connected to such grids, plant and equipment for use in electricity transmission operations, or in similar, related or connected sectors, and has been established to fulfil the obligations assumed by the energy-intensive companies in relation to implementation of the interconnection with Austria.				

* *5% is held by Terna Rete Italia S.p.A. and 30% by Transenergia S.r.l..*
** *5% is held by Terna Rete Italia S.p.A..*

NAME	REGISTERED OFFICE	CURRENCY	SHARE CAPITAL	% INTEREST	METHOD OF CONSOLIDATION
SUBSIDIARIES CONTROLLED THROUGH TERNA PLUS S.r.l.					
Terna Chile S.p.A.	Santiago (Chile)	Chilean peso	1,000,000	100%	Line-by-line
Business	Design, construction, administration, development, operation and maintenance of any type of electricity system, plant, equipment and infrastructure, including interconnectors; provision of all types of product and service, construction, electrical and civil engineering work; research, consultancy and assistance in matters relating to the core business; any other activity capable of improving the use and development of plant, resources and expertise.				
SPE Santa Maria Transmissora de Energia S.A.	San Paolo (Brazil)	Real	45,474,716	99.99%*	Line-by-line
Business	Provision of public electricity transmission services, including construction, operation and maintenance of transmission infrastructure or any other activity necessary in order to fulfil the above purpose.				
SPE Santa Lucia Transmissora de Energia S.A.	San Paolo (Brazil)	Real	208,714,431	99.99%*	Line-by-line
Business	Provision of public electricity transmission services, including construction, operation and maintenance of electricity transmission infrastructure or any other activity necessary in order to fulfil the above purpose.				
Terna Peru S.A.C.	Lima (Peru)	Sales	28,191,000	99.99%*	Line-by-line
Business	Design, construction, administration, development, operation and maintenance of any type of electricity system, plant, equipment and infrastructure, including interconnectors; provision of all types of product and service, construction, electrical and civil engineering work; research, consultancy and assistance in matters relating to the core business; any other activity capable of improving the use and development of plant, resources and expertise.				

** 0.01% Terna Chile S.p.A.*

NAME	REGISTERED OFFICE	CURRENCY	SHARE CAPITAL	% INTEREST	METHOD OF CONSOLIDATION
SUBSIDIARIES CONTROLLED THROUGH TERNA ENERGY SOLUTIONS S.R.L.					
Tamini Trasformatori S.r.l.	Melegnano (MI)	Euro	4,285,714	70%*	Line-by-line
Business	Construction, repair and trading in electrical equipment.				
Rete Verde 17 S.r.l.	Rome	Euro	10,000	100%	Line-by-line
Business	Implementation and development of renewable energy projects.				
Rete Verde 18 S.r.l.	Rome	Euro	10,000	100%	Line-by-line
Business	Implementation and development of renewable energy projects.				
Rete Verde 19 S.r.l.	Rome	Euro	10,000	100%	Line-by-line
Business	Implementation and development of renewable energy projects.				
Rete Verde 20 S.r.l.	Rome	Euro	10,000	100%	Line-by-line
Business	Implementation and development of renewable energy projects.				
Avvenia The Energy Innovator S.r.l.	Rome	Euro	10,000	70%**	Line-by-line
Business	Provision of energy efficiency, energy consulting and process engineering services to companies and public and private entities; the application of technology to increase energy end-use efficiency; the design, construction, development and maintenance of plant, equipment and infrastructure for networks and other uses.				
SUBSIDIARIES CONTROLLED THROUGH TAMINI TRASFORMATORI S.R.L.					
Tamini Transformers USA LLC	Sewickley - Pennsylvania	US dollar	52,089	100%	Line-by-line
Business	Commercialisation of industrial-grade and high-power electricity transformers.				
Tamini Trasformatori India Private Limited	Maharashtra (India)	Indian rupee	13,175,000	100%	Line-by-line
Business	Commercialisation of industrial-grade and high-power electricity transformers.				

* *30% Holdco TES (controlled by the Xenon Private Equity V fund, Riccardo Reboldi and Giorgio Gussago).*
** *30% Avvenia S.r.l..*

The following changes in the structure of the Group have taken place with respect to 31 December 2017:

- as part of the process of identifying and acting on new commercial opportunities for the provision of energy efficiency services and projects, on 15 February 2018, Terna completed the acquisition of a 70% interest in Avvenia The Energy Innovator S.r.l.;
- on 16 July 2018, Resia Interconnector S.r.l. was incorporated. This company will be involved in construction of the private Italy-Austria interconnector, for which the process of obtaining the necessary consents for the Passo Resia - Glorenza cable section should be completed in 2019.
- on 2 August 2018, the partial demerger of Terna Plus S.r.l. (a wholly-owned subsidiary of the parent, Terna S.p.A.), and the transfer of the demerged assets to a newly established company named Terna Energy Solutions S.r.l., came into effect. The demerged business is focused on Non-Regulated Activities and on the energy solutions activities already carried out by Terna Plus which, following the demerger, is responsible for the Group's South American activities.

The transaction also resulted in the transfer to Terna Energy Solutions of equity interests in the companies that carry out Non-Regulated Activities in Italy: Tamini Trasformatori S.r.l., Rete Verde 17 S.r.l., Rete Verde 18 S.r.l., Rete Verde 19 S.r.l., Rete Verde 20 S.r.l. and Avvenia The Energy Innovator S.r.l..

Associates

Associates are investees over which the Terna Group exercises significant influence, being the ability to participate in the determination of these companies' financial and operating policies, without having control or joint control. In assessing whether or not Terna has significant influence, potential voting rights that are exercisable or convertible are also taken into account.
These investments are initially recognised at cost and subsequently measured using the equity method. The profits or losses attributable to the Group are recognised in the consolidated financial statements when significant influence begins and until that influence ceases. Based on application of the equity method, if there is evidence that the investment has been impaired, the Group determines the amount of the impairment based on the difference between the recoverable amount and the carrying amount of the investment in question. In the event that the loss attributable to the Group exceeds the carrying amount of the equity interest, the latter is written off and any excess is recognised in a specific provision, if the Parent Company is required to meet the legal or constructive obligations of the investee or, in any case, to cover its losses.

Joint ventures

Investments in joint ventures, in which the Group exercises joint control with other entities, are recognised initially at cost and subsequently measured using the equity method. The profits or losses attributable to the Group are recognised in the consolidated financial statements when significant influence begins and until that influence ceases.
In assessing the existence of joint control, it is ascertained whether the parties are bound by a contractual agreement and whether this agreement attributes to the parties the joint control of the agreement itself. Joint control exists when an entity has control over an arrangement on a contractual basis, and only when decisions relating to the relevant activities require the unanimous consent of all parties that jointly control the arrangement.

The list of associates and joint ventures included is shown below:

NAME	REGISTERED OFFICE	CURRENCY	SHARE CAPITAL *	PROFIT FOR THE YEAR*	% INTEREST	METHOD OF CONSOLIDATION	CARRYING AMOUNT AT 31 DECEMBER 2018 (€M)
ASSOCIATES							
Cesi S.p.A.	Milan	Euro	8,550,000	7,478,270	42.698%	Equity Method	49
Business	Experimental research and provision of services related to electro-technology.						
Coreso S.A.	Brussels (Belgium)	Euro	1,000,000	245,771	15.84%	Equity Method	0.4
Business	Technical centre owned by several electricity transmission operators, responsible for coordinating joint operations of TSOs, in order to improve and upgrade the security and coordination of the electricity system in central and western Europe.						
CGES AD	Podgorica (Montenegro)	Euro	155,108,283	4,880,060	22.0889%	Equity Method	26.7
Business	Provision of transmission and dispatching services in Montenegro.						
JOINT VENTURES							
ELMED Etudes Sarl	Tunis (Tunisia)	Tunisian dinar	2,700,000	(178.503)	50%	Equity Method	0
Business	Conduct of preparatory studies for construction of the infrastructure required to connect the Tunisian and Italian electricity systems.						

* Amounts taken from the latest approved financial statements at the date of preparation of this document.

Basis of consolidation

All the separate financial statements of the investees used to prepare the consolidated financial statements were drafted as of 31 December 2018 and have been approved by their respective Boards of Directors and shareholders' meetings; they have been adjusted, where necessary, to align them with the Parent Company's accounting policies.

During preparation of the consolidated financial statements, intercompany balances, transactions, revenue and costs are fully eliminated, net of the related tax effect, where material ("consolidation on a line-by-line basis"). Unrealised gains and losses on transactions with associates and joint ventures are eliminated in proportion to the Group's interest therein. In both cases, unrealised losses are eliminated, unless they represent an impairment.

Translation of foreign currency items

In the Group's financial statements, all transactions in currencies other than the functional currency are recognised at the exchange rate prevailing on the date of the transaction. Monetary assets and liabilities in currencies other than the functional currency are subsequently adjusted at the exchange rate prevailing at year end. Any translation differences are taken to the income statement.

Non-monetary assets and liabilities in foreign currency stated at historical cost are converted at the exchange rate prevailing when the transaction was initially recognised. Non-monetary assets and liabilities in foreign currency stated at fair value are converted at the exchange rate prevailing when fair value was measured.

Property, plant and equipment

Property, plant and equipment is recognised at historical cost, including costs directly attributable to preparing the asset for its intended use. In the event of legal or constructive obligations, cost also includes the present value of the estimated cost of dismantling or removing the asset. The corresponding liability is recognised in provisions for risks and charges. Borrowing costs directly attributable to the purchase, construction or production of an asset that qualify for capitalisation pursuant to IAS 23 are capitalised as part of the cost of the asset. Costs incurred after purchase are recognised as an increase in the carrying amount of the asset to which they relate if it is probable that the future benefits of that cost will flow to the Group, and if the cost can be reliably measured. All other costs are expensed as incurred.

Each element of an item of property, plant and equipment of material value, with respect to the total value of the item to which it belongs, is recognised and depreciated separately.

Property, plant and equipment is shown net of accumulated depreciation and any impairment losses. Depreciation is calculated on a straight-line basis over the estimated useful economic life of the asset, which is reviewed annually, with revisions applied on a prospective basis. Depreciation of an asset begins when the asset becomes available for use.

Liabilities associated with items of property, plant and equipment are taken to a specific provision as a contra account of the related asset. The amount is taken to the income statement through the depreciation of the asset.

Property, plant and equipment is written off either at the time of disposal or when no future economic benefit is expected from their use or disposal. Any profit or loss, recognised in the income statement, is determined as the difference between the net proceeds deriving from disposal and the net carrying amount of the assets eliminated.

The main rates of depreciation, calculated on the basis of the useful lives of the relevant assets, are as follows:

RATES OF DEPRECIATION	
Civil and industrial buildings	2.50%
Transmission lines	2.22%
Transformer substations:	
- Electrical machinery	2.38%
- Electrical devices and equipment	3.13%
- Automation and control systems	6.70%
Central systems for remote management and control:	
- Devices, electrical equipment and ancillary plant	5.00%
- Computers	10.00%

Land, regardless of whether it is free of constructions or related to civil and industrial buildings, is not depreciated, since it has an indefinite useful life.

Property, plant and equipment obtained under finance leases - and through which the Group has substantially acquired all the risks and rewards of ownership - are recognised as the Group's assets at the lower of fair value and the present value of the minimum lease payments due, including any amounts to be paid to exercise the purchase option. The corresponding liability to the lessor is recognised as a financial liability. Assets are depreciated using the criteria and rates described above. If the Group is not reasonably certain that it will acquire ownership at the end of the lease, the asset is depreciated over the shorter of the term of the lease and the asset's useful life.

Leases in which the lessor maintains substantially all the risks and rewards of ownership are classified as operating leases. Costs related to operating leases are expensed out in equal instalments over the term of the lease.

Intangible assets

Intangible assets, which all have finite useful lives, are recognised at cost and shown net of accumulated amortisation and any impairment losses. Amortisation begins when the asset becomes available for use and is calculated on a straight-line basis over the estimated useful life of the related asset, which is reviewed annually. Any revisions to estimated figures are applied on a prospective basis.
Intangible assets essentially consist of the concession to exclusively provide electricity transmission and dispatching services, granted to the Parent Company Terna S.p.A. on 1 November 2005, with the acquisition of the TSO business unit. As established in the Decree issued by the Ministry of Productive Activities on 20 April 2005, this concession has a 25-year term, renewable for another 25 years, from the date of effective transfer of the activities, functions, assets and legal arrangements of the concession from GSE (formerly GRTN) to Terna S.p.A.. This intangible asset was initially recognised at cost, which reflected fair value.
Other intangible assets essentially refer to software developments and upgrades.
Development costs are capitalised by the Terna Group only if they can be reliably estimated and there is the technical possibility and intention to complete the intangible asset so that it will be available for use, and the asset can be used and it is possible to demonstrate that it will generate probable future economic benefits.
Financial expenses directly attributable to the acquisition, construction or production of a non-current asset which justifies capitalisation pursuant to IAS 23 are capitalised to the asset as part of its cost.
All other development costs and research expenses are recognised in the income statement when incurred. These intangible assets are amortised over their estimated residual useful life, which is normally three years, given their rapid obsolescence.

Infrastructure rights

Infrastructure includes the property, plant and equipment and intangible assets employed in dispatching activities in Italy and in the operations in Peru. These activities are carried out under concession arrangements, which fall within the scope of application of IFRIC 12, since the services provided are regulated and control exists over the residual interest. More specifically, infrastructure rights have been recognised as an intangible asset, as valued on the basis of the Intangible Asset model, given the return generated by dispatching activities thanks to the charges paid by users.
The revenue and costs relating to investment in dispatching activities are recognised with reference to the contracts concerned on a stage-of-completion basis; revenue recognised during the construction phase is limited to the amount of the internal and external construction costs incurred, considering that the fair value of the construction services is equivalent to the construction cost paid to third-party contractors plus the internal cost of the technical personnel employed on such construction activities. The assets continue to be amortised and depreciated in accordance with the initial schedule.
By contrast, dispatching revenue continues to be recognised in accordance with IFRS 15 and financial expenses continue to be capitalised pursuant to IAS 23.
IFRIC 12, instead, is not applicable to the part of the Parent Company's concession arrangement relating to transmission activities, since neither the concession nor the related legislation envisages that ownership of the NTG is to be restored to the public grantor, even for a consideration.

Goodwill

Goodwill, deriving from the acquisition of subsidiaries, is allocated to each of the cash generating units (CGU) identified, coinciding with Group companies that own electricity transmission grids and with the Tamini Group, relating to the production and commercialisation of transformers. Goodwill is not amortised after initial recognition but is adjusted to reflect impairment losses, measured as described below. Goodwill relating to investments in associates and joint ventures is included in the carrying amount of those companies. Where negative goodwill arises, it is recognised in the income statement at the time of acquisition.

Inventories

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

Financial instruments

Financial assets

The new standard, IFRS 9 - Financial Instruments, effective from 1 January 2018, is divided into the following phases: classification and measurement, derecognition, impairment and hedge accounting.
In order to classify and measure financial instruments, the Group recognises financial assets at fair value inclusive of transaction costs.
Financial assets represented by debt instruments, and falling within the scope of application of the standard, may be measured at amortised cost, at fair value through other comprehensive income or at fair value through profit or loss, depending on the business model adopted to manage the financial assets and the characteristics of the contractual cash flows.
In accordance with the provisions of IFRS 9, the Group correctly classifies these assets based on the results of so-called SSPI ("solely payments of principal and interest") tests. Under this test, assets may be recognised at amortised cost or fair value through other comprehensive income if the generate cash flows that are solely payments of principal and interest on the principal amount outstanding. This measurement is applied at the level of each individual instrument.

Specifically, the Group measures financial assets:
- at amortised cost, if the financial asset is held with the aim of collecting the contractual cash flows that meet the SPPI test, as the cash flows represent solely payments of principal and interest;
- at fair value through other comprehensive income ("FVOCI"), if the financial asset is held within a business model whose objective is achieved by collecting the contractual cash flows and by selling the financial asset, and the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. Changes in fair value after initial recognition are recognised in other comprehensive income and recycled through profit or loss on derecognition;
- at fair value through profit or loss ("FVTPL"), of the asset is not held in one of the above business models. This category primarily includes derivative financial instruments held for trading and debt instruments with contractual cash flows that are not solely payments of capital and interest.

Infrastructure rights

These include the property, plant and equipment and intangible assets employed in Brazil under concession arrangements falling within the scope of application of IFRIC 12, since the services provided are regulated and control exists over the residual interest. More specifically, infrastructure rights have been recognised in financial assets, as valued on the basis of the Financial Asset model, given the return generated by the activities. This derives from an unconditional contractual right to receive cash or another financial asset from, or at the direction of, the grantor and the fact that the grantor cannot avoid payment.
The revenue and costs relating to investment are recognised with reference to the contracts concerned on a stage-of-completion basis; revenue recognised during the construction phase includes a profit margin on the work performed.

Trade receivables

Trade receivables are initially recognised at fair value and subsequently measured at amortised cost, using the effective interest method. Receivables with due dates that reflect normal commercial terms are not discounted.
In accordance with the provisions of IFRS 9, the Group's trade receivables fall within the hold to collect business model, as these assets are held with the objective of collecting the cash flows primarily by collecting the contractual cash flows, the receivables primarily fall due within 12 months and do not include a significant financial component, and the Group does not intent to sell such receivables.
Trade receivables are recognised net of any losses recognised in a specific allowance for doubtful accounts (identified on the basis described in the paragraph, "Allowance for doubtful accounts"). The new standard,

IFRS 9, adopted from 1 January 2018, has introduced application of a model based on expected credit losses. This requires the Group to assess expected credit losses, and the related changes, at each reporting date, superseding the approach used in IAS 39. It is, therefore, no longer necessary for a trigger event to occur before the recognition of losses on receivables. Specifically, the Group has applied the simplified approach permitted by IFRS 9 to trade receivables, finance lease receivables and assets deriving from contracts with customers, in order to measure the allowance for doubtful accounts based on expected losses over the life of the receivable. The Group has thus determined the amount of expected credit losses using a provisioning matrix, based on information regarding historical credit losses for similar past due exposures, adjusted to take into account current conditions and forward-looking elements.

Cash and cash equivalents

Cash and cash equivalents are recognised at nominal value and include amounts that are available on demand or can be readily converted into a known amount of cash and are subject to an insignificant risk of changes in value.

Trade payables

Trade payables are initially recognised at fair value and subsequently stated at amortised cost. If their due dates reflect normal commercial terms, they are not discounted. The introduction of IFRS 9 has not led to material changes in the method of accounting for these payables.

Financial liabilities

Financial liabilities are recognised at the settlement date and measured at fair value, net of directly related transaction costs. Subsequently, financial liabilities are measured at amortised cost, using the original effective interest method. If the liabilities are covered by fair value hedges, they are adjusted to reflect changes in fair value with respect to the hedged risk.
Subsequent measurement of financial liabilities depends on their classification as financial liabilities at amortised cost or at fair value through profit or loss.

Derivative financial instruments

Derivatives are recognised at fair value at the trade date. The qualifying criteria applied in classifying derivatives as eligible for hedge accounting are as follows:

- the hedging relationship consists only of eligible hedging instruments and eligible hedged items;
- at the inception of the hedging relationship there is formal designation and documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge. That documentation includes identification of the hedging instrument, the hedged item, the nature of the risk being hedged and how the entity will assess whether the hedging relationship meets the hedge effectiveness requirements (including its analysis of the sources of hedge ineffectiveness and how it determines the hedge ratio);
- the hedge ratio of the hedging relationship is the same as that resulting from the quantity of the hedged item that the entity actually hedges and the quantity of the hedging instrument that the entity actually uses to hedge that quantity of hedged item.

An entity shall discontinue hedge accounting prospectively only when the hedging relationship (or a part of a hedging relationship) ceases to meet the qualifying criteria. This includes instances when the hedging instrument expires or is sold, terminated or exercised. For this purpose, the replacement or rollover of a hedging instrument into another hedging instrument is not an expiration or termination if such a replacement or rollover is part of, and consistent with, the entity's documented risk management objective.

For hedge accounting purposes, there are three types of hedge:

- fair value hedges when the hedge regards the exposure to changes in the fair value of the recognised asset or liability or there is an unrecognised firm commitment;
- cash flow hedges when the hedge regards the exposure to variability in cash flows that is attributable to a particular risk associated with all of the recognised asset or liability or a highly probable forecast transaction or the exchange rate risk on an unrecognised firm commitment;
- the hedge of a net investment in a foreign operation.

When derivatives cover the risk of changes in the cash flows of the hedged instruments (cash flow hedges), the portion of changes in the fair value qualifying as effective is initially recognised in "Other comprehensive income" and subsequently in profit or loss, as the cash flows from the hedged item affects profit or loss. The portion of the fair value of the hedging instrument that does not qualify as effective is recognised in profit or loss.
When hedging derivatives cover the risk of changes in the fair value of hedged instruments (fair value hedges), they are recognised at fair value in profit or loss. Accordingly, the hedged items are adjusted to reflect changes in the fair value associated with the hedged risk.
Changes in the fair value of derivatives that do not meet hedge accounting requirements in accordance with the EU-IFRS are recognised in profit or loss.
Fair value is measured on the basis of official quotations for instruments traded in regulated markets. The fair value of instruments not traded in regulated markets is measured by discounting projected cash flows along a yield curve prevailing in the market at the reporting date, and by translating amounts in currencies other than the euro at closing exchange rates.
Financial and non- financial contracts (which are not already measured at fair value) are also analysed to identify any embedded derivatives, which must be separated and measured at fair value.
This analysis is conducted at the time the entity becomes party to the contract or when the contract is renegotiated in a manner that produces a material change in the original associated cash flows.

Employee benefits

The liability associated with employee benefits payable on or after termination of employment relate to defined benefit plans (deferred compensation benefits, additional months' pay, payment in lieu of notice, energy discounts, ASEM health cover and other benefits) or other long-term employee benefits (loyalty bonuses) and is recognised net of any plan assets. The liability is measured separately for each plan on the basis of actuarial calculations that estimate the amount of vested future benefits that employees have accrued at the reporting date. The liability is recognised on an accruals basis over the vesting period and is measured by independent actuaries.

Provisions for risks and charges

Provisions set aside for risks and charges are recognised when, at the reporting date, the Group has a legal or constructive obligation as the result of a past event and it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the disbursement. Where the effect is material, provisions are made by discounting estimated future cash flows using a discount rate that reflects current market rates and the specific risk applicable to the obligation, if any. Where discounting is used, the increase in the provisions due to the passage of time is recognised in the income statement as a financial expense. If it relates to property, plant and equipment (site disposal and restoration, for example), the provision is recognised as a contra entry to the asset to which it relates. The expense is recognised in the income statement through depreciation of the item of property, plant and equipment to which it relates.
Changes in the estimates are recognised in the income statement for the year in which the change occurs, except for the expected costs of dismantling, removal and restoration resulting from changes in the timing and use of the economic resources necessary to extinguish the obligation, or are attributable to a material change in the discount rate. These costs are recognised as an increase or reduction in the related assets and recognised in the income statement through depreciation.

Government grants

Government grants are recognised when there is a reasonable certainty that they will be received and that the Group will comply with all the conditions required for disbursement. Grants received in relation to specific assets whose value is recognised under non-current assets are recognised, in the case of plant already in operation at 31 December 2002, among other liabilities and taken to the income statement over the depreciation period for the assets in question. As of the 2003 financial year, grants related to new plant entering service are recognised as a direct reduction in the non-current asset concerned.
Grants related to income are recognised in the income statement when the conditions for recognition are met.

Revenue

The Group's revenue can be categorised as follows:

- **Revenue from sales and services,** including revenue from contracts with customers and therefore falling within the scope of IFRS 15.
  In accordance with the provisions of IFRS 15, applied from 1 January 2018, revenue from contracts with customers is recognised when the performance obligations identified in the contract are satisfied and control over the goods or services is transferred to the customer for an amount that reflects the consideration that the Group expects to receive in exchange for the goods or services.
  The standard envisages two methods for identifying the correct time at which to recognise the revenue attributable to each performance obligation: at contract inception, the Group determines if the goods or services covered by the performance obligation will be transferred to the customer over a period of time or at a point in time:
  - *Revenue from the sale of goods* is recognised when control of the goods is transferred to the customer (at a point in time). The Group determines if there are other promises in the contract representing a performance obligation to which a part of the transaction consideration must be allocated. In determining the sale price, the Group takes into account the effects of a variable consideration, significant financial components, non-monetary components and amounts to be paid to the customer (if present);
  - *Revenue from services* is recognised with reference to the stage of completion of the activity, in accordance with the provisions of IFRS 15 (over a period of time).

- **Other revenue and income**, which includes revenue from lease arrangements (which from 1 January 2019 are governed by IFRS 16) and other residual forms of revenue, included within the scope of application of IFRS 15, deriving from sales of goods not forming part of the Group's ordinary activities.

Financial income and expenses

Financial expenses directly attributable to the acquisition, construction or production of an asset that qualify for capitalisation are capitalised as part of the cost of the asset. The property, plant and equipment and intangible assets involved are those that require at least one year in order to prepare them for use. The directly attributable financial expenses are expenses that would not have been incurred had the expenditure for the asset not been incurred.

Where funds are borrowed specifically, the costs eligible for capitalisation are the actual costs incurred less any income earned on the temporary investment of such borrowings. Where loans are obtained for general purposes, the eligible amount is determined by applying a capitalisation rate to the expenditure on that asset equal to the weighted average of the financial expenses applicable to the borrowings outstanding for the year, excluding any specifically borrowed funds. The amount of capitalised financial expenses during a year will in any case not exceed the amount of financial expenses incurred during that year.

Capitalisation commences as from the date all the following conditions are first met: (a) expenditure has been incurred for the asset; (b) financial expenses have been incurred; and (c) the activities involved in preparing the asset for its intended use or sale are in progress. Capitalisation ceases when the activities involved in preparing the asset for its intended use or sale are substantially complete.

The average capitalisation rate used for 2018 was 1.23% (the rate for 2017 was 1.30%).

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

Dividends

Dividends from investees are recognised when the shareholders' right to receive payment is established. Dividends and interim dividends payable to shareholders are shown as changes in equity at the date in which they are approved by the General Meeting of shareholders and the Board of Directors, respectively.

Earnings per share

Basic earnings per share is calculated by dividing the profit or loss for the year attributable to holders of the ordinary shares by the weighted average of ordinary shares outstanding during the year.

Income taxes

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

New accounting standards

International financial reporting standards effective as of 1 January 2018

Two new accounting standards, whose application has not had a material impact for the Group, and a number of new amendments to standards already applied came into effect from 1 January 2018.

The following information is provided with regard to the new accounting standards:

IFRS 15 - Revenue from Contracts with Customers
On 29 October 2016, the European Commission endorsed the new IFRS 15 on revenue recognition. The new standard introduced a five-step revenue recognition model. The steps are as follows: 1) identification of the contract; 2) identification of the performance obligations in the contract; 3) determination of the transaction price; 4) allocation of the transaction price; 5) recognition of revenue when the performance obligation is satisfied. Under the standard, the obligation is satisfied when control over the goods or services underlying the performance obligation is transferred to the customer. Control is defined as the ability to direct the use of and obtain substantially all of the remaining benefits from the asset.

The purpose of the new standard is to provide a consistent, overall framework for revenue recognition, applicable to all contracts with customers (with the exception of leases, insurance contracts and financial instruments). The new standard has replaced all existing revenue recognition requirements under IFRS. Specifically, it has replaced the following standards:
• IAS 11 - Construction Contracts and related interpretations;
• IAS 18 - Revenue;
• IFRIC 13 - Customer Loyalty Programmes;
• IFRIC 15 - Agreements for the Construction of Real Estate;
• IFRIC 18 - Transfers of Assets from Customers;
• SIC 31 - Revenue - Barter Transactions Involving Advertising Services.

In addition, on 31 October 2016, the European Commission endorsed guidance to clarify certain practical aspects brought to the fore during discussion of the TRG (Transition Resource Group for Revenue Recognition) regarding the application of IFRS 15: identifying performance obligations, principal versus agent considerations and application guidance on licensing. The new standard was effective from 1 January 2018, with early and retrospective application permitted.

The Terna Group has applied the new standard from 1 January 2018, using the modified retrospective approach, accounting for the cumulative effect of adoption of IFRS 15 from the date of first-time adoption, electing not to apply the standard to completed contracts.

Adoption of the new standard has had non-material quantitative effects for the Group, limited to minor aspects of its Regulated Activities (revenue from connections to the NTG) and certain contracts related to Non-Regulated Activities (consolidated revenue generated by the Tamini Group). The effects on the accounts of application of the new standard have resulted in a negative impact on Non-Regulated contract revenue, generating an overall after-tax reduction in the Group's equity at 1 January 2018 of approximately €1 million and trade receivables of approximately €2 million.

IFRS 9 - Financial Instruments

On 22 November 2016, the European Commission approved IFRS 9 - Financial Instruments, in its final version of 24 July 2014, which starts the complex and detailed process of replacing IAS 39, divided into the following phases: classification and measurement, derecognition, impairment and hedge accounting. The new standard was effective from 1 January 2018, with early application permitted. The main changes introduced by the new standard include, among other things, unified classification guidance for all types of financial instruments, including the requirements for recognition and measurement, impairment, derecognition and hedge accounting. Financial assets will therefore be classified as a whole and not subject to complex separation rules. The new classification criterion for financial instruments is based on the business model adopted by the Company to manage financial assets with reference to the collection of cash flows and to the characteristics of the contractual cash flows of the financial assets. As regards impairment, the model provided for in IAS 39 based on the criterion of incurred loss, which postponed the recognition of losses on receivables to the moment of occurrence of the trigger event, has been replaced, as it was considered a weakness. The new IFRS 9 provides for a model based on a prospective view, which requires the immediate recognition of losses on receivables expected over the life of the financial instrument, as a trigger event no longer needs to occur before the recognition of losses on receivables. The new standard has also completed the stage of the Hedge accounting project, except for the rules on macro hedge accounting, which will be published at a later date. It provides, among the other changes, for a substantial revision of hedge accounting so as to better reflect risk management activities in the financial statements.

The Terna Group has applied the new standard retrospectively from 1 January 2018 with regard to classification and measurement, derecognition and impairment, with presentation of the cumulative effects of first-time adoption at the transition date in equity.

Adoption of the new standard has had non-material quantitative effects for the Group, limited essentially to the impairment of trade receivables, bank deposits and financial guarantees. Analysis of the impact was applied to impaired financial assets held by the Group. In application of the simplified approach permitted by the standard, based on the recognition of losses on receivables expected over the life of the financial instrument, receivables classified in stage 2 (with particular regard to trade receivables representing the largest part of the Group's receivables) have been grouped according to due date. The Group then applied the impairment model based on a collective assessment of expected losses. In conducting the assessment, the Group used a matrix to calculate the expected loss, based on information regarding historical losses for similar instruments, adjusted to take into account forward-looking elements. The effects on the accounts of application of the new standard have resulted in a negative impact on trade receivables, reducing their value by approximately €1.5 million, and on bank deposits, which have been reduced by approximately €1.5 million. This generated an overall after-tax reduction in equity attributable to owners of the parent at 1 January 2018 of approximately €2 million and in equity attributable to non-controlling interests of approximately €0.9 million. With regard to hedge accounting, application was prospective from the date of first-time adoption. At that date, existing hedging relationships were not modified and the new accounting rules, with specific regard to the time value of options and the forward elements of forward contracts, did not result in any differences.

The following table shows changes in the consolidated statement of financial position at 1 January 2018 as a result of application of the two standards, IFRS 15 and IFRS 9.

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

(€m)

	AT 31 DECEMBER 2017	IMPACT OF IFRS 9	IMPACT OF IFRS 15	RESTATED AT 1 JANUARY 2018
A – NON-CURRENT ASSETS				
1. Property, plant and equipment	12,752.8			12,752.8
2. Goodwill	230.1			230.1
3. Intangible assets	275.6			275.6
4. Investments accounted for using the equity method	77.9			77.9
5. Non-current financial assets	120.1			120.1
6. Other non-current assets	14.2			14.2
Total non-current assets	**13,470.7**	**-**	**-**	**13,470.7**
B – CURRENT ASSETS				
1. Inventories	14.8			14.8
2. Trade receivables	1,265.9	(1.5)	(2.0)	1,262.4
3. Current financial assets	0.2			0.2
4. Cash and cash equivalents	1,989.2	(1.5)		1,987.7
5. Income tax assets	36.9			36.9
6. Other current assets	139.1			139.1
Total current assets	**3,446.1**	**(3.0)**	**(2.0)**	**3,441.1**
TOTAL ASSETS	**16,916.8**	**(3.0)**	**(2.0)**	**16,911.8**
C – EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT				
1. Share capital	442.2			442.2
2. Other reserves	820.4			820.4
3. Reserves	2,001.7	(2.0)	(1.0)	1,998.7
3. Retained earnings/ (accumulated losses)	(149.3)			(149.3)
4. Interim dividend	688.3			688.3
Total equity attributable to owners of the Parent	**3,803.3**	**(2.0)**	**(1.0)**	**3,800.3**
D – EQUITY ATTRIBUTABLE TO NON-CONTROLLING INTERESTS	**25.7**	**(0.2)**	**(0.4)**	**25.1**
Total equity attributable to owners of the Parent and non-controlling interests	**3,829.0**	**(2.2)**	**(1.4)**	**3,825.4**
E – NON-CURRENT LIABILITIES				
1. Long-term borrowings	8,671.6			8,671.6
2. Employee benefits	80.7			80.7
3. Provisions for risks and charges	266.5	0.1		266.6
4. Deferred tax liabilities	8.6	(0.9)	(0.6)	7.2
5. Non-current financial liabilities	10.5			10.5
6. Other non-current liabilities	251.0			251.0
Total non-current liabilities	**9,.288.9**	**(0.8)**	**(0.6)**	**9,287.6**
F – CURRENT LIABILITIES				
1. Short-term borrowings	118.0			118.0
2. Current portion of long-term borrowings	884.3			884.3
3. Trade payables	2,497.9			2,497.9
4. Tax expense	-			-
5. Current financial liabilities	105.7			105.7
6. Other current liabilities	193.0			193.0
Total current liabilities	**3,798.9**	**-**	**-**	**3,798.9**
TOTAL LIABILITIES AND AT EQUITY	**16,916.8**	**(3.0)**	**(2.0)**	**16,911.8**

(€m)

		IAS 39		IFRS 9
		RECEIVABLES AND LOANS	HELD TO MATURITY	HELD TO COLLECT
	AT 1 JANUARY 2018	RECEIVABLES	ASSETS HELD TO MATURITY	FINANCIAL ASSETS MEASURED AT AMORTISED COST
A – NON-CURRENT ASSETS				
5. Non-current financial assets	120.1	-	120.1	120.1
B – CURRENT ASSETS				
2. Trade receivables	1,262.4	1,262.4	-	1,262.4
3. Current financial assets	0.2	-	0.2	0.2
4. Cash and cash equivalents	1,987.7	-	1,987.7	1,987.7
TOTAL ASSETS		**1,262.4**	**2,108.0**	**3,370.4**

(€m)

		IAS 39		IFRS 9	
		OTHER FINANCIAL LIABILITIES	HEDGE ACCOUNTING	OTHER	HEDGE ACCOUNTING
	AT 1 JANUARY 2018	FINANCIAL LIABILITIES MEASURED AT AMORTISED COST	CASH FLOW HEDGES	FINANCIAL LIABILITIES MEASURED AT AMORTISED COST	CASH FLOW HEDGES
C – EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT					
2. Other reserves	820.4	807.7	12.7	807.7	12.7
E – NON-CURRENT LIABILITIES					
1. Long-term borrowings	8,671.6	8,671.6	-	8,671.6	-
5. Non-current financial liabilities	10.5	-	10.5	-	10.5
F – NON-CURRENT FINANCIAL LIABILITIES					
1. Short-term borrowings	118.0	118.0	-	118.0	-
2. Current portion of long-term borrowings	884.3	884.3	-	884.3	-
3. Trade payables	2,497.9	2,497.9	-	2,497.9	-
5. Current financial assets	105.7	105.7	-	105.7	-
TOTAL LIABILITIES AND EQUITY		**13,085.2**	**23.2**	**13,085.2**	**23.2**

The new amendments are not expected to have a material impact, with the main ones described below:

IFRIC 22: Foreign Currency Transactions and Advance Consideration

On 28 March 2018, the European Commission endorsed the interpretation of IAS 21 through Regulation 2018/519. The interpretation providing guidance in the selection of an exchange rate to be used when recording a transaction in a foreign currency, should the consideration in the foreign currency have been received or paid in advance of recognition of the related assets.

Amendment to IFRS 15: Clarifications to IFRS 15 Revenue from Contracts with Customers

On 31 October 2017, the European Commission endorsed the amendment to IFRS 15 through Regulation 2017/1987. This amendment provides clarifications on certain aspects of the standard's requirements and proposes transition relief for entities adopting the standard.

Amendment to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts

On 3 November 2017, the European Commission endorsed the amendment to IFRS 4 through Regulation 2017/1988. This amendment aims to remedy the temporary accounting impact of the different effective dates of IFRS 9 and of the new standard governing insurance contracts, IFRS 17, which replaces IFRS 4.

Amendment to IFRS 2: Classification and Measurement of Share-based Payment Transactions

On 26 February 2018, the European Commission endorsed the amendment to IFRS 2 through Regulation 2018/289. This amendment clarifies the classification and measurement of share-based payments.

Amendment to IAS 40: Transfers of Investment Property

On 14 March 2018, the European Commission endorsed the amendment to IAS 40 through Regulation 2018/400. This amendment regards the account impact of changes in the use of a property, and above all clarifies the cases in which an entity is authorised to classify a property as investment property.

International financial reporting standards endorsed but not yet effective

IFRS 16 - Leases

Endorsed on 31 October 2017, through Regulation 2017/1986, the new IFRS 16 governs accounting for leases, replacing the previous IAS 17. Among the changes, the new standard, in dispensing with the distinction between operating and finance leases, bases the accounting presentation on the "right-of-use" approach, which for the lessee makes the accounting uniform for any type of lease. The method of accounting applicable to lessors under IFRS 16 remains substantially unchanged with respect to the current accounting policy under IAS 17. Lessors will continue to classify all leases using the same classification rules applicable under IAS 17 and will distinguish between two types of lease: operating and finance. The standard also includes two recognition exemptions for lessees for leases where the underlying asset is of "low value" (for example, personal computers or assets with a unit value of below US$5,000) and short-term leases (lease arrangements with a lease term of less than or equal to 12 months). Under the accounting standard just described, at the inception date of a lease, the lessee must recognise a lease liability and an asset representing the right to use the underlying asset during the lease term (the right of use). Lessees must recognise interest expense on the lease liability separately from the depreciation charge on the right-of-use asset.

Terna will adopt the standard from the mandatory effective date of 1 January 2019, retrospectively accounting for the cumulative effect of initial application of the standard at the date of initial application, in accordance with paragraph C8b). In the case of leases previously classified as operating leases (under IAS 17), the Group will recognise:

a) the lease liability at the date of initial application at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate at the date of initial application;
b) the right-of-use asset at an amount equal to the lease liability adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position immediately before the date of initial application.

Terna will apply the exemptions put forward by the standard for lease arrangements expiring within 12 months of the initial date of application and for leases where the underlying asset is of low value.

Terna has elected to apply the practical expedient provided for in the standard, excluding leases for which the lease term ends within 12 months of the initial date of application from the calculation, when this term has been determined in application of the guidance provided by IFRS16. However, as required by the standard, Terna will provide a specific disclosure in this regard at the time of initial application and on a continuous basis.

Applying this model, Terna will recognise: (i) assets and liabilities for all leases with terms in excess of twelve months; (ii) depreciation of the recognised assets and interest expense on the lease liability separately in the income statement.

Terna is further assessing the impact of application of the new standard, with particular regard to assets such as buildings, equipment and motor vehicles and Indefeasible Rights of Use (IRU).

The assessment process, which is close to completion, does not indicate that there will be a material impact on the Group's financial statements in 2019 as a result of application of this standard, limited essentially to recognition of the right-of-use assets and the lease liabilities.

Amendment to IFRS 9: Prepayment Features with Negative Compensation

Endorsed by the European Commission on 22 March 2018, with Regulation 2018/498, the amendment to IFRS 9 allows the measurement of certain financial assets with a prepayment option with negative compensation features at amortised cost or at fair value through comprehensive income. The amendment will come into effect from 1 January 2019.

IFRIC 23 - Uncertainty over Income Tax Treatments

Endorsed by the European Commission on 23 October 2018, with Regulation 2018/1595, IFRIC 23 came into effect from 1 January 2019. The interpretation clarifies how to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. It also provides guidance on how to account for current and deferred tax assets and liabilities.

International financial reporting standards awaiting endorsement

For newly-issued amendments, standards and interpretations that have not yet been endorsed by the EU, but which address issues that affect or could affect the Terna Group, assessments are currently being conducted of the possible impact of their application on the financial statements, taking into account the date on which they will take effect. In particular:

IFRS 17 - Insurance Contracts

The new accounting standard for insurance contracts was published by the IASB on 18 May 2017, to replace the interim version of IFRS 4. The standard defines the new principles for the recognition, measurement, presentation and disclosure of insurance contracts. The General Model of reference is based on the discounting of expected cash flows, with the indication of a risk adjustment and upfront profits through the "contractual service margin", which cannot be negative, released to income over the term of the contract.

Amendment to IAS 28: Long-term Interests in Associates and Joint Ventures

Published by the IASB on 12 October 2017, the amendment to IAS 28 clarifies which long-term receivables are part of the net investment in the associate or joint venture.

Improvements to IFRSs (2015-2017 Cycle)

Published by the IASB on 12 December 2017, the annual improvements related to the 2015-2017 cycle contain minor amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23.

Amendment to IAS 19: Plan Amendment, Curtailment or Settlement

Published by the IASB on 7 February 2018, the amendment to IAS 19 clarifies how pension costs should be calculated in the event of modifications to a defined-benefit plan.

References to the Conceptual framework in IFRS Standards

Published on 29 March 2018, this is an amendment to the Conceptual Framework for Financial Reporting. The main changes regard a new section on measurement, improved definitions and guidance, above all with reference to the definition of liabilities and clarification on concepts such as prudence and measurement uncertainties.

Amendment to IFRS 3: Definition of a Business

Published by the IASB on 22 October 2018, the amendment to IFRS 3 provides a clearer definition of a business, giving guidance and illustrative examples for identifying when a group of assets constitutes a business, thereby falling within the scope of application of IFRS 3.

Amendment to IAS 1 and IAS 8: Definition of Material

As part of the "Disclosure Initiative" project, the amendment to IAS 1 and IAS 8 was published on 31 October 2018. This modifies the definition of materiality in relation to the two standards, in order to standardise and clarify the definitions currently provided in the standards and in the Conceptual Framework.

B. Notes to the consolidated income statement

Revenue

1. REVENUE FROM SALES AND SERVICES - €2,272.5 MILLION

(€m)

	2018	2017	CHANGE
Transmission charges billed to grid users	1,789.1	1,803.8	(14.7)
Back-billing of transmission charges for previous years	-	(0.2)	0.2
Other energy-related revenue and from services performed under concession	262.3	214.0	48.3
Quality of service bonuses/(penalties)	7.4	7.4	0.0
Other sales and services	213.7	159.0	54.7
TOTAL	**2,272.5**	**2,184.0**	**88.5**

Transmission charges

The charges for use of the NTG regard the revenue attributable to the Parent Company (€1,657.5 million) and the subsidiary, Rete S.r.l. (€131.6 million) as owners and operators of the grid.

The reduction in revenue from the transmission service (down €14.5 million) broadly reflects revision of the related tariff to reflect completion, in 2017, of revenue from work in progress and a reduction in the volume of energy transported, offset by an increase in the portion of the NTG owned by the two companies. The balance also includes the estimated impact of the revised contribution from international interconnections.

Other energy-related revenue and from services performed under concession

This item regards dispatching and metering revenue (essentially relating to €111.0 million for the dispatching component and €32.0 million regarding certain expenses[1] not covered by the dispatching charge) and revenue from infrastructure construction and upgrade services performed under concession, recognised in application of IFRIC 12 (€119.1 million). This includes revenue from activities in South America (€92.4 million in Brazil and €1.3 million in Peru).

The increase in “Other energy-related revenue and from services performed under concession” compared with 2017, totalling €48.3 million, is primarily linked to increases in the dispatching charge and the above expenses not covered by the charge (up €31.2 million). New investment in assets held under concession in South America was also a factor in the increase (up €12.7 million).

(€m)

OTHER ENERGY-RELATED REVENUE AND FROM SERVICES PERFORMED UNDER CONCESSION	2018	2017	Δ
Dispatching and metering revenue	143.2	111.9	31.3
Revenue from services performed under concession (IFRIC 12)	119.1	102.1	17.0
- of which in Italy	*25.5*	*21.1*	*4.4*
- of which overseas	*93.7*	*81.0*	*12.7*
TOTAL OTHER ENERGY-RELATED REVENUE AND FROM SERVICES PERFORMED UNDER CONCESSION	**262.3**	**214.0**	**48.3**

Quality of service bonuses/(penalties)

This item, amounting to €7.4 million, regards the RENS incentive mechanism introduced by Resolution 653/2015/r/eel, calculated on a pro rata basis taking into account the estimated overall results expected in the 2016-2019 regulatory period.

The figure is unchanged with respect to the previous year.

[1] ARERA has decided to allow the recovery of expenses through the uplift mechanism provided for in art.44 of Resolution 111/2006. These expenses regard receivables that are no longer recoverable and relating to the period 2006-2015 (ref. Resolution 218/2018) and increased payments made to fund the regulator for the years 2013-2017.

Other sales and services

The item, “Other sales and services”, amounting to €213.7 million, mainly regards revenue from Non-regulated Activities, regarding:

- the sale of transformers by the subsidiary, Tamini (€99.6 million);
- Energy Solutions (€35.5 million), including maintenance services, totalling €16.4 million and energy efficiency (€4.2 million), primarily attributable to the subsidiary, Avvenia The Energy Innovator S.r.l., in addition to revenue from EPC contracts, totalling €14.9 million;
- Connectivity (€28.0 million) with specific regard to support and housing services for fibre networks.

This item also includes revenue from the private Italy-France Interconnector (€9.0 million), representing the accrued portion of the revenue attributable to the Group for services provided during construction.
The item also includes revenue attributable to the Group’s International Activities relating to construction of the power line in Uruguay, totalling €38.7 million.

The increase compared with 2017 (up €54.7 million) primarily reflects the following:

- increased revenue as construction work in Uruguay progresses (up €31.5 million);
- the new classification of revenue from support and housing services for fibre networks, totalling €22.9 million, essentially following the reclassification of this revenue - classified in other revenue and income in 2017 - in application if the new standard, IFRS 15;
- an increase in revenue at the Tamini Group (up €8.1 million), primarily due increased sales of transformers during the year;
- an increase in revenue from Energy Solutions (up €6.0 million), primarily due to the contribution from energy efficiency activities (up €4.1 million, reflecting Avvenia’s contribution), new contracts (up €4.5 million) after the reduction in O&M revenue (down €2.6 million), above all in the photovoltaic sector following the renegotiation of contracts with a company operating in the sector;
- a reduction in revenue from the private Italy-France Interconnector (down €7.0 million), due to the increase in revenue recognised in 2017 following recovery of the amount due for the period prior to being granted the exemption;
- reduced revenue from connection services (down €4.2 million).

Pass-through revenue/expenses

This item regards "pass-through" revenue and expenses (the balance of which amounts to zero) attributable solely to the Parent Company. These items result from daily purchases and sales of electricity from electricity market operators. Measurements for each point of injection and withdrawal are taken and the differences, with respect to energy market schedules are calculated. These differences, known as imbalances, are then measured using algorithms established by the regulatory framework. The net charge resulting from calculation of the imbalances and the purchases and sales, carried out by the Parent Company Terna on the DSM, is billed on a pro rata basis to each end consumer via a specific uplift payment. This item also reflects the portion of the transmission charge that the Parent Company passes on to other grid owners, not included in the scope of consolidation.

The components of these transactions are shown in greater detail below:

(€m)

	2018	2017	CHANGE
Power Exchange-related revenue items	**3,860.1**	**4,039.8**	**(179.7)**
- Uplift	1,648.4	2,093.5	(445.1)
- Electricity sales	523.0	434.6	88.4
- Imbalances	506.2	543.6	(37.4)
- Congestion revenue	331.1	368.0	(36.9)
- Charges for right to use transmission capacity and market coupling	337.8	297.6	40.2
- Interconnectors/shippers	75.2	75.1	0.1
- Load Profiling for public lighting	66.8	73.7	(6.9)
- Other Power Exchange-related pass-through revenue items	371.6	153.7	217.9
Total over-the-counter revenue items	**1,311.7**	**1,260.2**	**51.5**
- Transmission revenue passed on to other NTG owners	4.8	5.9	(1.1)
- Charge to cover cost of essential plants	392.6	327.5	65.1
- Charge to cover cost of energy delivery capacity	277.6	208.9	68.7
- Charge to cover cost of interruptibility service	279.5	359.8	(80.3)
- Charge to cover cost of LV capacity and protection service	276.2	267.6	8.6
- Other pass-through revenue for over-the-counter trades	81.0	90.5	(9.5)
TOTAL PASS-THROUGH REVENUE	**5,171.8**	**5,300.0**	**(128.2)**
Total Power Exchange-related cost items	**3,860.1**	**4,039.8**	**(179.7)**
- Electricity purchases	2,496.5	2,322.9	173.6
- Imbalances	331.6	771.3	(439.7)
- Congestion revenue	217.1	280.6	(63.5)
- Charges for right to use transmission capacity and market coupling	136.1	116.0	20.1
- Interconnectors/Shippers	366.8	330.8	36.0
- Load Profiling for public lighting	80.5	81.1	(0.6)
- Other Power Exchange-related pass-through cost items	231.5	137.1	94.4
Total over-the-counter cost items	**1,311.7**	**1,260.2**	**51.5**
- Transmission costs passed on to other NTG owners	4.8	5.9	(1.1)
- Fees paid for essential units	392.6	327.5	65.1
- Fees paid for energy delivery capacity	277.6	208.9	68.7
- Fees paid for interruptibility service	279.5	359.8	(80.3)
- Fees paid for LV capacity and protection service	276.2	267.6	8.6
- Other pass-through costs for over-the-counter trades	81.0	90.5	(9.5)
TOTAL PASS-THROUGH COSTS	**5,171.8**	**5,300.0**	**(128.2)**

The total uplift cost in 2018, amounting to €1,648.4 million, is down €445.1 million on the figure for the previous year, primarily reflecting a reduction in the cost of demand- and supply-side imbalances, linked partly to the application of new regulations effective from September 2017.

2. OTHER REVENUE AND INCOME - €46.6 MILLION

(€m)

	2018	2017	CHANGE
Revenue from IRU contracts for fibre	10.7	11.2	(0.5)
Insurance proceeds as compensation for damages	10.3	3.2	7.1
Sundry grants	8.4	8.5	(0.1)
Gains on sale of components of plant	3.8	2.8	1.0
Sales to third parties	3.5	2.5	1.0
Contingent assets	2.2	9.1	(6.9)
Rental income	0.7	23.1	(22.4)
Other revenues	7.0	3.6	3.4
TOTAL	**46.6**	**64.0**	**(17.4)**

The most significant components of "Other revenue and income" primarily regard IRU contracts for fibre (€10.7 million), insurance proceeds (€10.3 million), sundry grants (€8.4 million) and other revenues (€7.0 million).

This item, totalling €46.6 million, is down €17.4 million compared with the previous year, primarily due to the fact that the figure for 2017 included revenue from support and housing services for fibre networks, totalling €22.1 million, which from 2018 has been reclassified to revenue from sales and services in application of the new standard, IFRS 15, as described above.

The figure also reflects adjustment, in 2017, of the exposure to contractual obligations following the sale of a photovoltaic project (down €6.2 million) and an increase of €3.4 million in other revenues, including €3.0 million reflecting revenue recognised following the acquisition of Avvenia, partially offset by an increase of €7.1 million in insurance proceeds.

Operating costs

3. RAW AND CONSUMABLE MATERIALS USED - €204.4 MILLION

This item includes the value of the various materials and equipment used in the ordinary operation and maintenance of the plant belonging to the Group and third parties, and the materials consumed in the performance of contract work by the Tamini Group and in South America.

The increase of €46.3 million compared with the previous year (€158.1 million in 2017), an increase in costs relating to construction of the power line in Uruguay (up €37.5 million) and an increase in costs relating to contracts acquired as part of Non-regulated Activities, above all regarding the increase in contracts for the supply of transformers by the subsidiary, Tamini (up €9.2 million) and the contribution from the subsidiary, Avvenia The Energy Innovator, totalling €3.0 million.

4. SERVICES - €191.2 MILLION

(€m)

	2018	2017	CHANGE
Maintenance and sundry services	91.9	86.8	5.1
Tender costs for plant	45.9	42.8	3.1
Remote transmission and telecommunications	12.3	12.2	0.1
Lease expense	17.2	13.2	4.0
IT services	13.0	16.4	(3.4)
Insurance	10.9	11.0	(0.1)
TOTAL	**191.2**	**182.4**	**8.8**

This item, totalling €191.2 million, reflect an increase of €8.8 million compared with 2017 (€182.4 million). This reflects revised right-of-way fees in certain regions of Italy and the increased cost of maintenance, works and various services provided by external contractors, after a reduction in the cost of contract work carried out by the Tamini Group, amounting to €4.3 million.

5. PERSONNEL EXPENSES - €244.1 MILLION

(€m)

	2018	2017	CHANGE
Salaries, wages and other short-term benefits	300.4	293.2	7.2
Directors' remuneration	2.2	2.4	(0.2)
Termination benefits (*TFR*) energy discounts and other employee benefits	9.7	5.8	3.9
Early retirement incentives	-	19.6	(19.6)
Gross personnel expenses	***312.3***	***321.0***	***(8.7)***
Capitalised personnel expenses	(68.2)	(63.8)	(4.4)
TOTAL	**244.1**	**257.2**	**(13.1)**

Personnel expenses, amounting to €244.1 million in 2018, are down €13.1 million, primarily due to net provisions for early retirement schemes in 2017 (down €19.6 million), partially offset by the significant increase in the average workforce primarily as a result of the launch, in 2018, of the new initiatives envisaged in the Strategic Plan.

The following table shows the Group's workforce by category at the end of the year and the average for the year.

	AVERAGE WORKFORCE		WORKFORCE AT	
	2018	2017	31 DECEMBER 2018	31 DECEMBER 2017
Senior managers	72	72	67	71
Middle managers	620	579	638	569
Office staff	2,144	2,024	2,290	2,021
Blue-collar workers	1,252	1,263	1,257	1,236
TOTAL	**4,088**	**3,938**	**4,252**	**3,897**

The net increase in the average workforce compared with 2017 amounts to 150.

At 31 December 2018, the Terna Group's workforce breaks down as follows:

	TERNA S.P.A.	TERNA RETE ITALIA S.P.A.	TERNA ENERGY SOLUTIONS S.R.L.	AVVENIA THE ENERGY INNOVATOR S.R.L.	GRUPPO TAMINI	TERNA CRNA GORA D.O.O.	SPE SANTA MARIA TRANSMISSORA DE ENERGIA S.A.	SPE SANTA LUCIA TRANSMISSORA DE ENERGIA S.A.	TERNA PERU S.A.C.	DIFEBAL S.A.	TOTAL
Number	648	3,150	45	16	355	9	4	13	5	7	4,252

6. AMORTISATION, DEPRECIATION AND IMPAIRMENT LOSSES - €554.1 MILLION

(€m)

	2018	2017	CHANGE
Amortisation of intangible assets	52.0	50.4	1.6
- of which rights on infrastructure	*22.8*	*24.8*	*(2.0)*
Depreciation of property, plant and equipment	488.0	465.2	22.8
Impairment losses on property, plant and equipment	13.4	9.3	4.1
Impairment losses on current assets	0.7	1.6	(0.9)
TOTAL	**554.1**	**526.5**	**27.6**

Amortisation, depreciation and impairment losses, amounting to €554.1 million, is up €27.6 million compared with 2017, following the entry into service of new infrastructure.

7. OTHER OPERATING COSTS - €28.8 MILLION

(€m)

	2018	2017	CHANGE
Indirect taxes and local taxes and levies	6.8	7.1	(0.3)
Quality of service costs	5.1	10.5	(5.4)
of which mitigation and sharing mechanisms	*3.1*	*7.7*	*(4.6)*
of which the Fund for Exceptional Events	*1.9*	*2.4*	*(0.5)*
of which compensation mechanisms for HV users	*0.1*	*0.4*	*(0.3)*
Adjustment of provisions for litigation and disputes	(2.6)	9.3	(11.9)
Losses on sales/disposal of plant	0.3	0.7	(0.4)
Net contingent liabilities	4.5	1.4	3.1
Other	14.7	17.4	(2.7)
TOTAL	**28.8**	**46.4**	**(17.6)**

The Group's other operating costs, amounting to €28.8 million, are primarily attributable to the Parent Company (€18.2 million) and the Tamini Group (€6.3 million). They include indirect taxes and local taxes and levies, totalling €6.8 million and including €3.7 million in Tosap (Tassa per l'Occupazione del Suolo Pubblico, a tax on the occupation of public land) and Tares (Tassa Rifiuti e Servizi, a tax on waste and municipal services). These costs also include net quality of service costs (€5.1 million), the adjustment to provisions for litigation and disputes set aside to cover outstanding liabilities that, at the end of the year, could result from court judgements and out-of-court settlements regarding the Group's activities (down €2.6 million) and other costs (€14.7 million), which include membership dues and contributions to trade bodies and associations, donations and other expenses.

The reduction of €17.6 million in this item primarily reflects the adjustment to provisions for litigation and disputes (down €11.9 million), mainly as a result of the favourable outcomes to a number of disputes arising in previous years, in addition to the net costs resulting from the mechanisms designed to regulate the quality of service, broadly reflecting higher costs incurred in 2017, totalling €5.4 million, in relation to certain major events in central and southern Italy, with respect to outages in 2018 essentially due to events in northern Italy in October.

8. FINANCIAL INCOME/(EXPENSES) - (€91.4) MILLION

(€m)

	2018	2017	CHANGE
FINANCIAL EXPENSES			
Financial expenses paid to Cassa Depositi e Prestiti	(3.0)	(3.7)	0.7
Interest expense on medium/long-term borrowings and related hedge	(101.0)	(94.0)	(7.0)
Discounting of termination benefits (TFR) other provisions for employee benefits and provisions for risks and charges	(0.7)	(1.1)	0.4
Capitalised financial expenses	15.1	12.8	2.3
Translation differences	(7.5)	(0.8)	(6.7)
Other financial expenses	(1.2)	(9.7)	8.5
Total expenses	**(98.3)**	**(96.5)**	**(1.8)**
FINANCIAL INCOME			
Interest income and other financial income	6.9	1.2	5.7
Restructuring of bond issues and related hedges	-	2.7	(2.7)
Total income	**6.9**	**3.9**	**3.0**
TOTAL	**(91.4)**	**(92.6)**	**1.2**

Net financial expenses of €91.4 million are broadly in line with the previous year. They are essentially attributable to the Parent Company (€86.6 million) and reflect €98.3 million in financial expenses and €6.9 million in financial income. The reduction in new financial expenses compared with 2017, amounting to €1.2 million, primarily reflects the following:

- an increase in financial expenses on medium/long-term borrowings and the related hedges (€7.0 million), primarily due to the greater amount of debt in 2018 and rising inflation recorded during the year;
- an increase in capitalised financial expenses (€2.3 million) linked to an increase in the Group's investment during the year;
- an increase in interest income and other financial income (€5.7 million), primarily reflecting an increase in liquidity invested during the year and the improved return on that liquidity;

9. SHARE OF PROFIT/(LOSS) OF INVESTEES ACCOUNTED FOR USING THE EQUITY METHOD - €2.6 MILLION

This item, amounting to €2.6 million, reflects a reduction of €1.2 million compared with last year (€3.8 million), broadly due to the adjustment to the Group's share of equity in the associate CESI (down €1.3 million).

10. INCOME TAX EXPENSE - €296.1 MILLION

(€m)

	2018	2017	CHANGE
Income tax for the year			
Current tax expense:			
- IRES (corporate income tax)	271.4	273.4	(2.0)
- IRAP (regional tax on productive activities)	57.9	60.2	(2.3)
Total current tax expense	***329.3***	***333.6***	***(4.3)***
New temporary differences:			
- deferred tax assets	(18.4)	(27.9)	9.5
- deferred tax liabilities	6.2	0.9	5.3
Reversal of temporary differences:			
- deferred tax assets	27.5	22.8	4.7
- deferred tax liabilities	(32.7)	(31.2)	1.5
Total deferred tax (income)/expense	***(17.4)***	***(35.4)***	***18.0***
Adjustments of taxes for previous years	(15.8)	(3.8)	(12.0)
TOTAL	**296.1**	**294.4**	**1.7**

Current income tax expense of €329.3 million is down €4.3 million compared with the previous year, essentially due to the impact of the tax relief designed to stimulate economic growth (*ACE - Aiuto alla Crescita Economica*), accelerated depreciation applied by the Parent Company and a reduction in non-deductible items for the purposes of IRAP compared with the previous year.

Deferred tax income of €17.4 million is down €18.0 million, primarily linked to the impact on taxation of depreciation and amortisation and the movement in provisions for risks and charges and employee benefits.

Adjustments to taxes for previous years, amounting to €15.8 million, reflect the overpayment of tax in previous years. The change in 2018 (an increase of €12.0 million) is primarily attributable to the Parent Company.

The effective tax charge for the year (€296.1 million) results in a tax rate of 29.4%, compared with a rate of 29.8% for 2017.
For a clearer presentation of the differences between the theoretical and effective tax rates, the table below reconciles the profit before taxes with taxable income for IRES (corporate income tax) purposes.

(€m)

	2018	2017
Profit before tax	1,007.7	988.6
THEORETICAL TAX CHARGE	**241.8**	**237.3**
IRAP	57.9	60.2
Permanent differences	5.9	0.7
Increased taxation paid by overseas companies	**6.3**	**-**
TAX (after adjustment for previous years and one-off changes)	**309.2**	**298.2**
TAX RATE	30.70%	30.20%
Adjustments of taxes for previous years	(15.8)	(3.8)
INCOME TAX EXPENSE FOR THE YEAR	**296.1**	**294.4**
EFFECTIVE TAX RATE	**29.4%**	**29.8%**

11. EARNINGS PER SHARE

Earnings per share, which corresponds to diluted earnings per share, amounts to €0.352 (based on profit for the year attributable to owners of the Parent, totalling €706.6 million, divided by the number of shares outstanding, totalling 2,009,992.0 thousand).

C. Operating segments

In line with the Business Plan 2019-2023, and in compliance with IFRS 8, the Terna Group's identified operating segments are described below:

- **Regulated in Italy**
- **Non-Regulated**
- **International**

The Regulated segment includes the development, operation and maintenance of the National Transmission Grid, in addition to dispatching and metering, and the activities involved in the construction of storage systems. These activities have been included in one operating segment, as they are all regulated by ARERA and have similar characteristics, in terms of the remuneration model and the method for setting the related tariffs.

The Non-regulated segment includes deregulated activities and specific business initiatives, above all relating to the provision of services to third parties in the areas of Energy Solutions, consisting of the development of technical solutions and the supply of innovative services, including EPC (Engineering, Procurement and Construction) services, operation and maintenance of high-voltage and very high-voltage infrastructure, and the supply of energy efficiency services, broadly attributable to the subsidiary, Avvenia The Energy Innovator S.r.l., acquired during the year. This segment also includes Connectivity (support and housing services for fibre networks and IRU contracts for fibre).

This segment also includes the activities carried out in relation to the private interconnectors launched by Law 99/2009, legislation that assigned Terna responsibility for selecting undertakings (the "selected undertakings"), on the basis of public tenders, willing to finance specific interconnectors in exchange for the benefits resulting from a decree granting a third-party access exemption with regard to the transmission capacity provided by the new infrastructure. The Non-regulated segment also includes the operations of the Tamini Group, relating essentially to the construction and commercialisation of electrical equipment, above all power transformers.

On the other hand, the International segment includes the results deriving from opportunities for international expansion, which the Group aims to exploit by leveraging its core competencies developed in Italy as a TSO, where such competencies are of significant importance in its home country. Overseas investment focuses on countries with stable political and regulatory regimes and a need to develop their electricity infrastructure. This segment includes the results of the two Brazilian companies, SPE Santa Lucia Trasmissora de Energia S.A. and SPE Santa Maria Trasmissora de Energia S.A., the Peruvian company Terna Peru S.A.C., the Uruguayan company Difebal S.A. and the Chilean company Terna Chile S.p.A..

(€m)

	2018	2017	CHANGE	% CHANGE
REGULATED REVENUE IN ITALY	1,989.6	1,967.2	22.4	1.1%
NON-REGULATED REVENUE	194.9	189.1	5.8	3.1%
INTERNATIONAL REVENUE*	12.5	6.5	6.0	92.3%
Cost of International Activities	122.1	85.2	36.9	43.3%
TOTAL REVENUE	**2,319.1**	**2,248.0**	**71.1**	**3.2%**
GROSS OPERATING PROFIT (EBITDA)**	**1,650.6**	**1,603.9**	**46.7**	**2.9%**
of which Regulated EBITDA in Italy ***	1,586.5	1,541.7	44.8	2.9%
of which Non-Regulated EBITDA	60.5	62.4	(1.9)	(3.0%)
of which International EBITDA	3.6	(0.2)	3.8	-
Reconciliation of segment result with Group's pre-tax result				
GROSS OPERATING PROFIT (EBITDA)	**1,650.6**	**1,603.9**		
Amortisation. depreciation and impairment losses	554.1	526.5		
OPERATING PROFIT/(LOSS) (EBIT)	**1,096.5**	**1,077.4**		
Financial income/(expenses)	*(91.4)*	*(92.6)*		
Share of profit/(loss) of investees accounted for using the equity method	2.6	3.8		
Profit/(Loss) before tax	**1,007.7**	**988.6**		

* *Relating directly to the margins earned on overseas concessions.*

** *Gross operating profit - EBITDA is an indicator of operating performance, obtained by adding "Amortisation, depreciation and impairment losses" to "Operating profit/(loss) (EBIT)".*

*** *EBITDA including indirect costs.*

The group's revenue for 2018 amounts to €2,319.1 million, an increase of €71.1 million (3.2%) compared with 2017.
Gross operating profit (EBITDA) of €1,650.6 million is up €46.7 million (2.9%) on the €1,603.9 million of 2017.

Regulated EBITDA in Italy amounts to €1,586.5 million for 2018, an increase of €44.8 million compared with the previous year, primarily due to the increase in tariff revenue for dispatching services and a reduction in personnel expenses and other costs.

Non-Regulated EBITDA for 2018 amounts to €60.5 million, a slight decline of €1.9 million, broadly reflecting the accumulated revenue from the private Italy-France Interconnector recognised in 2017, after an increased contribution from the Tamini Group.

International EBITDA for 2018 amounts to €3.6 million, an increase of €3.8 million compared with the previous year. This primarily reflects construction services provided in **Brazil** (up €12.4 million), after the loss incurred on the contract for the construction of a power line in **Uruguay** (down €5.4 million) and an increase in costs incurred in providing **support for overseas initiatives**, totalling €2.2 million, reflecting an increase in the cost of existing contracts and of overseas initiatives.
Information on the financial position periodically reported to senior management is not provided directly on the basis of each individual segment, but based on the measurement and presentation of gross invested capital as a whole, given that the contribution from Non-regulated and International Activities is not material. The following table shows this indicator at 31 December 2018 and 31 December 2017.

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017
Net non-current assets *	14,083.6	13,466.4
of which investments in associates and joint ventures	*76.1*	*77.9*
Net working capital **	(1,822.5)	(1,485.2)
Gross invested capital ***	12,261.1	11,981.2

* *Net non-current assets include the value of "property, plant and equipment", "Goodwill", "Intangible assets", "Investments accounted for using the equity method", "Other non-.current assets" and "Non-current financial assets".*

** *Net working capital is the difference between total current assets less cash and the item, "Current financial assets", and total current liabilities, less the short-term portion of long-term borrowings and the items, "Short-term borrowings" and "Current financial liabilities", and the item, "Other non-current liabilities.*

*** *Gross invested capital is the sum of net non-current assets and net working capital).*

D. Notes to the consolidated statement of financial position

Assets

12. PROPERTY, PLANT AND EQUIPMENT - €13,244.3 MILLION

(€m)

	LAND	BUILDINGS	PLANT AND EQUIPMENT	INDUSTRIAL AND COMMERCIAL EQUIPMENT	OTHER ASSETS	ASSETS UNDER CONST. AND PREPAY-MENTS	TOTAL
COST AT 1 JANUARY 2018	**192,4**	**1,844,7**	**16,830,9**	**100,0**	**145,3**	**1,615,3**	**20,728,6**
Investment	0.5	1.0	5.2	3.4	4.1	1,020.5	1,034.7
Assets entering service	8.5	92.2	621.6	4.6	6.8	(733.7)	-
Contribution of newly acquired companies	-	-	-	0.1	-	-	0.1
Other additions	-	-	1.5	-	-	(1.5)	-
Disposals and impairments	(0.1)	(0.3)	(39.7)	(0.1)	(0.2)	(13.2)	(53.5)
Other movements	(0.1)	(0.8)	(9.4)	-	-	(31.3)	(41.6)
Reclassifications	(0.5)	4.3	0.5	0.1	(0.1)	(1.8)	2.5
COST AT 31 DECEMBER 2018	**200.7**	**1,941.1**	**17,410.6**	**108.1**	**155.9**	**1,854.4**	**21,670.8**
ACCUMULATED DEPRECIATION AND IMPAIRMENTS AT 1 JANUARY 2018	**-**	**(525.9)**	**(7,258.6)**	**(81.5)**	**(109.8)**	**-**	**(7,975.8)**
Depreciation for the year	-	(45.6)	(425.9)	(4.8)	(11.7)	-	(488.0)
Disposals	-	0.2	37.2	-	0.2	-	37.6
Other movements	-	(0.3)	-	-	-	-	(0.3)
ACCUMULATED DEPRECIATION AND IMPAIRMENTS AT 31 DECEMBER 2018	**-**	**(571.6)**	**(7,647.3)**	**(86.3)**	**(121.3)**	**-**	**(8,426.5)**
Carrying amount							
AT 31 DECEMBER 2018	**200.7**	**1,369.5**	**9,763.3**	**21.9**	**34.6**	**1,854.4**	**13,244.3**
AT 31 DECEMBER 2017	**192.4**	**1,318.8**	**9,572.3**	**18.5**	**35.5**	**1,615.3**	**12,752.8**
Change	**8.3**	**50.7**	**191.0**	**3.4**	**(0.9)**	**239.1**	**491.5**

The category, "Plant and equipment" at 31 December 2018 includes the electricity transmission grid and transformer substations in Italy.

"Property, plant and equipment" is up €491.5 million compared with the previous year, reflecting ordinary movements during the year as a result of:

- investment of €1,034.7 million, including €952.0 million invested in the Group's Regulated Activities and €82.7 million in Non-regulated Activities, primarily with regard to the private "Italy-France" Interconnector and other projects;
- depreciation for the year of €488 million;
- other changes during the year, resulting in a reduction of €39.4 million, including grants related to assets (€42.2 million, primarily in relation to projects financed by the Ministry for Economic Development and the EU, and disposals and impairments (€15.9 million).

A summary of movements in property, plant and equipment during the year is shown below.

	(€m)
Investment	
- Power lines	554.6
- Transformer substations	392.1
- Storage systems	1.6
- Other	86.4
Total investment in property, plant and equipment	**1,034.7**
Contribution of newly acquired companies	0.1
Depreciation for the year	(488.0)
Other changes	(39.4)
Disposals and impairments	(15.9)
TOTAL	**491.5**

The following information regards work on the principal projects during the year in relation to Regulated Activities: progress on construction of the various overseas interconnections, consisting of the power lines linking Italy and Montenegro (€64.7 million) and Italy and France (€56.1 million), progress with the "Functional separation" project (€68.4 million), extension of the fibre network as part of the "Fibre for the Grid" project (€42.5 million, including €2.3 million attributable to the subsidiary, Rete S.r.l.), the laying of cables in the Venetian lagoon (€23.6 million), construction of the Sorrento Peninsula interconnector (€17.5 million), restructuring of the grid serving the city of Naples (€16 million), continued work on devices to mitigate the risk of ice and snow (€11.4 million), construction of the Foggia-Benevento II power line (€10.8 million) and the upgrade of power lines in the north-west of the country (€10.7 million).

13. GOODWILL - €230.1 MILLION

Goodwill regards the Parent Company's acquisition of Terna Rete Italia S.r.l. in previous years, accounted for in the financial statements at a carrying amount of €101.6 million, the acquisition of RTL, with a carrying amount of €88.6 million, the acquisition of Rete S.r.l., with a carrying amount of €26.3 million, and the acquisition of TES- Transformer Electro Services within the Tamini Group, with a carrying amount of €13.6 million.

There are no changes in this item compared with the previous year.

Impairment testing

For the purposes of impairment testing, goodwill has been allocated to two cash generating units (CGUs): the first consisting of "Transmission activities" within the Group's Regulated Activities, amounting to €216.5 million, and the second relating to the "Production and commercialisation of transformers", forming part of the Group's Non-regulated Activities, totalling €13.6 million.

Disclosures regarding the impairment testing of the goodwill allocated to the Group's "Transmission" CGU is provided below. Measurement of the recoverable value of the Group's "Transmission" CGU was based on the fair value less costs of disposal. This was determined taking into account Terna's share price at 31 December 2018, appropriately adjusted for the estimated fair value of assets and liabilities not attributable to the CGU that includes transmission activities.

The resulting value is significantly higher than the carrying amount inclusive of goodwill.

14. INTANGIBLE ASSETS - €289.3 MILLION

(€m)

	INFRASTRUCTURE RIGHTS	CONCESSIONS	OTHER ASSETS	ASSETS UNDER DEVELOPMENT AND PREPAYMENTS	TOTAL
Cost	412.1	135.4	271.9	34.6	854.0
Accumulated amortisation	(308.2)	(68.1)	(202.1)	-	(578.4)
BALANCE AT 31 DECEMBER 2017	**103.9**	**67.3**	**69.8**	**34.6**	**275.6**
Investment	1.3	-	0.6	54.5	56.4
Assets entering service	20.0	-	32.0	(52.0)	-
Contribution of newly acquired companies	-	-	17.5	-	17.5
Amortisation for the year	(22.8)	(5.6)	(23.6)	-	(52.0)
Other movements	-	-	0.3	-	0.3
Reclassifications	(1.8)	-	-	-	(1.8)
Disposals and impairments	-	-	(6.7)	-	(6.7)
BALANCE AT 31 DECEMBER 2018	**100.6**	**61.7**	**89.9**	**37.1**	**289.3**
Cost	430.9	135.4	315.6	37.1	919.0
Accumulated amortisation	(330.3)	(73.7)	(225.7)	-	(629.7)
BALANCE AT 31 DECEMBER 2018	**100.6**	**61.7**	**89.9**	**37.1**	**289.3**
Change	**(3.3)**	**(5.6)**	**20.1**	**2.5**	**13.7**

Intangible assets amount to €289.3 million (€275.6 million at 31 December 2017); this item includes:

- the infrastructure used in provision of the dispatching service in Italy and in activities in Peru, carried out under concession and accounted for in accordance with "IFRIC 12 - Service Concession Arrangements". The carrying amount of the former, at 31 December 2018, is €100.6 million, whilst the carrying amount of infrastructure under construction, included in the category "Assets under development and prepayments", is €27.8 million (at 31 December 2017, €103.9 million and €20.3 million, respectively);
- the concession for electricity transmission and dispatching activities in Italy (with a carrying amount of €61.7 million at 31 December 2018); this 25-year concession was recognised in 2005, initially at fair value and subsequently at cost.

Other intangible assets primarily include software applications, either produced internally or purchased as part of systems development programmes. Investment in these assets during the year, primarily attributable to the Parent Company (€26.7 million), essentially regard internal development programmes.

The increase compared with the previous year (up €13.7 million) broadly reflects the net effect of investment (up €56.4 million, including €26.4 million in infrastructure rights), amortisation (down €52.0 million), the contribution resulting from the acquisition of Avvenia the Energy Innovator S.r.l. (up €17.5 million, primarily relating to the company's order book) and disposals and impairments (down €6.7 million).
Investment in intangible assets during the year (€56.4 million, including €51.8 million attributable to the Parent Company's Regulated Activities) included expenditure on the development of software applications for the Remote Management System for Dispatching (€11.2 million), the Power Exchange (€4.1 million), the Metering System (€1 million) and for protection of the electricity system (€2.1 million), as well as software applications and generic licences (€24.6 million).

15. DEFERRED TAX ASSETS - €3.3 MILLION

(€m)

	31 DECEMBER 2017	RESTATEMENT OF OPENING BALANCES	PROVISIONS	USES AND OTHER MOVEMENTS	EFFECTS RECOGNISED IN COMPRE-HENSIVE INCOME	31 DECEMBER 2018
DEFERRED TAX ASSETS						
Provisions for risks and charges	39.1	-	**9.6**	(12.1)	-	**36.6**
Allowance for doubtful accounts	3.2	-	**-**	-	-	**3.2**
Employee benefits	22.2	-	**2.0**	(9.6)	(0.2)	**14.4**
Cash flow hedges	4.0	-	**-**	-	10.6	**14.6**
Tax relief on goodwill	34.4	-	**-**	(5.5)	-	**28.9**
Other	7.8	-	**6.8**	(0.2)	-	**14.4**
Measurement of financial instruments - IFRS 9/15	-	1.4	**-**	(0.2)	(0.2)	**1.0**
TOTAL DEFERRED TAX ASSETS	**110.7**	**1.4**	**18.4**	**(27.6)**	**10.2**	**113.1**
DEFERRED TAX LIABILITIES						
Property. plant and equipment	(114.8)	-	**-**	32.1	-	**(82.7)**
Other	(1.4)	-	**(6.2)**	(16.4)	-	**(24.0)**
Employee benefits and financial instruments	(3.1)	-	**-**	-	-	**(3.1)**
TOTAL DEFERRED TAX LIABILITIES	**(119.3)**	**-**	**(6.2)**	**15.7**	**-**	**(109.8)**
NET DEFERRED TAX ASSETS	**(8.6)**	**1.4**	**12.2**	**(11.9)**	**10.2**	**3.3**

The balance of this item, amounting to €3.3 million, includes the net impact of movements in the Group's deferred tax assets and liabilities.

Deferred tax assets (€113.1 million) are up by a net €2.4 million compared with 31 December 2017 (€110.7 million). These assets underwent the following movements during the year:

- net provisions that did not impact profit or loss, totalling €10.2 million, primarily reflecting the tax effect of movements in cash flow hedges and employee benefits;
- provisions recognised by the subsidiary Rete S.r.l., for the non-deductible portion of book depreciation recognised by the subsidiary (€2.4 million);
- use of the accrued portion recognised in relation to tax relief on the goodwill resulting from the merger of RTL with and into Terna Rete Italia S.r.l. and attributable to the Parent Company (€5.5 million);
- recognition of the net impact of the adjustment to the opening balance due to first-time adoption of the new accounting standards, IFRS 9/15 (€1.4 million).
- net uses of provisions for risks and charges (€2.5 million), primarily reflecting the impact on taxation of releases from the provisions for litigation and disputes (€2.5 million);
- net uses of provisions for employee benefits (€7.8 million).

Deferred tax liabilities (€109.8 million) are down by a net amount of €9.5 million, essentially due to:

- provisions and other net movements of €22.6 million, primarily following the recognition of deferred tax liabilities on the South American contracts;
- the use of previous provisions for accelerated depreciation at the Parent Company, Terna (down €31.1 million).

16. INVESTMENTS ACCOUNTED FOR USING THE EQUITY METHOD - €76.1 MILLION

This item, amounting to €76.1 million, regards the Parent Company's investments in the associate CESI S.p.A. (€49.0 million), the associate CORESO S.A. (€0.4 million) and the associate CGES - CrnoGorski Elektroprenosni Sistem AD (€26.7 million).

The change with respect to the previous year, a reduction of €1.8 million, essentially reflects the reduction in the investment in CGES (down €3.3 million) as a result of the dividend declared at the end of 2018, and an increase in the investment in CESI, totalling €1.4 million, compared with the previous year. The latter movement is due to the adjustment of the value to reflect equity in the same company (€2.5 million) at the end of the year attributable to the Parent Company, after taking into account the dividend collected during the year (down €1.1 million).

17. FINANCIAL ASSETS

(€m)

	MEASUREMENT	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Financial assets under concession	amortised cost	167.8	73.5	94.3
Deposit in the Interconnector Guarantee Fund	amortised cost	61.1	42.2	18.9
Other investments	FVTOCI	0.1	0.1	-
Other non-current financial assets		-	4.3	(4.3)
NON-CURRENT FINANCIAL ASSETS		**229.0**	**120.1**	**108.9**
Government securities	FVTOCI	**402.6**	**-**	**402.6**
Cash flow hedges	Fair value	1.3	-	1.3
Other current financial assets		0.6	0.2	0.4
CURRENT FINANCIAL ASSETS		**404.5**	**0.2**	**404.3**

"Non-current financial assets" are up €108.9 million compared with the previous year, above all reflecting the increase in investment during the year in infrastructure under concession in Brazil, recognised in application of IFRIC 12 (up €94.3 million) and an increase in the Interconnector Guarantee Fund, set up to fund investment in interconnections by art. 32 of Law 99/09 (up €18.9 million).

"Current financial assets" are up €404.3 million compared with the previous year, primarily following the purchase of government securities for €400 million, maturing in December 2019 (€402.6 million) and the recognition of a foreign currency derivative (€1.3 million) entered into to hedge exchange rate differences linked to overseas activities.

18. OTHER ASSETS

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Loans and advances to employees	9.4	9.3	0.1
Deposits with third parties	5.4	4.9	0.5
OTHER NON-CURRENT ASSETS	**14.8**	**14.2**	**0.6**
Other tax credits	44.1	76.8	(32.7)
Amounts due from associates	3.3	-	3.3
Prepayments to suppliers	13.4	35.1	(21.7)
Prepayments of operating expenses and accrued operating income	14.7	18.5	(3.8)
Amounts due from partners selected for Interconnector projects	4.0	4.1	(0.1)
Amounts due from others	6.5	4.6	1.9
OTHER CURRENT ASSETS	**86.0**	**139.1**	**(53.1)**

"Other non-current assets" amount to €14.8 million. substantially in line with the previous year (up €0.6 million, primarily due to amounts deposited with third parties).

"Other current assets", totalling €86.0 million, are down €53.1 million compared with 31 December 2017, primarily reflecting:

- other tax credits (down €32.7 million), primarily reflecting a decrease in the Group's refundable VAT (down €33.4 million), due to higher payments on account in the previous year as a result of the Ministerial Decree of 27 June 2017;
- a reduction in prepayments to suppliers (down €21.7 million), mainly due to the prepayments made in 2017 for work carried out in South America that began in the previous year (down €22.8 million);
- a reduction in expenses already paid for but accruing after 31 December 2018 (down €3.8 million), primarily due to decreases in the prepayment of costs relating to supply of the cable for the new Sardinia-Corsica-Italy - SACOI III connection (down €2.7 million) and in insurance premiums (down €1.1 million);
- the recognition of amounts due from the associate, CGES (up €3.3 million) as a result of the dividend declared at the end of the year;
- amounts due from others (up €1.9 million), broadly reflecting the subscription for shares in Avvenia the Energy Innovator S.r.l. (€1.3 million) and yet to be settled.

19. INVENTORIES - €15.2 MILLION

This item, amounting to €15.2 million, is broadly in line with the previous year (up €0.4 million) and primarily consists of materials and equipment for use in the operation, maintenance and construction of plant and in contract work carried out by the Tamini Group.

20. TRADE RECEIVABLES - €1,189.7 MILLION

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Energy-related receivables	743.7	772.8	(29.1)
Transmission charges receivable	310.8	312.2	(1.4)
Other trade receivables	135.2	180.9	(45.7)
TOTAL	**1,189.7**	**1,265.9**	**(76.2)**

Trade receivables amount to €1,189.7 million at 31 December 2018 and are accounted for less any losses on items deemed not to be recoverable and recognised in the allowance for doubtful accounts (€26.1 million for energy-related receivables and €17.8 million for other items in 2018, compared with €26.9 million for energy-related items and €17.2 million for other items in 2017). The carrying amount shown broadly approximates to fair value.

Energy-related/regulated receivables - €743.7 million

This item includes so-called "pass-through items" relating to the Parent Company's activities in accordance with Resolution 111/06 (€715 million) and receivables due from the users of dispatching services forming part of Regulated Activities (€13.9 million). It also includes the amount due from the Fund for Energy and Environmental Services (Cassa per i Servizi Energetici e Ambientali - CSEA), based on the RENS performance for the year (€14.8 million).

The balance is down €29.1 million overall compared with the previous year, essentially due to energy-related pass-through receivables (down €30.9 million), following a reduction of €68.9 million in the uplift, reflecting the reduction in net costs to be recovered linked to both the Dispatching Services Market (DSM) and to imbalances (the related receivables are up €32.2 and €20.3 million, respectively). The change also reflects the reduction in amounts due from the users of dispatching services in relation to the interruptibility service (€41.6 million), partly offset by amounts due from CSEA guaranteeing full coverage of the cost of this service (€28.3 million).

Transmission charges receivable - €310.8 million

Transmission charges receivable, amounting to €310.8 million, represent the amount due to the Parent Company and other grid owners from electricity distributors for use of the National Transmission Grid. The receivable is down €1.4 million compared with 31 December 2017, primarily due to the mechanism for recovering one-off payments recognised in 2017 for the early effect of the tariff adjustment linked to investment.

Other trade receivables - €135.2 million

Other trade receivables primarily regard amounts receivable from customers of the Non-Regulated business. These amounts derive from the provision of specialist services to third parties, primarily in relation to plant engineering services, the operation and maintenance of high-voltage and very high-voltage infrastructure, and the housing of telecommunications equipment and maintenance services for fibre networks, as well as in relation to the Tamini Group's contract work.

The balance is down €45.7 million compared with the previous year, broadly due to the recognition of receivables due from Piemonte Savoia S.r.l. at the end of 2017 for construction work following the achievement of contract milestones (€49.3 million), which were collected in January 2018.

The following table shows receivables resulting from contract work in progress (€107.3 million), being carried out by the Group under multi-year contracts with third parties:

(€m)

	PREPAYMENTS	VALUE OF CONTRACT	BALANCE AT 31 DECEMBER 2018	PREPAYMENTS	VALUE OF CONTRACT	BALANCE AT 31 DECEMBER 2017
Receivables resulting from contract work in progress	(36.2)	143.5	**107.3**	(23.6)	60.5	**36.9**

The Group's receivables resulting from contract work in progress are up €70.4 million on the previous year, primarily in relation to the contract in Uruguay (up €40.3 million) and an increase in contract work at the Tamini Group (up €29.1 million).

Bank guarantees given to third parties in the interest of Group companies at 31 December 2018 total €272.3 million. These break down as follows: €104.1 million in the interests of Terna S.p.A., €39.2 million in the interests of Terna Interconnector S.r.l., €43.5 million in the interests of Terna Rete Italia S.p.A., €9.5 million in the interests of Terna Plus S.r.l., €11.2 million in the interests of Difebal S.A., €3.4 million in the interests of Rete S.r.l., €1.5 million in the interests of Terna Energy Solutions S.r.l. and €59.9 million in the interests of Tamini Trasformatori S.r.l..

21. CASH AND CASH EQUIVALENTS - €1,328.9 MILLION

Cash amounts to €1,328.9 million at 31 December 2018, including €751.5 million invested short-term, readily convertible deposits and €577.2 million deposited in bank current accounts.

22. INCOME TAX ASSETS - €19.3 MILLION

Income tax assets, amounting to €19.3 million, are down €17.6 million compared with the previous year, essentially reflecting the assets recognised at the end of 2017 compared with the liabilities recognised at 31 December 2018 in "Tax liabilities". This reflects higher payments on account made in the previous year (determined on the basis of a higher rate of IRES applied in 2016) and an increase in tax payable for the period (essentially due to the increase in pre-tax profit).

Equity and liabilities

23. EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT - €4,019.2 MILLION

Share capital - €442.2 million

The Parent Company's share capital consists of 2,009,992,000 ordinary shares with a par value of €0.22 per share.

Legal reserve - €88.4 million

The legal reserve accounts for 20% of the Parent Company's share capital.

Other reserves - €700.1 million

The other reserves have decreased by €31.9 million compared with the previous year, primarily as a result of other comprehensive income. This reflects:

- fair value adjustments to the Parent Company's cash flow hedges (down €32.1 million, taking into account the related tax asset of €10.1 million);
- the recognition of actuarial gains and losses on provisions for employee benefits (a gain of €0.9 million, taking into account the related tax liability of €0.3 million).

Retained earnings and accumulated losses - €2,240.1 million

The increase in "Retained earnings and accumulated losses", amounting to €238.4 million, primarily regards the remaining portion of the Group's profit for 2017, following the Parent Company's payment of the dividend for 2017 (totalling €442.2 million).

Interim dividend for 2018

On 9 November 2018, the Parent Company's Board of Directors, having obtained the Independent Auditor's opinion required by article 2433-*bis* of the Italian Civil Code, decided to pay an interim dividend of €0.0787 per share, amounting to a total payout of €158.2 million. The dividend was payable from 21 November 2018, with an ex-dividend date for coupon 29 of 19 November 2018.

Equity attributable to non-controlling interests

Equity attributable to non-controlling interests, relating to the non-controlling shareholders of the Tamini Group, Terna Interconnector S.r.l. and Avvenia The Energy Innovator S.r.l. (consolidated for the first time during the year), amounts to €35.0 million, an increase of €9.3 million compared with 31 December 2017.

This change primarily reflects the profit reported by Terna Interconnector S.r.l. (€6.0 million) and the contribution from Avvenia (€4.9 million).

24. BORROWINGS AND FINANCIAL LIABILITIES

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Bond issues	6,563.2	6,541.9	21.3
Bank borrowings	1,664.4	2,129.7	(465.3)
LONG-TERM BORROWINGS	**8,227.6**	**8,671.6**	**(444.0)**
Cash flow hedges	59.2	10.5	48.7
NON-CURRENT FINANCIAL LIABILITIES	**59.2**	**10.5**	**48.7**
SHORT-TERM BORROWINGS	**25.0**	**118.0**	**(93.0)**
Bond issues	616.7	749.9	(133.2)
Bank borrowings	613.9	134.4	479.5
CURRENT PORTION OF LONG-TERM BORROWINGS	**1,230.6**	**884.3**	**346.3**
TOTAL	**9,542.4**	**9,684.4**	**(142.0)**

Borrowings and financial liabilities are down €142.0 million compared with the previous year to €9,542.4 million.

The reduction in bond issues (down €111.9 million) is due to the adjustment to these instruments to reflect their amortised cost. The balance also reflects the repayment of bonds issued on 16 October 2012, totalling €750 million and the green bond issue of 23 July 2018 (€750 million).

The latest official prices at 31 December 2018 and 31 December 2017 for the bonds listed on the Luxembourg Stock Exchange are detailed below:

(€)

	PRICE AT 31 DECEMBER 2018	PRICE AT 31 DECEMBER 2017
bond maturity 2024:	120.51	128.98
bond maturity 2023:	127.61*	135.46
bond maturity 2019:	103.62	108.74
bond maturity 2026:	103.52	102.85
bond maturity 2021:	109.79	114.80
bond maturity 2022:	100.64	102.50
bond maturity 2028:	89.83	96.16
bond maturity 2027:	94.53	100.51
bond maturity 2018:	-	100.38
bond maturity 2023 (Green Bond):	100.17	-

** Source: BNP Paribas, in the absence of up-to-date prices sourced from Reuters and Bloomberg.*

Compared to the previous year, bank borrowings have increased by €14.2 million, due mainly to the following:
- drawdowns on new loans of €152.8 million;
- repayments made to the EIB at maturity and on outstanding leases, totalling €134.1 million.

Long-term borrowings

(€m)

	MATURITY	AT 31 DECEMBER 2017	AT 31 DECEMBER 2018*	PORTION FALLING DUE WITHIN 12 MONTHS	PORTION FALLING DUE AFTER 12 MONTHS	2020	2021	2022	2023	2024	BEYOND	COUPON INTEREST	AVERAGE NET INTEREST RATE ON HEDGES AT 31 DECEMBER 2018
Bonds	2024	1,013.4	982.9		982.9		-	-	-	982.9	-	4.90%	0.86%
IL bonds	2023	692.9	679.2		679.2		-	-	679.2	-	-	2.73%	0.30%
PP bonds	2019	638.7	616.7	616.7			-	-	-	-	-	4.88%	1.14%
PP bonds	2026	78.8	78.9		78.9		-	-	-	-	78.9	1.60%	1.79%
1250 bonds	2021	1,388.7	1,345.9		1,345.9		1,345.9	-		-	-	4.75%	1.20%
1000 bonds	2022	996.8	997.6		997.6		-	997.6	-	-	-	0.88%	0.95%
750 bonds	2018	749.9	-				-	-	-	-	-	2.88%	2.99%
750 bonds	2028	740.1	740.9		740.9		-	-	-	-	740.9	1.00%	1.19%
1000 bonds	2027	992.5	993.2		993.2		-	-	-	-	993.2	1.38%	1.45%
750 bonds	2023	-	744.6		744.6		-	-	744.6	-		0.00%	1.16%
EIB	2039	238.6	368.6		368.6		-	4.6	20.5	20.5	323.0	1.44%	1.44%
Total fixed rate		**7,530.4**	**7,548.5**	**616.7**	**6,931.8**	**-**	**1,345.9**	**1,002.2**	**1,444.3**	**1,003.4**	**2,136.0**		
EIB	2030	1,488.3	1,355.9	111.3	1,244.6	116.1	116.7	128.6	112.7	112.7	657.8	0.25%	1.12%
CDP	2019	500.0	500.0	500.0	-	-	-	-	-	-	-	0.93%	1.04%
Difebal borrowing	2034	32.6	56.9	0.6	56.3	1.9	2.5	2.7	3.0	3.3	42.9	6.48%	6.93%
Leases	2019-2021-2222	4.6	2.4	2.0	0.4	0.3	0.1	-	-	0.1	(0.8)	0.88%	0.88%
Total variable rate		**2,025.5**	**1,915.2**	**613.9**	**1,301.3**	**118.3**	**119.3**	**131.3**	**115.7**	**116.0**	**700.7**		
TOTAL		**9,555.9**	**9,463.7**	**1,230.6**	**8,233.1**	**118.3**	**1,465.2**	**1,133.5**	**1,560.0**	**1,119.4**	**2,836.7**		

** The balance does not include fees of €5.5 million.*

At 31 December 2018, the Terna Group's borrowings amount to €9,458.2 million (€1,230.6 million maturing within 12 months and €8,227.6 million maturing after 12 months), of which €2,836.7 million maturing after five years.

The table below shows movements in long-term debt during the year, including also the nominal amount:

(€m)

	AT 31 DECEMBER 2017			REPAYMENTS AND CAPITALISATIONS	DRAWDOWNS	OTHER	CHANGE IN CARRYING AMOUNT	AT 31 DECEMBER 2018		
	NOMINAL DEBT	CARRYING AMOUNT	FAIR VALUE					NOMINAL DEBT	CARRYING AMOUNT	FAIR VALUE
Bonds maturing 2024	800.0	1,013.4	1,031.8	-	-	(30.5)	(30.5)	800.0	982.9	964.1
IL bonds	570.5	692.9	677.3	-	-	(13.7)	(13.7)	579.0	679.2	638.1
Private Placement 2019	600.0	638.7	652.4	-	-	(22.0)	(22.0)	600.0	616.7	621.7
Private Placement 2026	80.0	78.8	82.3	-	-	0.1	0.1	80.0	78.9	82.8
Bonds maturing 2021	1,250.0	1,388.7	1,435.0	-	-	(42.8)	(42.8)	1,250.0	1,345.9	1,372.4
Bonds maturing 2022	1,000.0	996.8	1,025.0	-	-	0.8	0.8	1,000.0	997.6	1,006.4
Bonds maturing 2018	750.0	749.9	752.8	(750.0)	-	0.1	(749.9)	-	-	-
Bonds maturing 2028	750.0	740.1	721.2	-	-	0.8	0.8	750.0	740.9	673.7
Bonds maturing 2027	1,000.0	992.5	1,005.2	-	-	0.7	0.7	1,000.0	993.2	945.3
Bonds maturing 2023	-	-	-	-	750.0	(5.4)	744.6	750.0	744.6	751.3
Total bond issues	**6,800.5**	**7,291.8**	**7,383.0**	**(750.0)**	**750.0**	**(111.9)**	**(111.9)**	**6,809.0**	**7,179.9**	**7,055.8**
Bank borrowings	2,265.5	2,264.1	2,270.4	(134.1)	152.8	(4.5)	14.2	2,285.3	2,278.3	2,301.2
Total borrowings	**2,265.5**	**2,264.1**	**2,270.4**	**(134.1)**	**152.8**	**(4.5)**	**14.2**	**2,285.3**	**2,278.3**	**2,301.2**
Total debt	**9,066.0**	**9,555.9**	**9,653.4**	**(884.1)**	**902.8**	**(116.4)**	**(97.7)**	**9,094.3**	**9,458.2**	**9,357.0**

At 31 December 2018, the Group has access to additional financing of €2,450.0 million, represented by three revolving credit facilities entered into in December 2015, July 2016 and September 2018. In addition, the Group has uncommitted bank credit lines totalling approximately €806 million and approximately €59 million in loans agreed but not yet disbursed.

In addition, as provided for in IFRS 7, the table shows the fair value of borrowings and bond issues. In the case of bond issues, this is market value based on prices at the reporting date, whilst variable rate loans are measured by discounting expected cash flows based on the market interest rate curve at the reporting date.

Non-current financial liabilities

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Cash flow hedges	59.2	10.5	48.7
TOTAL	**59.2**	**10.5**	**48.7**

Non-current financial liabilities, amounting to €59.2 million, reflect the fair value of cash flow hedges at 31 December 2018.

Fair value was measured by discounting the expected cash flows using the market yield curve at the reporting date. The increase of €48.7 million compared with 31 December 2017 reflects the change in the market interest rate curve and the change in the notional value of the derivatives portfolio.

Short-term borrowings - €25.0 million

Short-term borrowings are down €93 million compared with the previous year due to the repayment of facilities used primarily by the Parent Company.

Current financial liabilities

Current financial liabilities at 31 December 2018 include the value of net interest expense accrued on financial instruments and not yet paid. This item is down €15.3 million compared with the previous year.

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
DEFERRED LIABILITIES ON:			
Hedging derivatives	2.3	1.8	0.5
Bond issues	85.9	101.9	(16.0)
Borrowings	2.2	2.0	0.2
TOTAL	**90.4**	**105.7**	**(15.3)**

Net debt

Pursuant to the CONSOB Communication of 28 July 2006 and in compliance with Recommendation ESMA no. 319 of 2013, the Group's net debt is as follows:

(€m)

	31 DECEMBER 2018
A. Cash	577.4
B. Term deposits	751.5
C. Cash and cash equivalents (A) + (B)	**1,328.9**
D. Current portion of non-current borrowings	1,230.6
of which from related parties	*500.0*
E. Short-term borrowings	25.0
F. Other net financial liabilities	89.8
of which from related parties	*0.5*
G. Current financial assets	403.9
H. Current debt (D+E+F)	**941.5**
I. Current net debt (G) - (C)	**(387.4)**
J. Non-current borrowings	1,664.4
K. Bond issues	6,563.2
L. Derivative financial instruments held in portfolio	59.2
M. Non-current net debt (I) + (J) + (K)	**8,286.8**
N. Net debt (H) + (L)	**7,899.4**

Default risk and debt covenants

This risk is associated with the possibility that the loan agreements or bond terms and conditions to which the Group is a party may contain provisions that, if certain events occur, authorise counterparties to call in such loans immediately, thereby generating liquidity risk.

Certain long-term loans obtained by the Parent Company, Terna S.p.A., contain covenants that are typical of international practice. The principal covenants relate to:

- the Company's bond issues, which consist of an €800.0 million issue in 2004 and eight issues as part of its EMTN Programme (the "€ 8,000,000,000 Medium Term Notes Programme"), totalling €6,009 million;
- bank borrowings, consisting of three revolving line of credit of €800 million, €500 million and €1,150 million, ("bank debt");
- a series of loans to the Company from the European Investment Bank (EIB), amounting to a total of €2,225 million;
- project financing, totalling approximately €57 million, to fund the development transmission infrastructure in Brazil and Uruguay, where the Group operates through the operators SPE Santa Maria Transmissora de Energia S.A. and SPE Santa Lucia Transmissora de Energia S.A. (Brazil) and Difebal S.A. (Uruguay).

The main covenants relating to the bond issues and the EMTN Programme involve clauses regarding i) "negative pledges", on the basis of which the Issuer or its Relevant Subsidiaries undertake not to create or maintain mortgages, pledges or other encumbrances on their assets or revenue, to guarantee listed bonds (with the exception of certain "permitted guarantees"); ii) "pari passu", on the basis of which the securities constitute a direct, unconditional and unsecured obligation by the Issuer, ranking equally among them and with at least the same level of seniority as other present and future unsecured and non- subordinated borrowings of the Issuer; iii) "event of default", on the basis of which if certain predetermined events occur (e.g., failure to make a repayment, the liquidation of the Issuer, the breach of contractual obligations, a cross-default, etc.) a situation of default is established and the loan is immediately called in.

The main covenants relating to bank borrowings involve clauses related to i) negative pledges, on the basis of which the Issuer or the Relevant Subsidiaries undertake not to create or maintain guarantees on their assets to secure borrowings, with the exception of "permitted guarantees"; ii) "pari passu" on the basis of which the Borrower's payment obligations in relation to the loan agreements in question are not subordinated to any obligation related to other unsecured and non-subordinated creditors, without prejudice to privileges under the law; iii) "event of default", on the basis of which if certain predetermined events occur (e.g. failure to make a repayment, serious inaccuracies in documents and/or declarations, insolvency, business discontinuation, substantially prejudicial effects, the breach of contractual obligations, including pari passu conditions, a cross-default, etc.) a situation of default is established and the loan is immediately called in; iv) accelerated repayment should the rating fall below investment grade (BBB-) for the majority of rating agencies or should the Company cease to be rated by all the agencies.

The main covenants related to the EIB loans involve clauses related to i) negative pledges, on the basis of which the Company cannot create encumbrances, with the exception of encumbrances granted in relation to borrowings below given amounts and under contractually specified circumstances; ii) the provision to the Bank, at its request, of new guarantees should ratings below BBB+/Baa1 be assigned by two ratings agencies out of three, or in the event that all of the agencies cease to publish ratings; iii) "*pari passu*", on the basis of which the Company ensures that payment obligations rank equally with those related to all other unsecured, non-subordinated creditors; iv) cases of contract termination/application of the call provision/withdrawal (e.g. failure to make a repayment, serious inaccuracies in documents and/or declarations, insolvency, events that have a negative impact on financial commitments made by the Company, extraordinary administration, liquidation, substantial prejudicial changes, the breach of contractual commitments, etc.); v) accelerated loan payment following the occurrence of given events (e.g. change of control over the Company, loss of the concession, extraordinary corporate events, etc.).

The main covenants related to the project financing involve clauses related to i) 'securities' by which the companies undertake to pledge and to continue to pledge shares in the companies and/or their assets to the lenders throughout the terms to maturity of the loans, ii) limitations and/or restrictions on payments and on the distribution of profit until certain conditions have been met, such as completion of a certain number of repayments and/or the fact that financial ratios have remained above certain minimum thresholds, and ii) "*event of default*", on the basis of which if certain predetermined events occur (e.g. failure to make a repayment, serious inaccuracies in declarations, insolvency, the cessation of operations, etc.) a situation of default is established and the loan is immediately called in.

To date, no covenant has been breached.

25. EMPLOYEE BENEFITS - €69.4 MILLION

The Group provides its employees with benefits during their period of employment (loyalty bonuses), on termination of employment (*TFR*, additional months' pay and payment in lieu of notice) and after termination in the form of post-employment benefits (ASEM health cover).
Loyalty bonuses are payable to the Group's employees and senior managers once certain requirements have been met regarding length of service (on completing 25 and 35 years of service).
Termination benefits (*TFR*) are payable to all employees, whilst employees hired by 30 June 1996 receive energy discounts, senior managers recruited or appointed before 28 February 1999 receive payment in lieu of notice and employees (blue-collar workers, office staff and middle managers) employed prior to 24 July 2001 are due additional months' pay on termination.
Post-employment benefits consist of a form of supplementary health cover in addition to that provided by the Italian national health service, as provided for in the national collective contract for industrial managers (the ASEM health plan).

The following table shows the composition of provisions for TFR and other employee benefits and movements during the year ended 31 December 2018.

(€m)

	31 DECEMBER 2017	PROVISIONS	INTEREST COST	USES AND OTHER MOVEMENTS	ACTUARIAL GAINS/ (LOSSES)	31 DECEMBER 2018
Benefits during the period of employment						
Loyalty bonuses	4.6	0.2	0.1	(0.2)	-	4.7
Total	**4.6**	**0.2**	**0.1**	**(0.2)**	**-**	**4.7**
Termination benefits						
Deferred compensation benefits (*TFR*)	46.4	-	0.4	(2.1)	(1.0)	43.7
Energy discounts	13.0	0.4	0.1	(8.3)	0.1	5.3
Additional months' pay	7.1	0.2	-	(0.3)	(0.1)	6.9
Payment in lieu of notice and other similar	0.3	-	-	(0.1)	-	0.2
Total	**66.8**	**0.6**	**0.5**	**(10.8)**	**(1.0)**	**56.1**
Post-employment benefits						
ASEM health plan	9.3	0.3	0.1	(0.9)	(0.2)	8.6
Total	**9.3**	**0.3**	**0.1**	**(0.9)**	**(0.2)**	**8.6**
TOTAL	**80.7**	**1.1**	**0.7**	**(11.9)**	**(1.2)**	**69.4**

This item, amounting to €69.4 million at 31 December 2018, is down €11.3 million compared with the previous year, attributable primarily to the release of provisions for the energy discounts (down €8.3 million) due to changes to the plan and use of provisions for TFR (down €2.1 million), essentially in relation to generational turnover.

The following table shows the current service cost and interest income and expense.

(€m)

	LOYALTY BONUSES	TFR	ADDITIONAL MONTHS' PAY	PAYMENT IN LIEU OF NOTICE AND OTHER SIMILAR	ENERGY DISCOUNTS	ASEM HEALTH COVER	TOTAL
Net impact recognised in profit or loss							
- current service cost	0.2	-	0.2	-	0.4	0.3	**1.1**
- curtailment (revenue) and other costs	-	-	-	(0.1)	(8.2)	(0.7)	**(9.0)**
- interest income and expense	0.1	0.4	-	-	0.1	0.1	**0.7**
TOTAL RECOGNISED IN PROFIT OR LOSS	**0.3**	**0.4**	**0.2**	**(0.1)**	**(7.7)**	**(0.3)**	**(7.2)**

Revaluation of the net liability for employee benefits is shown in the following table, which provides details of the type of actuarial gain or loss recognised in other comprehensive income.

(€m)

	TFR	ADDITIONAL MONTHS' PAY	PAYMENT IN LIEU OF NOTICE AND OTHER SIMILAR	ENERGY DISCOUNTS	ASEM HEALTH COVER	TOTAL
Actuarial gain/losses						
- based on past experience	-	-	-	-	(0.1)	**(0.1)**
- due to changes in demographic assumptions	-	-	-	-	-	-
- due to changes in other economic assumptions	-	0.2	-	-	0.1	0.3
- due to changes in discount rate	(1.0)	(0.3)	-	0.1	(0.2)	**(1.4)**
TOTAL IMPACT ON OTHER COMPREHENSIVE INCOME	**(1.0)**	**(0.1)**	**-**	**0.1**	**(0.2)**	**(1.2)**

Finally, the following tables show the main actuarial assumptions applied, a sensitivity analysis of movements in the assumptions and the payment schedule for the plan. In line with 2017, the interest rate used to determine the present value of the obligation was calculated on the basis of the yield on the Iboxx Eurozone Corporates AA index at 31 December 2018, matching the duration of the relevant group of plan participants.

	LOYALTY BONUSES	*TFR*	ADDITIONAL MONTHS' PAY	PAYMENT IN LIEU OF NOTICE AND OTHER SIMILAR	ENERGY DISCOUNTS	ASEM HEALTH COVER
Discount rate	1.56%	1.16%	0.77%	0.43%	1.13%	1.57%
Inflation rate	1.50%	1.50%	0.00%	1.50%	1.50%	3.00%
Duration (in years)	10.6-12.3	9.1-27.2	5.2-5.8	4.48	5.3-9.1	9.6-17.5

(€m)

	LOYALTY BONUSES	*TFR*	ADDITIONAL MONTHS' PAY	PAYMENT IN LIEU OF NOTICE AND OTHER SIMILAR	ENERGY DISCOUNTS	ASEM HEALTH COVER	TOTAL
Discount rate +0.25%	4.7	43.0	6.7	0.2	5.1	8.5	**68.2**
Discount rate -0.25%	4.6	45.0	6.9	0.2	5.3	8.9	**70.8**
Inflation rate +0.25%	4.6	44.7	n/a	n/a	n/a	n/a	**49.3**
Inflation rate -0.25%	4.7	43.3	n/a	n/a	n/a	n/a	**48.0**
Annual rate of increase in health costs +3%	n/a	n/a	n/a	n/a	n/a	12.5	**12.5**
Annual rate of increase in health costs -3%	n/a	n/a	n/a	n/a	n/a	7.0	**7.0**
Conversion rate for KW/h +5%	n/a	n/a	n/a	n/a	n/a	n/a	**-**
Conversion rate for KW/h -5%	n/a	n/a	n/a	n/a	n/a	n/a	**-**

(€m)

	LOYALTY BONUSES	*TFR*	ADDITIONAL MONTHS' PAY	PAYMENT IN LIEU OF NOTICE AND OTHER SIMILAR	ENERGY DISCOUNTS	ASEM HEALTH COVER	TOTAL
By the end of 2019	0.3	2.3	1.9	-	0.4	0.2	**5.1**
By the end of 2020	0.4	2.6	0.7	-	0.5	0.2	**4.4**
By the end of 2021	0.5	2.6	0.8	-	0.6	0.2	**4.7**
By the end of 2022	0.3	3.4	0.6	-	0.7	0.3	**5.3**
By the end of 2023	0.2	3.0	0.5	-	0.7	0.3	**4.7**
After 5 years	3.0	29.8	2.4	0.2	2.4	7.4	**45.2**
TOTAL	**4.7**	**43.7**	**6.9**	**0.2**	**5.3**	**8.6**	**69.4**

26. PROVISIONS FOR RISK AND CHARGES - €241.4 MILLION

(€m)

	PROVISIONS FOR LITIGATION AND DISPUTES	PROVISIONS FOR SUNDRY RISKS AND CHARGES	PROVISIONS FOR EARLY RETIREMENT INCENTIVES	TOTAL
Amount at 31 December 2017	**23.9**	**179.6**	**63.0**	**266.5**
New provisions	3.9	37.8	-	41.7
Uses and other movements	(8.8)	(48.5)	(9.6)	(66.9)
Restatement of opening balances	-	0.1	-	0.1
Amount at 31 December 2018	**19.0**	**169.0**	**53.4**	**241.4**

Provisions for litigation and disputes - 19.0 million

These provisions, set aside to cover outstanding liabilities that, at the end of the year, could result from court judgements and out-of-court settlements regarding the activities of Group companies, have been assessed partly on the basis of recommendations from internal and external legal advisors. The provisions are down €4.9 million compared with the previous year, reflecting an increase in net uses during the year following positive outcomes to a number of disputes arising in previous years.

Provisions for sundry risks and charges - €169.0 million

These provisions are down €10.6 million compared with the previous year, reflecting:

- net provisions for staff incentive plans, totalling €10.9 million;
- a net decrease of €7.3 million due to the higher value of provisions made in the previous year for urban and environmental redevelopment schemes;
- a reduction of €6.6 million following the payment, by ARERA, of expenses not covered by the transmission and dispatching charges;
- a reduction of €3.9 million due to an adjustment to the provisions for taxation;
- a net reduction of €3.1 million in provisions linked to regulation of the quality of the electricity service (the mitigation and sharing mechanism introduced by ARERA Resolution 653/2015/R/eel) which, after provisions for estimated penalties linked to outages during the year, reflects payments to distribution companies and releases following final determination of the penalties due to previous years.

Provisions for early retirement incentives - €53.4 million

Provisions for early retirement incentives reflects the estimated extraordinary expenses to be incurred in relation to the cost of the scheme for the year, linked to the early retirement of Group employees who have reached pensionable age. This item has decreased by a net €9.6 million, reflecting payments during the year in relation to the existing plan for generational turnover.

27. OTHER NON-CURRENT LIABILITIES - €373.8 MILLION

This item, amounting to €373.8 million at 31 December 2018, regards accrued grants related to assets receivable by the Parent Company (€90.9 million), in addition to payments on account received in relation to construction of the Italy-France Interconnector (€217.6 million).

This item also includes the Interconnector Guarantee Fund set up by Terna S.p.A. following the issue of the 2016 Stability Law (€65.2 million), in order to fund investment in interconnections by art. 32 of Law 99/09.

The increase in this item compared with the previous year, amounting to €122.8 million, essentially reflects the recognition of payments on account received from the entities financing the Italy-France Interconnector (up €106.1 million) and reflects the recognition of payments on account received from the entities financing the Italy-France Interconnector (up €21.9 million).

28. CURRENT LIABILITIES

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Short-term borrowings *	25.0	118.0	(93.0)
Current portion of long-term borrowings *	1,230.6	884.3	346.3
Trade payables	2,514.1	2,497.9	16.2
Tax liabilities	5.1	-	5.1
Current financial liabilities *	90.4	105.7	(15.3)
Other current liabilities	239.7	193.0	46.7
TOTAL	**4,104.9**	**3,798.9**	**306.0**

** Information on these items is provided in note 24, "Borrowings and financial liabilities.*

TRADE PAYABLES - €2,514.1 MILLION

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Suppliers:			
- Energy-related payables	1,518.1	1,602.6	(84.5)
- Non-energy-related payables	978.9	874.4	104.5
Amounts due to associates	8.2	14.9	(6.7)
Payables resulting from contract work in progress	8.9	6.0	2.9
TOTAL	**2,514.1**	**2,497.9**	**16.2**

Suppliers

Energy-related/regulated payables - €1,518.1 million

The reduction of €84.5 million in this item compared with the previous year essentially reflects energy-related pass-through payables (down €106 million). This is primarily due to:

- payables related to provision of the dispatching service (down €81 million), primarily due to a significant reduction during the year in the cost of both demand- and supply-side imbalances;
- payables linked to plants that are essential for the security of the electricity system - *UESS* (down €113.9 million), reflecting increased payments at the end of the year;
- amounts due from final customers linked to the interruptibility service (down €24.7 million) and amounts due to the Fund for Energy and Environmental Services (*Cassa per i Servizi Energetici e Ambientali* - CSEA) to cover the cost of the protection service (down €12.6 million);

in part offset by

- payables relating to capacity payments (up €124.7 million), the increase reflecting the cost of the capacity obtained after one single payment made during the year (in accordance with ARERA Resolution 248/2018).

The change also reflects the payable (€22.2 million) resulting from the difference between the amount collected from CSEA for the RENS bonus for 2016 and the related receivable recognised in the financial statements, calculated on a pro-rata basis taking into account the overall results expected in the regulatory period 2016-2019.

Non-energy-related payables

The exposure to suppliers regards invoices received and to be received for contract work, services and purchases of materials and equipment.

The balance at 31 December 2018 (€978.9 million) is up €104.5 million on the previous year, largely due to increased capital expenditure towards the end of the year.

Amounts due to associates

This item, amounting to €8.2 million, is down €6.7 million on the previous year and regards amounts payable to the associate CESI S.p.A., for services provided primarily to the Parent Company (€0.8 million) and to the subsidiary Terna Rete Italia S.p.A. (€7.0 million), relating to electro technical studies and research.

Payables resulting from contract work in progress

Payables resulting from contract work in progress, amounting to €8.9 million at 31 December 2018, are up €2.9 million on the figure for 31 December 2017 (€6.0 million), essentially due to a reduction in amounts payable on contract work at the Tamini Group (€2.0 million).
This item breaks down as follows.

(€m)

	PREPAY-MENTS	VALUE OF CONTRACT	BALANCE AT 31 DECEMBER 2018	PREPAY-MENTS	VALUE OF CONTRACT	BALANCE AT 31 DECEMBER 2017
Payables resulting from contract work in progress	(23.7)	14.8	**(8.9)**	(19.0)	13.0	**(6.0)**

The carrying amount of trade payables broadly approximates to fair value.
The commitments assumed by the Group towards suppliers amount to approximately €3,428.9 million and regard purchase commitments linked to the normal "operating cycle" projected for the period 2019-2023.

Tax liabilities - €5.1 million

This item amounts to €5.1 million at 31 December 2018, compared to a zero balance at the end of 2017. This essentially reflected higher payments on account made in the previous year (determined on the basis of a higher rate of IRES in 2016) and an increase in tax payable for 2018 (essentially due to the increase in pre-tax profit).

OTHER CURRENT LIABILITIES - €239.7 MILLION

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Prepayments	69.7	22.3	47.4
Other tax liabilities	7.4	7.8	(0.4)
Social security payables	25.0	24.2	0.8
Amounts due to personnel	41.6	47.0	(5.4)
Other amounts due to third parties	96.0	91.7	4.3
TOTAL	**239.7**	**193.0**	**46.7**

Prepayments

This item (€69.7 million) regards grants related to assets collected by the Group (€64.9 million attributable to the Parent Company, €2.8 million to Rete S.r.l. and €2.0 million to Terna Rete Italia S.p.A.) to fund the construction of non-current assets in progress at 31 December 2018.
Compared with the balance at 31 December 2017 (€22.3 million), this item is up €47.4 million, essentially due to the net impact of grants deducted directly from the carrying amount of the related assets, totalling €42.2 million, and new grants received from third parties, primarily the Ministry for Economic Development (€61.6 million).

Other tax liabilities

Other tax liabilities, amounting to €7.4 million, are broadly in line with the figure at 31 December 2017. These liabilities largely regard IRPEF withholdings on salaries and deferred compensation (TFR) paid to the employees of Terna Rete Italia S.p.A. (€5.0 million).

Social security payables

Social security payables, essentially relating to contributions payable to INPS (the National Institute of Social Security) by the Parent Company and the subsidiary Terna Rete Italia S.p.A., amount to €25.0 million and are broadly in line with the previous year. This item also included the amount payable to the Fondo Previdenza Elettrici - F.P.E. (the Electricity Industry Pension Fund), amounting to €3.5 million.

Amounts due to personnel

Amounts due to personnel, amounting to €41.6 million, essentially regard the Parent Company and the subsidiary Terna Rete Italia S.p.A.. They primarily relate to:

- incentives payable in the subsequent year (€24.9 million);
- amounts due to employees in the form of accrued and unused annual leave and bank holiday entitlements (€11.2 million).

This item is down €5.4 million, primarily due to a decrease in payables recognised in 2018 as a result of amounts payable to personnel who have opted to take part in the current generational turnover plan (down €7.4 million), partially offset by other amounts payable to staff amounts to be reimbursed (up €1.1 million).

Other payables due to third parties

Other payables due to third parties, amounting to €96.0 million, primarily regard guarantee deposits (€67.4 million) received from electricity market operators to guarantee their contractual obligations under dispatching and virtual interconnection contracts. This item also includes deferred income (€12.0 million, primarily attributable to the Group's non-regulated business).
This item is up by a total of €4.3 million, essentially due to an increase in accrued expenses and deferred income (up €3.4 million).

E. Commitments and risks

Risk management

The Group's financial risk

In the course of its operations, the Terna Group is exposed to different financial risks: market risk, liquidity risk and credit risk.
This section provides information regarding the Terna Group's exposure to all the above risks, along with a presentation of the objectives, policies and processes for managing those risks and the methods used to assess them, with further quantitative disclosures concerning the separate financial statements for 2018.
The Group's risk management policies seek to identify and analyse the risks that Group companies are exposed to, establishing appropriate limits and controls and monitoring the risks and compliance with such limits. These policies and the related systems are reviewed on a regular basis, in order to take account of any changes in market conditions or in the companies' operations.
The Terna Group's exposure to the aforementioned risks is substantially represented by the exposure of the Parent Company. As a part of the financial risk management policies approved by the Board of Directors, Terna has established the responsibilities and operating procedures for financial risk management, specifically as concerns the instruments to be used and the precise operating limits to apply in managing them.

(€m)

	31 DECEMBER 2018		31 DECEMBER 2017	
	RECEIVABLES AT AMORTISED COST	HEDGING DERIVATIVES	RECEIVABLES AT AMORTISED COST	HEDGING DERIVATIVES
Assets				
Derivative financial instruments	-	1.3	-	-
Cash on hand and deposits	1,328.9	-	1,989.2	-
Trade receivables	1,189.7	-	1,265.9	-
TOTAL	**2,518.6**	**1.3**	**3,255.1**	**-**

(€m)

	31 DECEMBER 2018			31 DECEMBER 2017		
	PAYABLES AT AMORTISED COST	HEDGING DERIVATIVES	TOTAL	PAYABLES AT AMORTISED COST	HEDGING DERIVATIVES	TOTAL
Liabilities						
Long-term debt	9,458.2	-	9,458.2	9,555.9	-	9,555.9
Derivative financial instruments	-	59.2	59.2	-	10.5	10.5
Trade payables	2,514.1	-	2,514.1	2,497.9	-	2,497.9
TOTAL	**11,972.3**	**59.2**	**12,031.5**	**12,053.8**	**10.5**	**12,064.3**

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument may fluctuate as a result of changes in financial market conditions. Market risk includes three types of risk: exchange rate risk, interest rate risk and inflation risk.

Risk management must be performed with the objective of minimising the related risks by selecting counterparties and instruments compatible with the Company's Risk Management Policy. Speculative activity is not form part of the Parent Company's activities.

The Terna Group seeks to adopt a dynamic approach to financial risk management. This approach is characterised by risk aversion, aimed at minimising risk through continuous monitoring of financial markets in order to obtain new financing and conclude hedging transactions in favourable market conditions. The dynamic approach enables the Group to intervene in order to improve existing hedges should there be a change in market conditions or changes in the hedged item, making the hedges inappropriate or excessively costly.

The fair value of financial instruments is determined in accordance with the fair value hierarchy envisaged under IFRS 7 (Level 2), by means of appropriate valuation techniques for each category of financial instrument, using market data at the closing date (such as interest rates, exchange rates and volatility) and discounting projected cash flows on the basis of the market yield curve at the reporting date.

Interest rate risk

Interest rate risk is represented by the uncertainty associated with interest rate fluctuations. This is the risk that a change in market interest rates may produce effects on the fair value or future cash flows of financial instruments.

In the course of its operations, the Group is exposed to the risk of fluctuations in interest rates. Its main source of interest rate risk is associated with its borrowings and the related hedges in the form of derivative instruments that generate financial expenses. The borrowing strategy focuses on long-term borrowings, whose term reflects the useful life of the Group's assets. It pursues an interest rate risk hedging policy that aims to guarantee that the percentage of debt represented by fixed rate liabilities is at least 40%, as provided for in the relevant policies. Considering the low level of interest rates, the Group has converted all its debt to fixed rate.

At 31 December 2018, interest rate risk is hedged by cash flow hedges, which hedge the risk connected with movements in interest rates relating to long-term borrowings.

Below are the notional amounts and fair values of the derivative financial instruments entered into by the Terna Group:

(€m)

	31 DECEMBER 2018		31 DECEMBER 2017		CHANGE	
	NOTIONAL	FAIR VALUE	NOTIONAL	FAIR VALUE	NOTIONAL	FAIR VALUE
Cash flow hedges	3,246.3	(59.2)	2,566.0	(10.5)	679.2	(48.7)

The notional amount of outstanding cash flow hedges at 31 December 2018, amounting to €3,245.2 million, breaks down as follows:

- €1,325.7 million (fair value loss of €14.7 million) maturing 2021;
- €150.0 million (fair value loss of €3.8 million) maturing 2026;
- €800.0 million (fair value loss of €19.6 million) maturing 2027;
- €950.0 million (fair value loss of €21.0 million) maturing 2028;
- €20.6 million (fair value loss of €0.1 million), relating to the subsidiary, Difebal, maturing 2032.

Sensitivity to interest rate risk

As regards the management of interest rate risk, following the restructuring of its portfolio, Terna has floating-to-fixed interest rate swaps (cash flow hedges) in place to hedge the risk associated with the expected future cash flows.

Since the hedging relationship between the derivative and the hedged item is formally documented and the effectiveness of the hedge, as verified initially and periodically over its life, is high, the Company has elected to use hedge accounting to ensure a perfect match between the maturities of the hedge and the hedged item. The aim of hedge accounting is to recognise the effects of the hedges and the hedged items in profit or loss at the same time. Accordingly, in the case of cash flow hedges, changes in the fair value of the derivative must be recognised in "Other comprehensive income" (recognising any ineffective portion immediately through profit or loss) and then recycled through profit or loss in the same period in which the cash flows of the hedged instrument materialise. The characteristics of cash flow hedges mirror those of the underlyings, with the timing of the related cash flows matching the timing of interest payments on the debt, without changes in fair value having any impact on profit or loss.

The following table reports the amounts recognised through profit or loss and in "Other comprehensive income" for positions that are sensitive to changes in interest rates, in addition to the theoretical value of the positions following a positive or negative shift in the yield curve and the differential impact of such changes recognised through profit or loss and in "Other Comprehensive Income". A hypothetical 10% movement in interest rates with respect to market interest rates at the reporting date was assumed:

(€m)

	OCI		
	CURRENT RATES +10%	CURRENT AMOUNTS	CURRENT RATES -10%
31 December 2018			
Positions sensitive to interest rate variations (bond issues, CFHs)	(48.5)	**(59.2)**	(69.9)
Hypothetical change	*10.7*	-	*(10.7)*
31 December 2017			
Positions sensitive to interest rate variations (bond issues, CFHs)	(12.3)	**(12.8)**	(13.3)
Hypothetical change	*0.5*	-	*(0.5)*

Inflation risk

As regards inflation risk, the rates established by the regulator to provide a return on Terna S.p.A.'s activities are determined so as to cover the allowed costs. Such cost components are updated on an annual basis to take into account the impact of inflation. Having used an inflation-linked bond issue in 2007, the Company has put in place an effective hedge of net income; in fact, any decrease in expected revenue due to a decrease in the inflation rate would be offset by lower financial expenses.

Exchange rate risk

The management of exchange rate risk must aim to protect a company's earnings from the risk of currency fluctuations by keeping a close eye on market movements and constantly monitoring the existing exposures. In managing this risk, Terna from time to time selects hedging instruments with structures and durations matching the Group's exchange rate exposure. The instruments used by Terna are of limited complexity, highly liquid and easy to price, such as forwards and options. Such contracts have a notional amount and maturity date less than or equal to that of the underlying financial liability, or the expected cash flows, so that any change in the fair value and/or estimated cash flows deriving from a rise or fall in the euro against other currencies is fully offset by a corresponding change in the fair value and/or estimated cash flows of the underlying position.

At 31 December 2018, the component of financial instruments associated with exchange rate risk is residual in nature and attributable to the investments in Latin America. This exposure is managed, at 31 December 2018, via currency hedges with a notional value of €368.9 million and a fair value gain of €1.3 million.

Liquidity risk

Liquidity risk is the risk that the Terna Group might encounter difficulty in discharging its obligations in respect of its financial liabilities and operating cycle. Liquidity risk management seeks to ensure adequate coverage of borrowing requirements by obtaining adequate credit lines and appropriate management of any surplus liquidity. At 31 December 2018, Terna had available short-term credit lines of €805.8 million and revolving credit lines of €2,450 million.

Credit risk

Credit risk is the risk a customer or one of the counterparties to a transaction in financial instruments could cause a financial loss by failing to discharge an obligation. It is mainly generated by the Group's trade receivables and financial investments.

The credit risk originated by open positions on transactions in derivatives is considered to be marginal since the counterparties, in compliance with the financial risk management policies adopted, are leading international banks with high ratings.

Terna provides its services essentially to counterparties considered solvent by the market, and therefore with a high credit standing, and does not have high concentrations of credit risk.

Credit risk management is driven by the provisions of ARERA Resolution 111/06, which, in art. 49, introduced instruments designed to limit the risks related to the insolvency of dispatching customers, both on a preventive basis and in the event of an actual insolvency. In particular, the Resolution establishes three instruments to safeguard the electricity market: a guarantee system (bank guarantees provided by individual dispatching customers, based on their turnover); the option of terminating dispatching contracts (in the event of insolvency or failure to replace enforced guarantees); and, finally, the possibility of recovering uncollected debts, after having taken all other possible collection actions, through a specific fee to be fixed by ARERA.

The following table summarises the exposure to such risk at the reporting date:

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Cash and cash equivalents	1,328.9	1,989.2	(660.3)
Trade receivables	1,189.7	1,265.9	(76.2)
TOTAL	**2,518.6**	**3,255.1**	**(736.5)**

The total value of the exposure to credit rate risk at 31 December 2018 is represented by the carrying amount of trade receivables and cash and cash equivalents.

The following tables provide qualitative information on trade receivables regarding the geographical distribution and type of customers.

GEOGRAPHICAL DISTRIBUTION

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017
Italy	1,088.9	1,166.9
Euro-area countries	24.4	75.5
Other countries	76.4	23.5
TOTAL	**1,189.7**	**1,265.9**

CUSTOMER TYPE

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017
Distributors	309.8	311.2
CSEA	114.0	95.3
Dispatching customers for injections	200.8	195.9
Dispatching customers for withdrawals (not distributors)	408.9	465.3
Parties which have signed virtual import contracts and virtual import services (interconnectors and shippers)	13.7	13.2
Sundry receivables	142.5	185.0
TOTAL	**1,189.7**	**1,265.9**

The following table breaks down customer receivables by due date, showing any potential impairment.

(€m)

	31 DECEMBER 2018		31 DECEMBER 2017	
	IMPAIRMENT	GROSS	IMPAIRMENT	GROSS
Current	(0.4)	1,020.5	-	1,159.3
0-30 days past due	(0.1)	13.0	-	43.8
31-120 days past due	(0.4)	9.2	-	17.8
Over 120 days past due	(43.0)	190.9	(44.1)	89.1
TOTAL	**(43.9)**	**1,233.6**	**(44.1)**	**1,310.0**

Movements in the allowance for doubtful accounts in the course of the year were as follows.

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017
Balance at 1 January*	(45.6)	(43.6)
Release of provisions	2.5	0.9
Impairments for the year	(0.8)	(1.4)
Balance	**(43.9)**	**(44.1)**

* *The opening balance at 1 January 2018 was adjusted by €1.5 million following application of the new standard, IFRS9.*

The value of guarantees received from eligible electricity market operators is illustrated below.

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017
Dispatching - injections	233.7	236.6
Dispatching - withdrawals	1,099.6	1,185.2
Transmission charges due from distributors	305.0	302.4
Virtual imports	84.0	81.1
Balance	**1,722.3**	**1,805.3**

In addition, Non-regulated Activities are exposed to “counterparty risk”, in particular in relation to the entities with which sales contracts are entered into, in consideration of the credibility and solvency of the parties in question and the impact that their possible insolvency could have on the financial strength of the business. Counterparty risk is mitigated by implementing special procedures to assess counterparties, measuring operating, financial and reputational aspects of the counterparties in question.

Default risk and debt covenants

This risk is associated with the possibility that the loan agreements or bond terms and conditions to which the Parent Company is a party may contain provisions authorising counterparties to call in such loans immediately upon the occurrence of certain events, thereby generating liquidity risk. More information on the contractual provisions of outstanding borrowings at 31 December 2018 is provided in the section, “Borrowings and financial liabilities” in the notes to the Terna Group’s consolidated financial statements.

Litigation

The main commitments and risks not disclosed in the statement of financial position at and for the year ended 31 December 2018, relating to the Parent Company Terna, its subsidiary Terna Rete Italia S.p.A. and the Tamini Group companies, are described below. There are no significant commitments or risks for the other subsidiaries at that date.

Environmental and urban planning litigation

Part of environmental litigation deriving from the construction and operation of Terna's power plants, consists of legal actions taken against the alleged negative effects of electric and magnetic fields generated by power lines. In general, this litigation necessarily involves the Parent Company, which owns the infrastructure in question. Moreover, it cannot be ruled out that the parties concerned may also initiate legal proceedings against the subsidiary Terna Rete Italia S.p.A., as the electromagnetism generated by power lines relates not only to ownership of the plant, but also to its operation and the quantity and quality of electricity it transports. Regarding this matter, it should be noted that the issue of the Cabinet Office Decree of 8 July 2003 - which specifically set the values of the three parameters (exposure limits, safety thresholds and quality targets) provided for in Framework Law 36 of 22 February 2001, which electricity infrastructure must comply with - led to a significant reduction in any such litigation.
Other environmental and urban planning disputes, which do not relate to electromagnetic fields, are also pending with regard to Terna S.p.A.. These disputes are connected with the operation of certain Terna-owned plant, which in the event of an unfavourable outcome could also generate immediate effects for Terna Rete Italia S.p.A. (to date unforeseeable and therefore not included in "Provisions for litigation and sundry risks"), both as the entity appointed by Terna S.p.A. to build the related infrastructure and as the entity responsible for its operation. In particular, charges may arise for Terna Rete Italia S.p.A. connected with changes to the infrastructure involved in such disputes and its temporary unavailability. However, after examination of the disputes in question by Terna S.p.A. and external counsel appointed by the Company, it appears that the possibility of any negative outcomes is remote.

Litigation regarding the legitimacy of construction permits and plant operations

Another aspect of litigation connected with the plant owned by the Parent Company derives from legal actions brought before the competent administrative courts, aimed at obtaining the annulment of decisions granting consent for the construction and operation of infrastructure.

Litigation relating to activities carried out under concession

As the operator of transmission and dispatching activities since 1 November 2005, the Parent Company has been a party in a number of court cases, most of which have contested determinations adopted by ARERA (Italy's Regulatory Authority for Energy, Networks and the Environment), and/or the Ministry for Economic Development, and/or Terna, in relation to these activities. In cases in which the plaintiffs have, in addition to inherent defects in the contested determinations, alleged violation of the regulations laid down by the aforementioned authorities, or in cases in which the determination has had an impact on Terna, the Company has also taken action to defend its interests through the legal system. Within the scope of such litigation - even though some cases have been concluded, at first and/or second instance, with the annulment of ARERA's resolutions and, when applicable, of the consequent determinations adopted by Terna - any negative outcomes for the Company itself may be deemed unlikely, as these disputes normally relate to pass-through items.

Litigation regarding supply contracts

This litigation only refers to Tamini Group companies and relates to supply contracts entered into between Tamini Group companies and its customers, regarding the supply of transformers and/or the related components.
It also concerns certain claims for damages brought against companies, regarding alleged damage caused by machinery and/or components supplied by them.

With regard to these judgements, it is impossible to exclude, in absolute terms, any unfavourable outcomes. Where such outcomes are deemed likely, specific accruals are made to the provisions for risks and charges.

In the opening months of 2019, Terna initiated the necessary liability actions against certain suppliers, in response to their violation of article 101 of the Treaty on the Functioning of the European Union, prohibiting anti-competitive behaviour. Such behaviour was confirmed by the European Commission in 2014 in decision C (2014) 2139 of 2 April 2014, as upheld in full by the court at first instance ruling of 18 July 2018. The Company's actions aim to obtain redress for the inefficiencies caused by the illegal conduct of the above external suppliers.

F. Business combinations

Acquisition of Avvenia The Energy Innovator S.r.l.

On **15 February 2018**, Terna - via its subsidiary, Terna Plus[2] - completed the acquisition of a 70% stake in **Avvenia The Energy Innovator S.r.l.**, a new company to which the principal assets of Avvenia, a leader in the energy efficiency sector and certified as an Energy Service Company (ESCo), have been transferred.

Avvenia is an Energy Service Company ("ESCo"), established in 2001 in Albano Laziale. The company occupies a leading position in the energy efficiency market, thanks to the high degree of specialisation and the wide range of sectors in which it has acquired contracts and in which its customers operate. The company's main aim is to improve the way its customers use energy and operate, using a network of professionals (engineers and architects) with proven experience in the sector to help its customers achieve operating and energy efficiencies.

The company had 16 employees at 31 December 2018.

This transaction is part of the process of identifying and acting on new commercial opportunities for the provision of energy efficiency services and projects, in order to further strengthen Terna Plus's role as a supplier of comprehensive integrated energy services and expand its range of innovative solutions as an Energy Solutions Provider. This is in line with the strategy set out in the Strategic Plan for the Group's Non-regulated Activities.

The company was acquired by Terna for a consideration of €7 million, 80% of which has been paid at the reporting date, whilst the remaining 20% will be payable by Terna based on the new company's financial statements for the year ended 31 December 2018, subject to an earnout basedthe company's performance goals. In this regard, it should be noted that the recognised purchase price already includes the outstanding consideration due, in view of the fact that the subsidiary has already achieved the above performance goals.

The sale agreement includes a call option on the remaining 30% of the new company's shares, exercisable within 24 months of the date of transfer of the initial stake.

The following table summarises the consideration paid to acquire Avvenia The Energy Innovator S.r.l. and shows amounts for assets acquired and liabilities assumed, as recognised at the acquisition date:

[2] On 2 August 2018, the partial demerger of Terna Plus S.r.l. (a wholly-owned subsidiary of the parent, Terna S.p.A.), and the transfer of the demerged assets to a newly established company named Terna Energy Solutions S.r.l., came into effect. As part of the demerger, the investment in Avvenia The Energy Innovator S.r.l. was also transferred to Terna Energy Solutions.

ASSETS ACQUIRED AND LIABILITIES ASSUMED AT 15 FEBRUARY 2018

	(€000)
	FAIR VALUE
ASSETS	
Non-current assets	
Property, plant and equipment	96.5
Intangible assets	17,493.8
Total non-current assets	**17,590.3**
Current assets	
Trade receivables	607.8
Other assets	2.605
Cash and cash equivalents	564.3
Total current assets	**3,777.0**
TOTAL ASSETS	**21,367.3**
LIABILITIES	
Non-current liabilities	
Employee benefits	75.7
Deferred tax liabilities	5,013.1
Total non-current liabilities	**5,088.8**
Current liabilities	
Trade payables	1.0
Other liabilities	2.5
Total current liabilities	**3.5**
TOTAL LIABILITIES	**5,092.3**
NET ASSETS ACQUIRED	**16,275.0**
Equity attributable to non-controlling interests	**4,882.5**
CONSIDERATION	**8,400.0**

After completing the process of accounting for the acquisition, in accordance with IFRS 3, the expected consideration was lower than the value of net assets at the acquisition date after deducting equity attributable to non-controlling interests, resulting in a bargain purchase and a gain of €3.0 million.

G. Related party transactions

Given that Terna S.p.A. is subject to the de facto control of Cassa Depositi e Prestiti S.p.A., a situation ascertained in 2007, related party transactions entered into by Terna during the year include transactions with the associates (Cesi S.p.A., Coreso S.A. and CGES) and employee pension funds (Fondenel and Fopen), as well as transactions with Cassa Depositi e Prestiti itself, with CDP Reti S.p.A. and with the companies directly or indirectly controlled by the Ministry of the Economy and Finance ("MEF").

Given that Terna Group companies and the companies directly or indirectly controlled by the Ministry of the Economy and Finance meet the definition for classification as "government-related entities", in accordance with IAS 24 - Related Party Disclosures, the Group has elected to adopt the partial exemption - permitted by the standard - from the disclosure requirements in respect of other companies controlled, influenced or jointly controlled by the same government entity. The remainder of this section provides qualitative and quantitative disclosures on transactions with government-related entities having a significant impact on the Group's results. Amounts relating to pass-through items are not included in these disclosures.

Related party transactions in 2018 broadly regard the provision of services in the course of ordinary activities and conducted on an arm's length basis.

The nature of sales to and purchases from related parties by the Terna Group is shown below, followed by details of the revenue and costs resulting from such transactions during the year and the related assets and liabilities outstanding at 31 December 2018.

RELATED PARTY	REVENUE-GENERATING TRANSACTIONS	COST-GENERATING TRANSACTIONS
Parent		
Cassa Depositi e Prestiti S.p.A.		Credit facilities.
Associates		
Cesi S.p.A.	Rental income on laboratories and other similar facilities for specific uses, dividends.	Technical studies and consultancy, research, design and experimentation.
CORESO S.A.		Technical coordination service for the TSO.
CGES	Dividends	
Other related parties		
GSE Group	Metering charge, dispatching charge.	Rental of spaces and workstations.
Enel Group	Transmission charge and aggregation of meter readings, dispatching charge, leases and rentals, power line maintenance, movement /re-routing of power lines, housing of fibre cable and maintenance of communications carried over proprietary power lines.	Recovery of energy discount, building services, MV power to new substations, specialist services for connection to Terna's control and protection systems.
Ferrovie Group	Dispatching charge, movement of power lines.	Right-of-way fees.
ENI Group	Dispatching charge.	Contributions for NTG connections, sundry services.
Snam Rete Gas S.p.A.	Movement /re-routing of power lines.	
ANAS S.p.A.	Movement /re-routing of power lines.	Right-of-way fees.
Fondenel and Fopen		Pension contributions payable by the Terna Group.
Other related parties of the MEF		Grants for NTG connections.

REVENUE AND COSTS

(€m)

	REVENUE COMPONENTS		COST COMPONENTS
	TRANSMISSION CHARGE AND OTHER REVENUE FROM REGULATED ACTIVITIES	NON-ENERGY-RELATED ITEMS	
De facto parent			
Cassa Depositi e Prestiti S.p.A.	-	-	3.1
Total de facto parent	**-**	**-**	**3.1**
Associates:			
Cesi S.p.A.	-	0.2	2.4
CORESO S.A.	-	-	1.6
Total associates	**-**	**0.2**	**4.0**
Other related parties:			
GSE Group	19.0	-	0.1
Enel Group	1,564.1	21.5	2.6
ENI Group	6.8	4.2	0.1
Ferrovie Group	2.4	0.9	12.4
Anas S.p.A.	-	-	0.3
Sace S.p.A.		-	0.2
Poste Italiane Group	-	-	0.1
Snam Rete Gas S.p.A.	-	0.2	-
Other related parties of MEF	-	0.4	-
Total other related parties	**1,592.3**	**27.2**	**16.1**
Pension funds:			
Fondenel	-	-	0.5
Fopen	-	-	2.3
Total pension funds	**-**	**-**	**2.8**
TOTAL	**1,592.3**	**27.4**	**26.0**

ASSETS AND LIABILITIES

(€m)

	PROPERTY, PLANT AND EQUIPMENT	RECEIVABLES AND OTHER ASSETS		PAYABLES AND OTHER LIABILITIES		CASH	GUARANTEES*
	CAPITALISED COSTS	OTHER	FINANCIAL	OTHER	FINANCIAL		
De facto parent							
Cassa Depositi e Prestiti S.p.A.	-	-		-	500.5		-
Total de facto parent	**-**	**-**	**-**	**-**	**500.5**	**-**	**-**
Associates:							
Cesi S.p.A.	10.3	0.3	-	8.1	-	-	1.2
CORESO S.A.	-	-	-	0.1	-	-	-
CGES	-	3.3	-	-	-	-	-
Total associates	**10.3**	**3.6**	**-**	**8.2**	**-**	**-**	1.2
Other related parties:							
GSE Group	-	3.1	-	0.1	-	-	-
Enel Group	13.0	402.1	-	30.7	-	-	586.8
ENI Group	-	3.3	-	1.9	-	-	32.8
Ferrovie Group	0.1	0.5	-	23.6	-	-	24.6
ANAS S.p.A.	3.4	0.1	-	1.5	-	-	-
Snam Rete Gas S.p.A.	-	0.1	-	0.7	-	-	-
Ansaldo Energia S.p.A.	13.8	-	-	12.7	-	-	-
Other related parties of MEF	0.3	0.2	-		-	0.1	-
Total other related parties	**30.6**	**409.4**	**-**	**71.2**	**-**	**0.1**	**644.2**
Pension funds:							
Fopen	-	-	-	2.0	-	-	-
Total pension funds	**-**	**-**	**-**	**2.0**	**-**	**-**	**-**
TOTAL	**40.9**	**413.0**	**-**	**81.4**	**500.5**	**0.1**	**645.4**

* *Guarantees regard surety bonds received from contractors.*

H. Significant non-recurring, atypical or unusual events and transactions

With the exception of the instances described above, no significant non-recurring, atypical or unusual events or transactions, involving either third or related parties, took place in 2018.

I. Notes to the statement of cash flows

Cash flow from **continuing operations** amounts to €1,306.6 million, with approximately €1,683.9 million in operating cash flow and an outflow of approximately €377.3 million generated by changes in net working capital.

The cash outflow for **investing activities** totals €1,036.9 million, and above all regards €992.5 million relating to investment in property, plant and equipment, €56.4 million invested in intangible assets, €15.1 million in capitalised financial expenses, in addition to the contribution deriving from the acquisition of Avvenia The Energy Innovator S.r.l., amounting to €17.6 million.
The net cash outflow for **shareholder transactions** amounts to €449.7 million, due primarily to payment of the final dividend for 2017 (€292.9 million) and the interim dividend for 2018 (€158.2 million), in addition to the contribution to equity attributable to non-controlling shareholders deriving from the acquisition of Avvenia (an inflow of €4.9 million).
As a result, net cash used in investing activities and to provide a return on equity during the year amounted to €1,486.6 million, for the most part covered by cash flow from continuing operations of €1,306.6 million. The remainder was funded through the use of cash reserves.
Net debt has risen by €103 million compared with the previous year.

The following table shows the reconciliation of net changes deriving from financing activities in the statement of cash flows:

(€m)

	31 DECEMBER 2017	CASH FLOW FROM FINANCING ACTIVITIES	CHANGE IN FV AND OTHER	31 DECEMBER 2018
- Long-term borrowings (including current portion)	9,555.9	14.2	(111.9)	9,458.2
- Short-term borrowings	118.0	(93.0)	-	25.0
- Current financial assets - Government securities	-	(401.5)	(1.1)	(402.6)
NET CHANGE DERIVING FROM FINANCING ACTIVITIES	**9,673.9**	**(480.3)**	**(113.0)**	**9,080.6**

L. Government grants

Article 1, paragraphs 125 to 129, of Law 124 of 4 August 2017 (the annual markets and competition law) has introduced a number of measures designed to ensure the transparency of the government grants system. These measures include an obligation for the relevant companies to disclose the grants received (paragraph 125) and those disbursed (paragraph 126) in their annual financial statements.

In accordance with Circular 5 of 22 February 2019 "Transparency in the government grants system: an assessment of the regulations and interpretation guidance", published by Assonime in February 2019, the Terna Group has adopted the following basis of reporting for government grants:
- the regulations only apply to entities resident in Italy;
- grants have the nature of grants or donations, and represent incentives or subsidies designed to give beneficiaries a recognised economic advantage; the grants therefore take the form of donations or giving and public aid for specific purposes, and are not awarded under a general aid regime;
- the public resources used are exclusively "national";
- grants are reported on a cash basis and if the amount is not less than €10,000 (with reference to each individual beneficiary) in the reporting period.

In line with the above, the following table shows government grants collected/disbursed by the Group in 2018:

GRANTS RECEIVED (PARAGRAPH 125)

	GRANTOR					
BENEFICIARY ENTITY	NAME	TAX CODE	VAT NUMBER	TYPE OF TRANSACTION	AMOUNT (€)	NOTE
TERNA S.p.A.	Ministry for Economic Development	80230390587	80230390587	State aid*	47,053,290.76	Advance on grants awarded for Terna S.p.A. projects financed by government grants, with funding provided under the National Operational Programme (NOP) for Enterprises and Competitiveness 2014 - 2020 ERDF - AXIS IV - investment priority 4d - Action 4.3.1
TERNA S.p.A.	Sicily Regional Authority	80012000826	02711070827	State aid*	14,499,449.49	Advance on grants awarded for Terna S.p.A. projects financed by government grants, with funding provided under the Regional Operational Programme (ROP) ERDF Sicily 2014 - 2020 - OT4 - Action 4.3.1
TOTAL					**61,552,740.25**	

** This transaction is covered by the obligation to publish in the National State Aid Register.*

GRANTS DISBURSED (PARAGRAPH 126)

	BENEFICIARY					
GRANTOR	NAME	TAX CODE	VAT NUMBER	TYPE OF TRANSACTION	AMOUNT (€)	NOTE
TERNA S.p.A.	Istituto Nazionale per l'Assicurazione contro gli Infortuni sul Lavoro		00968951004	Giving	12,000	The first edition of the Biennial Masters in "Integrated Safety and Health Management in a Changing Workplace"
TERNA S.p.A.	Fondazione Bambino Gesù Onlus	97531780589		Giving	40,000	Financial support for the provisions of accommodation for children's families
TOTAL					**52,000**	

M. Events after 31 December 2018

Revised zonal configuration for Brindisi, Foggia and Priolo

From **1 January 2019**, the new zonal configuration came into force. Compared to the past, the new arrangement has combined the production nodes with limited capacity in Brindisi, Foggia and Priolo with neighbouring zones (the South and Sicily zones, respectively), as well as transferring the Gissi node from the South to the Central-South zone. This change was made in accordance with the European CACM Regulation, which all the regulatory authorities and TSOs of European Union member states must comply with. In particular, the changes made are aimed at ensuring safe operation of the transmission system, as well as boosting the efficiency and cost-effectiveness of the electricity market. In Resolution 386/2018/R/eel, ARERA has approved Terna's proposed revision of the zonal configuration following the review process carried out in 2018 pursuant to the European CACM Regulation and ARERA Resolution 22/18/R/eel.

Private placement of green bond issue

On **10 January 2019**, Terna S.p.A. launched a fixed-rate green bond issue in the form of a private placement, amounting to €250 million. The issue was assigned ratings of "BBB+" by Standard and Poor's, "(P)Baa2" by Moody's and "BBB+" by Fitch. The proceeds will be used to finance the Company's eligible green projects, thus confirming the Group's strategy oriented towards combining sustainability with growth, in order to promote the ongoing energy transition and generate ever increasing benefits for Italy and its stakeholders.

Bloomberg Gender Equality Index

On **16 January 2019**, Terna was included for the first time in the Bloomberg Gender Equality Index (GEI), an international index that measures companies' performance regarding gender equality issues and the quality and transparency of their public reporting, a decisive factor in the overall assessment. For 2019, Bloomberg analysed over 9,000 companies listed on leading world financial markets, including only 230 of them in the GEI index (in total, there are three Italian companies), from 36 countries and representing 10 different sectors (including energy, industry, utilities and finance).

Veneto Regional Authority and Terna: Investment programme

On **21 January 2019**, the Governor of the Veneto Region, Luca Zaia, and Terna's Chief Executive Officer, Luigi Ferraris, signed a planning agreement regarding extraordinary works relating to the security of the electricity system and development of the region, with the aim of promoting sustainable development in the Veneto region and helping local society and the economy to recover from the exceptional weather events of November 2018 by rebuilding and developing regional electricity infrastructure. In this sense, Veneto Regional Authority and Terna have committed to adopting the most advanced forms of cooperation, with local authorities and communities to be closely and fully involved in deciding on the works and initiatives to be undertaken in the various areas. The agreement provides for substantial investment in the implementation of vital works on the Veneto electricity grid, the most significant being an upgrade between Venice and Padua at a cost of over €400 million.

Co-optation of a new Director on to the Board of Directors

Following the resignation of the non-executive Director, Stefano Saglia, on **15 February 2019**, Terna S.p.A.'s Board of Directors co-opted a new non-executive Director, Paolo Calcagnini (the Chief Financial Officer of Cassa Depositi e Prestiti S.p.A.), on to the Board in response to the invitation from the Cassa Depositi e Prestiti Group which, in a letter dated 6 February 2019, submitted Mr Calcagnini's candidacy for the Company's appropriate and independent evaluation.

Establishment of PI.SA. 2 S.r.l.

A new wholly owned subsidiary of Terna S.p.A., named PI.SA. 2 S.r.l., was established on **15 February 2019**. The company's purpose is the design, construction, management, development, operation and maintenance, including for third parties, of power lines and grid infrastructure and other infrastructure connected to the grid, in addition to plant and equipment used in the electricity transmission sector. The company will also engage in research, consulting and support on matters relating to the core business, conduct any form of activity enabling the improved use and deployment of the networks, structures, resources and expertise employed.

Terna and Genoa's electricity grid

As part of the planned rationalisation of the electricity grid in the city of Genoa, on **18 February 2019**, Terna completed the laying of underground cables for the 132kV power lines linking the Fiera and Central primary substations and the Genoa T. and Fiera primary substations. The works are necessary to support the increase in port activities, thanks to the modernisation of the local grid, and for the implementation of strategic projects for the development and urban renewal of the city of Genoa, which was badly hit by the collapse of the Morandi road bridge last August.

New electricity line in Brazil to drive development of renewable sources

The new high-voltage power line extending 158 km in Rio Grande do Sul, which will enable full integration of large quantities of energy produced from renewable sources, above all from wind, into the Brazilian national grid, was inaugurated on **19 February 2019**. Terna, through its subsidiary Santa Maria Transmissora de Energia, activated the new "Santa Maria 3 - Santo Angelo 2" 230 kV power line in the south-east of Brazil, considered of significant importance for the Rio Grande do Sul region, as it will allow for the integration of energy generated by wind farms in the south of Brazil into the Brazilian national transmission grid. With over 80% of electricity produced from clean sources and wind production having increased by 20% in the last year, Brazil currently represents the largest Latin American energy market and is among the top five in the world for its development potential.

Restructuring in the Venetian Lagoon

The underground and submarine cables for the 132kV power lines between the Sacca Serenella Primary Substation - Cavallino Primary Substation entered service on **21 February 2019**. This date also marks the start of work on other projects, such as demolition of the Fusina 2 - Sacca Fisola overhead power line, covering a distance of 6.5 km, and the removal of 24 electricity pylons, most of which located in the lagoon area, in order to boost the efficiency and security offered by the electricity grid in the area of the Venetian Lagoon.

Terna has also embarked on preparations for the demolition of a section of the Villabona - Fusina 2 line where it interferes with the area known as the Vallone Moranzani. Once the removal of the conductors has been completed, it will be possible to begin the dismantling of approximately 2 km of power lines and 9 pylons. The work will lead to the demolition of a further 3.6 km of lines, making a total of 15 lines located in the Malcontenta and Venice Ro-Ro port areas.

Restructuring of the Rimini - Riccione electricity grid

On **27 February 2019**, Terna presented its plan for the restructuring of the grid in the Rimini area, aimed at boosting the security and efficiency of the area's electricity system, above all during the summer season, when electricity consumption rises significantly, with the consequent risk of outages. A total of 8 municipalities are covered by the plan: Rimini, Riccione, Coriano, Sant'Arcangelo di Romagna, San Mauro Pascoli, Savignano sul Rubicone, Gatteo and Gambettola.
In Rimini, 84 pylons and around 21 km of power lines will be demolished, to be replaced with approximately 9 km of new underground lines and two new pylons. The city centre will benefit from the large area of land that removal of the old infrastructure will free up, above all two elementary schools, the "Padulli" and "Rodari", located in the area in which the restructuring will take place.

Operation Mato Grosso

On **27 February 2019**, an Implementation Agreement was signed by the Parish of Chacas and Terna Plus S.r.l. for the construction of over 16 km of high-voltage power line at a record altitude of 4,100 metres in the Andes. The new line will connect Peru's national grid with the Huallin hydroelectric plant located 500 km to the north of the capital Lima, significantly increasing the production and transmission of renewable energy for the benefit of both the local community and all the other communities in need that Operation Mato Grosso is designed to help.
For Terna, the Agreement falls within the wider scope of its "business solidarity" projects and voluntary activities already implemented for several years to support the well-being of the populations most in need in areas where it operates. This includes support for voluntary and non-profit organisations through charitable and social initiatives, again in the context of environmental sustainability.

Snam and Terna: research and innovation partnership and electricity-gas convergence

On **1 March 2019**, Snam and Terna signed a memorandum of understanding with the aim of defining and implementing joint initiatives, in particular regarding research, development and innovation and the potential for convergence between the electricity and gas systems.

The areas of activity covered by the agreement include the development of shared national and European energy scenarios with the aim of exploiting convergence between the gas and electricity systems, as part of Snam's plan for converting its compression and storage plants into "dual energy" gas-electric plants with significant benefits in terms of increased flexibility of the services rendered and reduction of environmental impact.

In addition, research and development initiatives will have great importance, with particular reference to the use of programmable renewable sources for electricity generation and to the new coupling sector technologies, aimed at ever-better use of resources, as well as the testing and development of innovative technological solutions for the analysis and monitoring of infrastructure, hydrogeological analysis, the monitoring of worksites and joint optimisation of the electricity and gas networks.

Restructuring of the electricity grid between Catanzaro and Calusia

On **4 March 2019**, Terna arranged 3 meetings open to residents in the province of Catanzaro and Crotone, during which the Company will provide information on the planned construction of a new 150kV power line in the local area. The project will involve the municipalities of Catanzaro, Soveria Simeri, Simeri Crichi, Zagarise, Sellia Marina, Belcastro, Andali, Cerva, Petronà, Sersale Cropani, Mesoraca, Cotronei, Petilia Policastro and Caccuri. The work aims to guarantee the increased stability and reliability of the local electricity system, to improve the quality of the service and the efficiency of the grid and to encourage increased production from renewables.

The 150kV power line, to be installed between the Catanzaro and Calusia Electrical Substations, with connections to the Belcastro substation and the primary transformer room at Mesoraca, will enable the demolition of around 90 km of overhead power lines.

New composition of Board committees

On **21 March 2019**, the Board of Directors modified the composition of the Company's Board committees, in order to ensure continued compliance with the recommendations in the Corporate Governance Code and remain in line with best governance practices. Gabriella Porcelli has taken on the chair of the Nominations Committee, whose other members continue to be Fabio Corsico and Yunpeng He. The Audit, Risk, Corporate Governance and Sustainability Committee, which continues to be chaired by Luca Dal Fabbro since his appointment on 9 November 2018, will continue to include Paola Giannotti and Elena Vasco. The latter has also been appointed a member of the Remuneration Committee, whose other members continue to be Fabio Corsico (as Chair) and Gabriella Porcelli. Finally, Paola Giannotti has been appointed Chair of the Related Party Transactions Committee, of which Luca Dal Fabbro and Gabriella Porcelli continue to be members.

Green bond launch

On **3 April 2019** TERNA S.p.A. launched a green bond addressed to institutional investors. The issuance is made under Terna's Euro 8,000,000,000 Medium Term Notes Programme (EMTN), which has been rated "BBB+" by Standard & Poor's, "(P)Baa2" by Moody's and "BBB+" by Fitch for an aggregate amount of 500 million Euro. The green bond has been issued with a tenor of 7 years and a maturity date falling on 10 April 2026, will pay a coupon of 1.000%, with an issue price equal to 99.886%, a spread of 78 basis points over the midswap and an indicative spread of approximately 100 basis points lower than the Italian BTP having same maturity. The actual cost for Terna, in respect of such issuance, is therefore equal to 1.02% as opposed to the aggregate average cost of the consolidated debt equal to 1.6% over the new Strategic Plan period.
The net proceeds from the issuance will be used to finance the company's eligible green projects of the Company.

Disclosure

pursuant to art. 149-*duodecies* of the CONSOB Regulations for Issuers

The following table, prepared pursuant to art. 149-*duodecies* of the CONSOB Regulations for Issuers, shows the fees paid for audit and other services provided by the Terna Group's independent auditors in 2018.

(€)

	ENTITY PROVIDING SERVICE	FEES DUE FOR THE YEAR
Audit of the accounts	PwC	797,397
Attestation and other services	PwC	160,613
TOTAL		**958,010**

Attestation

of the consolidated financial statements pursuant to art. 81-*ter* of CONSOB Regulation 11971 of 14 May 1999, as amended

"Terna Group"

1. The undersigned, Luigi Ferraris, as Chief Executive Officer, and Agostino Scornajenchi, as Manager responsible for Terna S.p.A.'s financial reporting, having also taken account of the provisions of art.154-*bis*, paragraphs 3 and 4 of Legislative Decree 58 of 24 February 1998, attest to:
   - the adequacy with regard to the nature of the Company, and
   - the effective application of the administrative and accounting procedures adopted in preparation of the consolidated financial statements during the year ended 31 December 2018.

2. The administrative and accounting procedures adopted in preparation of the consolidated financial statements for the year ended 31 December 2018 were drawn up, and their adequacy assessed, on the basis of the regulations and methods adopted by Terna S.p.A. in accordance with the Internal Control-Integrated Framework model issued by the Committee of Sponsoring Organizations of the Treadway Commission. This Commission has established a body of general principles providing a standard for internal control and risk management systems that is generally accepted at international level.

3. We also attest that:

   3.1 the consolidated financial statements for the year ended 31 December 2018:

   a. have been prepared in compliance with the International Financial Reporting Standards endorsed by the European Union through EC Regulation 1606/2002, issued by the European Parliament and by the Council on 19 July 2002 and the statutory requirements implementing the provisions of art. 9 of Legislative Decree 38/2005;

   b. are consistent with the underlying accounting books and records;

   c. provide a true and fair view of the financial position and results of operations of the issuer and the companies included in the scope of consolidation.

   3.2 the Directors' report on operations includes a reliable analysis of the operating and financial performance and situation of the issuer and the companies included in the scope of consolidation, as well as a description of the main risks and uncertainties to which they are exposed.

Rome, 21 March 2019

Chief Executive Officer	Manager responsible for financial reporting
Luigi Ferraris	**Agostino Scornajenchi**
(original signed)	*(original signed)*

Independent auditor's report

in accordance with article 14 of Legislative Decree 39 of 27 January 2010 and article 10 of Regulation (EU) 537/2014

Independent auditor's report

in accordance with article 14 of Legislative Decree 39 of 27 January 2010 and article 10 of Regulation (EU) 537/2014

To the shareholders of Terna SpA

Report on the Audit of the Consolidated Financial Statements

Opinion

We have audited the consolidated financial statements of Terna SpA and its subsidiaries (Terna group), which comprise the statement of financial position as of 31 December 2018, the income statement, the statement of comprehensive income, the statement of changes in equity, the statement of cash flows for the year then ended and the notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated financial statements give a true and fair view of the financial position of the Terna group as of 31 December 2018, and of the result of its operations and cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union, and with the regulations issued to implement article 9 of Legislative Decree 38/05.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISA Italia). Our responsibilities under those standards are further described in section Auditor's Responsibilities for the Audit of the Consolidated Financial Statements of this report. We are independent of Terna SpA (the Company) pursuant to the regulations and standards on ethics and independence applicable to audits of financial statements under Italian law. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key Audit Matters	*Auditing procedures performed in response to key audit matters*
Capital expenditure for the development and operation of the transmission grid *Section D – Notes to the consolidated statement of financial position – Note 12 Property, plant and equipment and Note 14 Intangible assets* Costs capitalised during the year as property, plant and equipment and intangible assets amount to Euro 1,091 million and mainly relate to capital expenditure for the development and operation of the transmission grid. Revenue from transmission and dispatching activities (regulated activities) is determined each year in accordance with the approved regulatory tariffs which are based on a pre-established return on capital invested, plus amortisation and depreciation and operating costs recognised. The capitalisation of costs for the operation and development of the transmission grid therefore represented a key matter in the audit of the consolidated financial statements, also considering the magnitude and the high number of transactions.	We performed an understanding and evaluation of the system of internal control over the capital expenditure cycle, with particular reference to identification of the key controls and the verification of their effectiveness. We assessed that the capitalisation of costs complied with the international accounting standards. We also performed substantive procedures analysing, on a sample basis, the supporting documentation of capitalised costs in order to verify that these costs were accurate, complete and pertaining to the reporting period. Our tests also included the analysis of the notes to the consolidated financial statements to verify the adequacy and completeness of the disclosures therein.
Revenue from non-regulated activities *Section B – Notes to the consolidated income statement - Note 1 Revenue from sales and services and Note 2 Other revenue and income and Section C – Operating segments* Total revenue, amounting to Euro 2,319 million, includes revenue from non-regulated activities of Euro 195 million equal to 8.4% of total revenue of the group. Non-regulated activities mainly consist of the development, production and sale of power transformers, miscellaneous services in favour of third parties and the construction of a part of international interconnectors, providing for a variety of cases and different degree of complexity of underlying transactions.	With respect to the main revenue streams from non-regulated activities, we performed an understanding and evaluation of key controls implemented by the group. We verified the recognition of revenue from non-regulated activities through substantive procedures including analyses, on a sample basis, of the supporting documentation, focusing on the contractual clauses underlying the recognition of revenue within the correct reporting period also in consideration of the requirements

Key Audit Matters	*Auditing procedures performed in response to key audit matters*
Therefore, the recognition of revenue from non-regulated activities was a key matter in the audit of the consolidated financial statements.	envisaged by the new IFRS 15 "Revenue from Contracts with Customers". Our tests also included the analysis of the notes to the consolidated financial statements to verify the adequacy and completeness of the disclosures therein.
Derivative financial instruments *Section D – Notes to the consolidated statement of financial position – Note 24 Borrowings and financial liabilities and Section E – Commitments and risks*	
The amount of borrowings in the consolidated financial statements at 31 December 2018 is Euro 9,483 million. In accordance with the risk management policies, the group mitigates its exposure to the change in interest rates by entering into derivative financial instruments for hedging purposes. The notional amount of derivatives at 31 December 2018 is Euro 3,246 million. Considering the magnitude of values, the degree of complexity of both the fair value measurement process and the recognition rules provided for by the new IFRS 9 "Financial Instruments", the verification of derivative financial instruments was considered as a key matter in the audit of the consolidated financial statements.	We performed an understanding and evaluation of the system of internal control over the measurement process of the derivative financial instruments and related accounting treatment. We recalculated, on a sample basis and involving the experts of the PwC network, the fair value of derivatives and we verified the hedge effectiveness in accordance with the provisions of IFRS 9 and with the corporate procedures. Our tests also included the analysis of the notes to the consolidated financial statements to verify the adequacy and completeness of the disclosures therein.

Responsibilities of the Directors and the Board of Statutory Auditors for the Consolidated Financial Statements

The directors are responsible for the preparation of consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the European Union, and with the regulations issued to implement article 9 of Legislative Decree 38/05 and, in the terms prescribed by law, for such internal control as they determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

The directors are responsible for assessing the group's ability to continue as a going concern and, in preparing the consolidated financial statements, for the appropriate application of the going concern basis of accounting, and for disclosing matters related to going concern. In preparing the consolidated financial statements, the directors use the going concern basis of accounting unless they either intend to liquidate Terna SpA or to cease operations, or have no realistic alternative but to do so.

The board of statutory auditors is responsible for overseeing, in the terms prescribed by law, the group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with International Standards on Auditing (ISA Italia) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

As part of an audit conducted in accordance with International Standards on Auditing (ISA Italia), we exercised professional judgment and maintained professional scepticism throughout the audit. Furthermore:

- we identified and assessed the risks of material misstatement of the consolidated financial statements, whether due to fraud or error; we designed and performed audit procedures responsive to those risks; we obtained audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- we obtained an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the group's internal control;
- we evaluated the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors;
- we concluded on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the group to cease to continue as a going concern;
- we evaluated the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation;
- we obtained sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of

the group audit. We remain solely responsible for our audit opinion on the consolidated financial statements.

We communicated with those charged with governance, identified at an appropriate level as required by ISA Italia regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identified during our audit.

We also provided those charged with governance with a statement that we complied with the regulations and standards on ethics and independence applicable under Italian law and communicated with them all relationships and other matters that may reasonably be thought to bear on our independence and, where applicable, related safeguards.

From the matters communicated with those charged with governance, we determined those matters that are of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report.

Additional Disclosures required by article 10 of Regulation (EU) 537/2014

We were appointed by the shareholders of Terna SpA at the general meeting held on 13 May 2011 to perform the audit of the Company separate and consolidated financial statements for the years ending 31 December 2011 through 31 December 2019.

We declare that we did not provide any prohibited non-audit services referred to in article 5, paragraph 1, of Regulation (EU) 537/2014 and that we remained independent of the Company in conducting the audit.

We confirm that the opinion on the consolidated financial statements expressed in this report is consistent with the additional report to the board of statutory auditors, in its capacity as audit committee, prepared pursuant to article 11 of the aforementioned Regulation.

Report on Compliance with other Laws and Regulations

Opinion in accordance with article 14, paragraph 2, letter e), of Legislative Decree 39/2010 and article 123-bis, paragraph 4, of Legislative Decree 58/1998

The directors of Terna SpA are responsible for preparing a report on operations and a report on the corporate governance and ownership structure of the Terna group as of 31 December 2018, including their consistency with the relevant consolidated financial statements and their compliance with the law.

We have performed the procedures required under auditing standard (SA Italia) 720B in order to express an opinion on the consistency of the report on operations and of the specific information included in the report on corporate governance and ownership structure referred to in article 123-bis, paragraph 4, of Legislative Decree 58/1998, with the consolidated financial statements of the Terna group as of 31 December 2018 and on their compliance with the law, as well as to issue a statement on material misstatements, if any.

In our opinion, the report on operations and the specific information included in the report on corporate governance and ownership structure mentioned above are consistent with the consolidated financial statements of the Terna group as of 31 December 2018 and are prepared in compliance with the law.

With reference to the statement referred to in article 14, paragraph 2, letter e), of Legislative Decree 39/2010, issued on the basis of our knowledge and understanding of the group obtained in the course of the audit, we have nothing to report.

Statement in accordance with article 4 of Consob Regulation implementing Legislative Decree 254 of 30 December 2016

The directors of Terna SpA are responsible for the preparation of the non-financial statement pursuant to Legislative Decree 254 of 30 December 2016.
We have verified that the directors approved the non-financial statements.

Pursuant to article 3, paragraph 10, of Legislative Decree 254 of 30 December 2016, the non-financial statement is the subject of a separate statement of compliance issued by ourselves.

Rome, 11 April 2019

PricewaterhouseCoopers SpA

Signed by

Luca Bonvino
(Partner)

This report has been translated from the original version which was issued in Italian language, solely for the convenience of international readers.

SEPARATE FINANCIAL STATEMENTS

Contents

Separate financial statements

Income statement of Terna S.p.A.

(€)

	NOTE	2018	2017
A - REVENUE			
1. Revenue from sales and services	1	1,892,840,140	1,861,453,047
of which: related parties		*1,616,989,988*	*1,618,317,512*
2. Other revenue and income	2	74,707,510	90,053,148
of which: related parties		*54,332,356*	*43,160,360*
Total revenue		**1,967,547,650**	**1,951,506,195**
B - OPERATING COSTS			
1. Raw and consumable materials used	3	5,290,261	10,024,776
of which: related parties		*244,934*	*119,063*
2. Services	4	364,580,334	349,832,712
of which: related parties		*309,122,126*	*300,498,593*
3. Personnel expenses	5	63,929,242	65,987,971
- gross personnel expenses		*67,117,442*	*69,027,451*
- capitalised personnel expenses		*(3,188,200)*	*(3,039,480)*
of which: related parties		*738,069*	*585,840*
4. Amortisation, depreciation and impairment losses	6	517,865,399	495,192,305
5. Other operating costs	7	18,172,002	39,011,448
of which: related parties		*26,033*	*98,418*
Total costs		**969,837,238**	**960,049,212**
A-B OPERATING PROFIT/(LOSS)		**997,710,412**	**991,456,983**
C - FINANCIAL INCOME/(EXPENSES)			
1. Financial income	8	13,020,750	5,729,373
of which: related parties		*8,096,591*	*1,951,401*
2. Financial expenses	8	(91,582,167)	(95,554,625)
of which: related parties		*(3,076,200)*	*(3,770,511)*
D - PROFIT/(LOSS) BEFORE TAX		**919,148,995**	**901,631,731**
E - INCOME TAX EXPENSE	9	**257,857,793**	**261,588,853**
F - PROFIT FOR THE YEAR		**661,291,202**	**640,042,878**

Statement of comprehensive income of Terna S.p.A.

(€)

	NOTE	2018	2017
PROFIT FOR THE YEAR		**661,291,202**	**640,042,878**
Other comprehensive income for the year reclassifiable to profit or loss			
- Cash flow hedges after taxation	20	(32,502,930)	5,904,878
- Financial assets at fair value through other comprehensive income, after taxation	20	1,168,219	-
- Cost of hedges, after taxation	20	(1,789,675)	-
Other comprehensive income for the year not reclassifiable to profit or loss			
- Actuarial gains/(losses) on provisions for employee benefits, after taxation	20	16,440	(24,536)
COMPREHENSIVE INCOME FOR THE YEAR		**628,183,256**	**645,923,220**

Statement of financial position of Terna S.p.A.

(€)

	NOTE	31 DECEMBER 2018	31 DECEMBER 2017
A - NON-CURRENT ASSETS			
1. Property, plant and equipment	10	12,034,962,379	11,705,228,618
of which: related parties		*73,329,994*	*66,973,041*
2. Goodwill	11	190,228,231	190,228,231
3. Intangible assets	12	237,451,427	234,080,643
4 Deferred tax assets	13	18,248,879	-
5. Non-current financial assets	14	1,091,128,621	1,009,659,871
of which: related parties		*9,956,332*	*339,745*
6. Other non-current assets	15	4,257,446	3,526,176
Total non-current assets		**13,576,276,983**	**13,142,723,539**
B - CURRENT ASSETS			
1. Inventories	16	-	5,307,324
2. Trade receivables	17	1,090,063,061	1,142,545,872
of which: related parties		*422,445,664*	*426,736,699*
3. Current financial assets	14	494,024,680	213,317
of which: related parties		*89,484,556*	-
4. Cash and cash equivalents	18	945,044,880	1,678,217,732
of which: related parties		*(204,749,945)*	*(219,450,417)*
5. Income tax assets	19	16,016,310	57,927,658
of which: related parties		-	*9,910,413*
6. Other current assets	15	20,446,631	63,226,507
of which: related parties		*3,266,360*	-
Total current assets		**2,565,595,562**	**2,947,438,410**
TOTAL ASSETS		**16,141,872,545**	**16,090,161,949**

(continued)

(continued)

(€)

	NOTE	31 DECEMBER 2018	31 DECEMBER 2017
C - EQUITY			
1. Share capital		442,198,240	442,198,240
2. Other reserves		792,531,833	825,639,778
3. Retained earnings/(accumulated losses)		2,113,051,689	1,916,706,986
4. Interim dividend		(158,186,370)	(149,268,036)
5. Profit for the year		661,291,202	640,042,878
Total equity	**20**	**3,850,886,594**	**3,675,319,846**
D - NON-CURRENT LIABILITIES			
1. Long-term borrowings	21	8,171,886,525	8,638,448,258
of which: related parties		-	*500,000,000*
2. Employee benefits	22	11,768,108	12,744,530
3. Provisions for risks and charges	23	213,829,474	243,496,364
4. Deferred tax liabilities	13	-	17,258,091
5. Non-current financial liabilities	21	59,089,581	9,904,232
6. Other non-current liabilities	24	196,119,231	181,316,955
of which: related parties		*39,929,872*	*41,855,770*
Total non-current liabilities		**8,652,692,919**	**9,103,168,430**
E - CURRENT LIABILITIES			
1. Short-term borrowings	21	-	90,000,000
2. Current portion of long-term borrowings	21	1,229,798,720	884,039,788
of which: related parties		*500,000,000*	-
3. Trade payables	25	2,113,384,836	2,106,382,361
of which: related parties		*472,324,200*	*403,564,166*
4. Tax expense	25	8,072,200	-
of which: related parties		*(18,871,910)*	-
5. Current financial liabilities	21	90,092,567	105,682,938
of which: related parties		*497,000*	*531,125*
6. Other current liabilities	25	196,944,709	125,568,586
of which: related parties		*15,724,498*	*4,646,208*
Total current liabilities		**3,638,293,032**	**3,311,673,673**
TOTAL LIABILITIES AND EQUITY		**16,141,872,545**	**16,090,161,949**

Statement of changes in equity

31 DECEMBER 2017 - 31 DECEMBER 2018
SHARE CAPITAL AND RESERVES OF TERNA S.P.A.

(€m)

	SHARE CAPITAL	LEGAL RESERVE	SHARE PREMIUM RESERVE	CASH FLOW HEDGE RESERVE	OTHER RESERVES	RETAINED EARNINGS/ (ACCUMULATED LOSSES)	INTERIM DIVIDEND	PROFIT FOR THE YEAR	EQUITY
EQUITY AT 31 DECEMBER 2017	442.2	88.4	20.0	(12.2)	729.5	1,916.7	(149.3)	640.0	3,675.3
Change in accounting standards						(1.3)			(1.3)
RESTATED EQUITY AT 1 JANUARY 2018	442.2	88.4	20.0	(12.2)	729.5	1,915.4	(149.3)	640.0	3,674.0
PROFIT FOR THE YEAR								661.3	661.3
OTHER COMPREHENSIVE INCOME:									
Change in fair value of cash flow hedges.after taxation				(32.5)					(32.5)
- Financial assets at fair value through other comprehensive income, after taxation					1.1				1.1
- Cost of hedges after taxation				(1.8)					(1.8)
Total other comprehensive income	-	-	-	(34.3)	1.1	-	-	-	(33.2)
COMPREHENSIVE INCOME	-	-	-	(34.3)	1.1	-	-	661.3	628.1
TRANSACTIONS WITH SHAREHOLDERS:									
Appropriation of profit for 2017:									-
- Retained earnings						197.8		(197.8)	-
- Dividends							149.3	(442.2)	(292.9)
Interim dividend 2018							(158.2)		(158.2)
Total transactions with shareholders	-	-	-	-	-	197.8	(8.9)	(640.0)	(451.1)
Other changes						(0.1)			(0.1)
EQUITY AT 31 DECEMBER 2018	442.2	88.4	20.0	(46.5)	730.6	2,113.1	(158.2)	661.3	3,850.9

31 DECEMBER 2016 - 31 DECEMBER 2017
SHARE CAPITAL AND RESERVES OF TERNA S.P.A.

(€m)

	SHARE CAPITAL	LEGAL RESERVE	SHARE PREMIUM RESERVE	*CASH FLOW HEDGE RESERVE*	OTHER RESERVES	RETAINED EARNINGS/ (ACCUMULATED LOSSES)	INTERIM DIVIDEND	PROFIT FOR THE YEAR	EQUITY
EQUITY AT 31 DECEMBER 2016	442.2	88.4	20.0	(18.1)	729.5	1,372.2	(144.9)	535.5	3,024.8
PROFIT FOR THE YEAR								640.0	640.0
OTHER COMPREHENSIVE INCOME:									
Change in fair value of cash flow hedges, after taxation				5.9					5.9
Total other comprehensive income	-	-	-	5.9	-	-	-	-	5.9
COMPREHENSIVE INCOME	-	-	-	5.9	-	-	-	640.0	645.9
TRANSACTIONS WITH SHAREHOLDERS:									
Appropriation of profit for 2016:									-
- Retained earnings						121.5		(121.5)	-
- Dividends							144.9	(414.0)	(269.1)
Merger contribution						423.0			423.0
Interim dividend 2017							(149.3)		(149.3)
Total transactions with shareholders	-	-	-	-	-	544.5	(4.4)	(535.5)	4.6
EQUITY AT 31 DECEMBER 2017	442.2	88.4	20.0	(12.2)	729.5	1,916.7	(149.3)	640.0	3,675.3

Statement of cash flows

(€m)

	2018	2017
PROFIT FOR THE YEAR ADJUSTED BY:	**661.3**	**640.0**
Amortisation, depreciation and impairment losses /(reversals of impairment losses) on non-current property, plant and equipment and intangible assets*	508.9	485.5
Accruals to provisions (including provisions for employee benefits) and impairment losses	33.9	64.3
(Gains)/Losses on sale of property, plant and equipment	(3.0)	(1.7)
Financial (income)/expense	78.7	80.1
Income tax expense	257.9	261.6
CASH FLOW FROM OPERATING ACTIVITIES BEFORE CHANGES IN NET WORKING CAPITAL	**1,537.7**	**1,529.8**
Increase/(decrease) in provisions (including provisions for employee benefits and taxation)	(39.0)	(2.1)
of which merger contribution	-	*48.2*
(Increase)/decrease in inventories	5.3	(5.4)
(Increase)/decrease in trade receivables and other current assets	121.8	230.2
Increase/(decrease) in trade payables and other current liabilities	81.4	125.7
Increase/(decrease) in other non-current assets	(21.1)	(23.7)
Increase/(decrease) in other non-current liabilities	19.9	16.9
Interest income and other financial income received	3.0	352.4
Interest expense and other financial expenses paid	(228.3)	(228.7)
Income tax paid	(272.6)	(337.1)
CASH FLOW FROM OPERATING ACTIVITIES [A]	**1,208.1**	**1,658.0**
- of which: related parties	*55.2*	*50.5*
Change in non-current property, plant and equipment	(793.8)	(1,774.9)
of which purchase of non-current property, plant and equipment after grants collected	*(793.8)*	*(685.7)*
of which merger contribution	-	*(1,089.2)*
Proceeds from the sale of non-current property, plant and equipment and other movements	4.8	(7.6)
Change in non-current intangible assets	(58.4)	(40.1)
of which intercompany additions	*(6.6)*	-
of which merger contribution	-	*(1.6)*
Capitalised financial expenses	15.1	12.3
Goodwill resulting from merger	-	(101.6)
(Increase)/decrease in investments	(55.7)	529.7
of which merger contribution	-	*559.7*
CASH FLOW FOR INVESTING ACTIVITIES [B]	**(888.0)**	**(1,382.2)**
- of which: related parties	*(6.4)*	*(8.4)*
Changes in equity due to merger	-	423.0
Increase/(decrease) in retained earnings and accumulated losses	(1.4)	-
Dividends paid	(451.1)	(418.4)
Movements in short- and medium/long-term financial liabilities (including short-term portion)**	(19.7)	341.0
Movement in short-term loans and borrowings	(179.5)	129.0
Movements in short-term financial investments	(401.5)	-
CASH FLOW FROM FINANCING ACTIVITIES [C]	**(1,053.2)**	**474.6**
- of which: related parties	*(99.1)*	*39.0*
INCREASE/(DECREASE) IN CASH AND EQUIVALENTS [A+B+C]	**(733.1)**	**750.4**
Cash and cash equivalents at beginning of year	1,678.2	927.8
Cash and cash equivalents at end of year	945.1	1,678.2

* *After grants related to assets recognised in the income statement for the year*
** *After derivatives and impact of fair value adjustments*

Notes

A. Accounting policies and measurement criteria

Introduction

Terna S.p.A., which provides electricity transmission and dispatching services, is a joint-stock company and its registered office is at Viale Egidio Galbani 70, Rome, Italy.
These financial statements were authorised for publication by the Board of Directors on 20 March 2019.
The financial statements at and for the year ended 31 December 2018 are available for inspection on request at Terna S.p.A.'s registered office at Viale Egidio Galbani 70, Rome, or on the Company's website at www.terna.it.
The Board of Directors has authorised the Chairwoman and the Chief Executive Officer to make any alterations to the form of the financial statements and any additions and adjustments to the sections concerning significant subsequent events.

Compliance with IAS/IFRS

The separate financial statements at and for the year ended 31 December 2018 have been prepared in accordance with International Financial Reporting Standards (IFRS), International Accounting Standards (IAS) issued by the International Accounting Standards Board (IASB) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and the Standing Interpretations Committee (SIC), as endorsed by the European Commission ("EU-IFRS").
This document has also been prepared taking into account the provisions of Legislative Decree 38 of 28 February 2005 of the Italian Civil Code and CONSOB Resolutions 15519 (*"Provisions governing financial statements in implementation of art. 9, paragraph 3 of Legislative Decree 38/2005"*) and 15520 ("*Amendments to the implementing rules for Legislative Decree 58/1998*"), as well as CONSOB Communication DEM/6064293 ("*Disclosure requirements for listed issuers and issuers of financial instruments that are widely held among the public pursuant to art. 116 of the Consolidated Law on Finance*").
The separate financial statements have been prepared on a historical cost basis, with the exception of certain financial instruments, and on a going concern basis.

Basis of presentation

The separate financial statements consist of the statement of financial position, the income statement, the statement of comprehensive income, the statement of cash flows, the statement of changes in equity and the notes thereto.
In the statement of financial position, assets and liabilities are classified on a "current/non-current" basis, with separate reporting of assets and liabilities held for sale. Current assets, which include cash and cash equivalents, are those held for realisation, sale or consumption in the Company's normal operating cycle; current liabilities are those expected to be settled in the Company's normal operating cycle or within one year of the end of the financial year.
The income statement is classified on the basis of the nature of costs. The income statement is presented as two statements, the first of which (the income statement) presents revenue and expense items for the year; the second (the statement of comprehensive income) starts with the result for the year and then presents the revenue and expense items (including reclassification adjustments) that are recognised in equity rather than profit or loss for the year.
The statement of cash flows has been prepared using the indirect method.
The separate financial statements are accompanied by the Integrated Report for Terna S.p.A. and the Group, which as from financial year 2008 has been prepared as a single document, exercising the option granted by Legislative Decree 32 of 2 February 2007, which amended art. 40 (Integrated Report) of Legislative Decree 127 of 9 April 1991.

The separate financial statements are presented in euros, whilst amounts in the notes are presented in millions of euros, unless otherwise stated.
The separate financial statements have been prepared on a historical cost basis, with the exception of certain items that, in accordance with EU-IFRS, are recognised at fair value, as indicated in the measurement criteria for individual items.

It should be noted that, for the purposes of comparison, certain amounts in the financial statements for the year ended 31 December 2017 have been restated, without, however, altering amounts in equity at 31 December 2017 or those in the income statement and the statement of comprehensive income for 2017.

Use of estimates

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

Impairment losses

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

Allowance for doubtful accounts

Trade receivables are initially recognised at fair value net of any losses relating to sums considered non-recoverable, for which specific provisions have been made in the allowance for doubtful accounts. The new accounting standard, IFRS 9, adopted from 1 January 2018, has introduced the application of a model based on expected credit losses. This requires the Company to assess expected credit losses, and the related changes, at each reporting date, superseding the approach used in IAS 39. It is, therefore, no longer necessary for a trigger event to occur before the recognition of losses on receivables.
Specifically, the Company has applied the simplified approach permitted by IFRS 9 to trade receivables, finance lease receivables and assets deriving from contracts with customers, in order to measure the allowance for doubtful accounts based on expected losses over the life of the receivable. The Company has thus determined the amount of expected credit losses using a provisioning matrix, based on information regarding historical credit losses for similar past due exposures, adjusted to take into account current conditions and forward-looking elements.

Provisions for risks and charges

Provisions for risks and charges are allocated when a disbursement of cash, for an amount which can be reliably estimated, will be necessary to fulfil a legal or constructive obligation arising as a result of a past event. Liabilities that can be associated with legal and tax disputes and liabilities associated with urban and environmental restoration projects are estimated by the Company. The measurement of provisions for legal disputes is based on the probability of incurring an expense, including through the use of external legal advisors supporting the Company; the estimate of provisions to be set aside for urban and environmental restoration projects, the "offsets" aimed at compensating for the environmental impact of the construction of new plant, is based on an analysis of the agreements entered into with the local authorities concerned and the progress of work on construction of the new plant. Where the time value of money is significant, provisions are discounted, using a rate that the Company believes to be appropriate (a rate is used gross of taxes, which reflects current market conditions and the specific risks connected with the liability). After initial recognition, the value of the provisions for risks and charges is updated to reflect the passage of time and any changes in the estimate following alterations to the amounts forecast, the timing and the discount rates used. Any increase in provisions associated with the passage of time is recognised in the income statement under "Financial expenses".

Employee benefits

The liability for employee benefits paid upon or following termination of employment in relation to defined benefit plans or other long-term benefits is recognised net of any plan assets and is measured on the basis of actuarial assumptions, estimating the amount of future benefits that employees have vested at the reporting date. The actuarial valuations used to quantify employee benefits (of all plans except termination benefits or *TFR*) were based on "vested benefits", applying the projected unit credit method. These valuations are based on economic and demographic assumptions: the discount rate (used to determine the current value of the obligation, determined considering returns on high quality bonds in line with the duration of the group of workers measured), the inflation rate, the rate at which future salary levels are expected to rise, the rate of increase for average health reimbursements, rate of increase for electricity prices and demographic factors, such as mortality and invalidity, retirement, resignation, advances and household composition.

Investments in subsidiaries and associates

Investments in subsidiaries are investments where Terna has the power to directly or indirectly govern the financial and operating policies of the investee so as to obtain benefits from its activities. Associates are investees over which Terna exercises significant influence.
In assessing whether or not Terna has control or significant influence, being the ability to participate in the determination of these companies' financial and operating policies, without having control or joint control, potential voting rights that are exercisable or convertible are also taken into account.
Investments in subsidiaries and associates are recognised at cost, written down in the event of an impairment loss. If the circumstances that gave rise to the impairment cease to exist, the value of the investment is restored to the extent of the impairment loss recognised and the reversal is recognised in the income statement.

In the event that the loss attributable to the Company exceeds the carrying amount of the equity interest, and the Company is required to meet the legal or constructive obligations of the investee or, in any case, to cover its losses, any excess is recognised in a specific provision.

Translation of foreign currency items

Terna's financial statements are prepared in euros, the Company's functional currency. In the financial statements, all transactions in currencies other than the functional currency are recognised at the exchange rate prevailing on the date of the transaction. Monetary assets and liabilities in currencies other than the functional currency are subsequently adjusted at the exchange rate prevailing at year end. Any translation differences are taken to the income statement.
Non-monetary assets and liabilities in foreign currency stated at historical cost are converted at the exchange rate prevailing when the transaction was initially recognised. Non-monetary assets and liabilities in foreign currency stated at fair value are converted at the exchange rate prevailing when fair value was measured.

Property, plant and equipment

Property, plant and equipment is recognised at historical cost, including costs directly attributable to preparing the asset for its intended use. In the event of legal or constructive obligations, cost also includes the present value of the estimated cost of dismantling or removing the asset. The corresponding liability is recognised in provisions for risks and charges. Borrowing costs directly attributable to the purchase, construction or production of an asset that qualify for capitalisation pursuant to IAS 23 are capitalised as part of the cost of the asset. Costs incurred after purchase are recognised as an increase in the carrying amount of the asset to which they relate if it is probable that the future benefits of that cost will flow to the Company, and if the cost can be reliably measured. All other costs are expensed as incurred.
Each element of an item of property, plant and equipment of material value, with respect to the total value of the item to which it belongs, is recognised and depreciated separately.
Property, plant and equipment is shown net of accumulated depreciation and any impairment losses. Depreciation is calculated on a straight-line basis over the estimated useful economic life of the asset, which is reviewed annually, with revisions applied on a prospective basis. Depreciation of an asset begins when the asset becomes available for use.
Liabilities associated with items of property, plant and equipment are taken to a specific provision as a contra account of the related asset. The amount is taken to the income statement through the depreciation of the asset.
Property, plant and equipment is written off either at the time of disposal or when no future economic benefit is expected from their use or disposal. Any profit or loss, recognised in the income statement, is determined as the difference between the net proceeds deriving from disposal and the net carrying amount of the assets eliminated.

The main rates of depreciation, calculated on the basis of the useful lives of the relevant assets, are as follows

RATES OF DEPRECIATION

Civil and industrial buildings	2.50%
Transmission lines	2.22%
Transformer substations:	
- Electrical machinery	2.38%
- Electrical devices and equipment	3.13%
- Automation and control systems	6.70%
Central systems for remote management and control:	
- Devices, electrical equipment and ancillary plant	5.00%
- Computers	10.00%

The estimated useful life of transmission lines has been reviewed to take account of empirical evidence, primarily of physical deterioration and technical obsolescence. This process has resulted in the reasonable conclusion that the expected useful life of transmission lines should be raised to 45 years (from the 40 years previously used). Based on similar considerations, ARERA has conducted its own review of the useful life of the lines for regulatory purposes (see Resolution 654/2015/R/eel).
Land, regardless of whether it is free of constructions or related to civil and industrial buildings, is not depreciated, since it has an indefinite useful life.
Property, plant and equipment obtained under finance leases - and through which the Company has substantially acquired all the risks and rewards of ownership - are recognised as the Company's assets at the lower of fair value and the present value of the minimum lease payments due, including any amounts to be paid to exercise the purchase option. The corresponding liability to the lessor is recognised as a financial liability. Assets are depreciated using the criteria and rates described above. If the Company is not reasonably certain that it will acquire ownership at the end of the lease, the asset is depreciated over the shorter of the term of the lease and the asset's useful life.

Intangible assets

Intangible assets, which all have finite useful lives, are recognised at cost and shown net of accumulated amortisation and any impairment losses. Amortisation begins when the asset becomes available for use and is calculated on a straight-line basis over the estimated useful life of the related asset, which is reviewed annually. Any revisions to estimated figures are applied on a prospective basis.
Intangible assets essentially consist of the concession to exclusively provide electricity transmission and dispatching services, granted to Terna S.p.A., on 1 November 2005, with the acquisition of the TSO business unit. As established in the Decree issued by the Ministry of Productive Activities on 20 April 2005, this concession has a 25-year term, renewable for another 25 years, from the date of effective transfer of the activities, functions, assets and legal arrangements of the concession from GSE (formerly GRTN) to Terna S.p.A.. This intangible asset was initially recognised at cost, which reflected fair value.
Other intangible assets essentially refer to software developments and upgrades.
Development costs are capitalised by the Company only if they can be reliably estimated and there is the technical possibility and intention to complete the intangible asset so that it will be available for use, and the asset can be used and it is possible to demonstrate that it will generate probable future economic benefits.
Financial expenses directly attributable to the acquisition, construction or production of a non-current asset which justifies capitalisation pursuant to IAS 23 are capitalised to the asset as part of its cost.
All other development costs and research expenses are recognised in the income statement when incurred.
These intangible assets are amortised over their estimated residual useful life, which is normally three years, given their rapid obsolescence.

Infrastructure rights

Infrastructure includes the property, plant and equipment and intangible assets employed in dispatching activities in Italy and in the operations in Peru. These activities are carried out under concession arrangements, which fall within the scope of application of IFRIC 12, since the services provided are regulated and control exists over the residual interest. More specifically, infrastructure rights have been recognised as an intangible asset, as valued on the basis of the Intangible Asset model, given the return generated by dispatching activities thanks to the charges paid by users.
The revenue and costs relating to investment in dispatching activities are recognised with reference to the contracts concerned on a stage-of-completion basis; revenue recognised during the construction phase is limited to the amount of the internal and external construction costs incurred, considering that the fair value of the construction services is equivalent to the construction cost paid to third-party contractors plus the internal cost of the technical personnel employed on such construction activities. The assets continue to be amortised and depreciated in accordance with the initial schedule.
By contrast, dispatching revenue continues to be recognised in accordance with IFRS 15 and financial expenses continue to be capitalised pursuant to IAS 23.
IFRIC 12, instead, is not applicable to the part of the Parent Company's concession arrangement relating to transmission activities, since neither the concession nor the related legislation envisages that ownership of the NTG is to be restored to the public grantor, even for a consideration.

Goodwill

Goodwill, deriving from the acquisition of subsidiaries, is allocated to each of the identified cash generating units (CGU) or groups of CGUs, coinciding with Group companies that own electricity transmission grids. Goodwill is not amortised after initial recognition but is adjusted to reflect impairment losses, measured as described below. Goodwill relating to investments in associates and joint ventures is included in the carrying amount of those companies. Where negative goodwill arises, it is recognised in the income statement at the time of acquisition.

Inventories

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

Financial instruments

Financial assets

The new standard, IFRS 9 - Financial Instruments, effective from 1 January 2018, is divided into the following phases: classification and measurement, derecognition, impairment and hedge accounting.
In order to classify and measure financial instruments, the Company recognises financial assets at fair value inclusive of transaction costs.
Financial assets represented by debt instruments, and falling within the scope of application of the standard, may be measured at amortised cost, at fair value through other comprehensive income or at fair value through profit or loss, depending on the business model adopted to manage the financial assets and the characteristics of the contractual cash flows.

In accordance with the provisions of IFRS 9, the Company correctly classifies these assets based on the results of co-called SSPI ("solely payments of principal and interest") tests. Under this test, assets may be recognised at amortised cost or fair value through other comprehensive income if they generate cash flows that are solely payments of principal and interest on the principal amount outstanding. This measurement is applied at the level of each individual instrument.

Specifically, the Company measures financial assets:
- at amortised cost, if the financial asset is held with the aim of collecting the contractual cash flows that meet the SPPI test, as the cash flows represent solely payments of principal and interest;
- at fair value through other comprehensive income ("FVOCI"), if the financial asset is held within a business model whose objective is achieved by collecting the contractual cash flows and by selling the financial asset, and the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. Changes in fair value after initial recognition are recognised in other comprehensive income and recycled through profit or loss on derecognition;
- at fair value through profit or loss ("FVTPL"), of the asset is not held in one of the above business models. This category primarily includes derivative financial instruments held for trading and debt instruments with contractual cash flows that are not solely payments of capital and interest.

Trade receivables

Trade receivables are initially recognised at fair value and subsequently measured at amortised cost, using the effective interest method. Receivables with due dates that reflect normal commercial terms are not discounted.
In accordance with the provisions of IFRS 9, the Company's trade receivables fall within the hold to collect business model, as these assets are held with the objective of collecting the cash flows primarily by collecting the contractual cash flows, the receivables primarily fall due within 12 months and do not include a significant financial component, and the Company does not intent to sell such receivables.

Trade receivables are recognised net of any losses recognised in a specific allowance for doubtful accounts (identified on the basis described in the paragraph, "Allowance for doubtful accounts"). The new standard, IFRS 9, adopted from 1 January 2018, has introduced application of a model based on expected credit losses. This requires the Company to assess expected credit losses, and the related changes, at each reporting date, superseding the approach used in IAS 39. It is, therefore, no longer necessary for a trigger event to occur before the recognition of losses on receivables. Specifically, the Company has applied the simplified approach permitted by IFRS 9 to trade receivables, finance lease receivables and assets deriving from contracts with customers, in order to measure the allowance for doubtful accounts based on expected losses over the life of the receivable. The Company has thus determined the amount of expected credit losses using a provisioning matrix, based on information regarding historical credit losses for similar past due exposures, adjusted to take into account current conditions and forward-looking elements.

Cash and cash equivalents

Cash and cash equivalents are recognised at nominal value and include amounts that are available on demand or can be readily converted into a known amount of cash and are subject to an insignificant risk of changes in value.

Trade payables

Trade payables are initially recognised at fair value and subsequently stated at amortised cost. If their due dates reflect normal commercial terms, they are not discounted. The introduction of IFRS 9 has not led to material changes in the method of accounting for these payables.

Financial liabilities

Financial liabilities are recognised at the settlement date and measured at fair value, net of directly related transaction costs. Subsequently, financial liabilities are measured at amortised cost, using the original effective interest method. If the liabilities are covered by fair value hedges, they are adjusted to reflect changes in fair value with respect to the hedged risk.
Subsequent measurement of financial liabilities depends on their classification as financial liabilities at amortised cost or at fair value through profit or loss.

Derivative financial instruments

Derivatives are recognised at fair value at the trade date. The qualifying criteria applied in classifying derivatives as eligible for hedge accounting are as follows:
- the hedging relationship consists only of eligible hedging instruments and eligible hedged items;
- at the inception of the hedging relationship there is formal designation and documentation of the hedging relationship and the entity's risk management objective and strategy for undertaking the hedge. That documentation includes identification of the hedging instrument, the hedged item, the nature of the risk being hedged and how the entity will assess whether the hedging relationship meets the hedge effectiveness requirements (including its analysis of the sources of hedge ineffectiveness and how it determines the hedge ratio);

- the hedge ratio in the hedging relationship is the same as the ratio between the quantity of the hedged item that the entity effectively hedges and the quantity of the hedging instrument that the entity effectively uses to hedge the quantity of the hedged item.

An entity shall discontinue hedge accounting prospectively only when the hedging relationship (or a part of a hedging relationship) ceases to meet the qualifying criteria. This includes instances when the hedging instrument expires or is sold, terminated or exercised. For this purpose, the replacement or rollover of a hedging instrument into another hedging instrument is not an expiration or termination if such a replacement or rollover is part of, and consistent with, the entity's documented risk management objective.

For hedge accounting purposes, there are three types of hedge:
- fair value hedges when the hedge regards the exposure to changes in the fair value of the recognised asset or liability or there is an unrecognised firm commitment;
- cash flow hedges when the hedge regards the exposure to variability in cash flows that is attributable to a particular risk associated with all of the recognised asset or liability or a highly probable forecast transaction or the exchange rate risk on an unrecognised firm commitment;
- the hedge of a net investment in a foreign operation;

When derivatives cover the risk of changes in the cash flows of the hedged instruments (cash flow hedges), the portion of changes in the fair value qualifying as effective is initially recognised in "Other comprehensive income" and subsequently in profit or loss, as the cash flows from the hedged item affects profit or loss. The portion of the fair value of the hedging instrument that does not qualify as effective is recognised in profit or loss.
When hedging derivatives cover the risk of changes in the fair value of hedged instruments (fair value hedges), they are recognised at fair value in profit or loss. Accordingly, the hedged items are adjusted to reflect changes in the fair value associated with the hedged risk.
Changes in the fair value of derivatives that do not meet hedge accounting requirements in accordance with the EU-IFRS are recognised in profit or loss.
Fair value is measured on the basis of official quotations for instruments traded in regulated markets. The fair value of instruments not traded in regulated markets is measured by discounting projected cash flows along a yield curve prevailing in the market at the reporting date, and by translating amounts in currencies other than the euro at closing exchange rates.
Financial and non- financial contracts (which are not already measured at fair value) are also analysed to identify any embedded derivatives, which must be separated and measured at fair value.
This analysis is conducted at the time the entity becomes party to the contract or when the contract is renegotiated in a manner that produces a material change in the original associated cash flows.

Employee benefits

The liability associated with employee benefits payable on or after termination of employment relate to defined benefit plans (deferred compensation benefits, additional months' pay, payment in lieu of notice, energy discounts, ASEM health cover and other benefits) or other long-term employee benefits (loyalty bonuses) and is recognised net of any plan assets. The liability is measured separately for each plan on the basis of actuarial calculations that estimate the amount of vested future benefits that employees have accrued at the reporting date. The liability is recognised on an accruals basis over the vesting period and is measured by independent actuaries.

Provisions for risks and charges

Provisions set aside for risks and charges are recognised when, at the reporting date, the Company has a legal or constructive obligation as the result of a past event and it is probable that an outflow of resources will be required to settle the obligation and a reliable estimate can be made of the amount of the disbursement. Where the effect is material, provisions are made by discounting estimated future cash flows using a discount rate that reflects current market rates and the specific risk applicable to the obligation, if any. Where

discounting is used, the increase in the provisions due to the passage of time is recognised in the income statement as a financial expense. If it relates to property, plant and equipment (site disposal and restoration, for example), the provision is recognised as a contra entry to the asset to which it relates. The expense is recognised in the income statement through depreciation of the item of property, plant and equipment to which it relates.
Changes in the estimates are recognised in the income statement for the year in which the change occurs, except for the expected costs of dismantling, removal and restoration resulting from changes in the timing and use of the economic resources necessary to extinguish the obligation, or are attributable to a material change in the discount rate. These costs are recognised as an increase or reduction in the related assets and recognised in the income statement through depreciation.

Government grants

Government grants are recognised when there is a reasonable certainty that they will be received and that the Company will comply with all the conditions required for disbursement. Grants received in relation to specific assets whose value is recognised under non-current assets are recognised, in the case of plant already in operation at 31 December 2002, among other liabilities and taken to the income statement over the depreciation period for the assets in question. As of the 2003 financial year, grants related to new plant entering service are recognised as a direct reduction in the non-current asset concerned. Grants related to income are recognised in the income statement when the conditions for recognition are met.

Revenue

The Company's revenue can be categorised as follows:

- **Revenue from sales and services**, including revenue from contracts with customers and therefore falling within the scope of IFRS 15.
  In accordance with the provisions of IFRS 15, applied from 1 January 2018, revenue from contracts with customers is recognised when the performance obligations identified in the contract are satisfied and control over the goods or services is transferred to the customer for an amount that reflects the consideration that the Company expects to receive in exchange for the goods or services.
  The standard envisages two methods for identifying the correct time at which to recognise the revenue attributable to each performance obligation: at contract inception, the Company determines if the goods or services covered by the performance obligation will be transferred to the customer over a period of time or at a point in time:
  - *Revenue from the sale* of goods is recognised when control of the goods is transferred to the customer (at a point in time). The Company determines if there are other promises in the contract representing a performance obligation to which a part of the transaction consideration must be allocated. In determining the sale price, the Company takes into account the effects of a variable consideration, significant financial components, non-monetary components and amounts to be paid to the customer (if present);
  - *Revenue from services* is recognised with reference to the stage of completion of the activity, in accordance with the provisions of IFRS 15 (over a period of time).
- **Other revenue and income**, which includes revenue from lease arrangements (which from 1 January 2019 are governed by IFRS 16) and other residual forms of revenue, included within the scope of application of IFRS 15, deriving from sales of goods not forming part of the Company's ordinary activities.

Financial income and expenses

Financial expenses directly attributable to the acquisition, construction or production of an asset that qualify for capitalisation are capitalised as part of the cost of the asset. The property, plant and equipment and intangible assets involved are those that require at least one year in order to prepare them for use. The directly attributable financial expenses are expenses that would not have been incurred had the expenditure for the asset not been incurred.
Where funds are borrowed specifically, the costs eligible for capitalisation are the actual costs incurred less any income earned on the temporary investment of such borrowings. Where loans are obtained for general

purposes, the eligible amount is determined by applying a capitalisation rate to the expenditure on that asset equal to the weighted average of the financial expenses applicable to the borrowings outstanding for the year, excluding any specifically borrowed funds. The amount of capitalised financial expenses during a year will in any case not exceed the amount of financial expenses incurred during that year.
Capitalisation commences as from the date all the following conditions are first met: (a) expenditure has been incurred for the asset; (b) financial expenses have been incurred; and (c) the activities involved in preparing the asset for its intended use or sale are in progress. Capitalisation ceases when the activities involved in preparing the asset for its intended use or sale are substantially complete.
The average capitalisation rate used for 2018 was 1.23% (the rate for 2017 was 1.30%).
Financial income and expenses other than capitalised amounts are recognised on an accruals basis in respect of the interest on the net value of the related financial assets and liabilities, using the effective interest rate.

Dividends

Dividends from investees are recognised when the shareholders' right to receive payment is established. Dividends and interim dividends payable to shareholders are shown as changes in equity at the date in which they are approved by the General Meeting of shareholders and the Board of Directors, respectively.

Income taxes

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

New accounting standards

International financial reporting standards effective as of 1 January 2018

Two new accounting standards, whose application has not had a material impact for the Company, and a number of new amendments to standards already applied came into effect from 1 January 2018.

The following information is provided with regard to the new accounting standards:

IFRS 15 - Revenue from Contracts with Customers

On 29 October 2016, the European Commission endorsed the new IFRS 15 on revenue recognition. The new standard introduced a five-step revenue recognition model. The steps are as follows: 1) identification of the contract; 2) identification of the performance obligations in the contract; 3) determination of the transaction price; 4) allocation of the transaction price; 5) recognition of revenue when the performance obligation is satisfied. Under the standard, the obligation is satisfied when control over the goods or services underlying the performance obligation is transferred to the customer. Control is defined as the ability to direct the use of and obtain substantially all of the remaining benefits from the asset.

The purpose of the new standard is to provide a consistent, overall framework for revenue recognition, applicable to all contracts with customers (with the exception of leases, insurance contracts and financial instruments). The new standard replaced all existing revenue recognition requirements under IFRS. Specifically, it replaced the following standards:
- IAS 11 - Construction Contracts and related interpretations;
- IAS 18 - Revenue;
- IFRIC 13 - Customer Loyalty Programmes;
- IFRIC 15 - Agreements for the Construction of Real Estate;
- IFRIC 18 - Transfers of Assets from Customers;
- SIC 31 - Revenue - Barter Transactions Involving Advertising Services.

In addition, on 31 October 2016, the European Commission endorsed guidance to clarify certain practical aspects brought to the fore during discussion of the TRG (Transition Resource Group for Revenue Recognition) regarding the application of IFRS 15: identifying performance obligations, principal versus agent considerations and application guidance on licensing. The new standard was effective from 1 January 2018, with early and retrospective application permitted.

Terna has applied the new standard from 1 January 2018, using the modified retrospective approach, accounting for the cumulative effect of adoption of IFRS 15 from the date of first-time adoption, electing not to apply the standard to completed contracts.

IFRS 9 - Financial Instruments

On 22 November 2016, the European Commission approved IFRS 9 - Financial Instruments, in its final version of 24 July 2014, which starts the complex and detailed process of replacing IAS 39, divided into the following phases: classification and measurement, derecognition, impairment and hedge accounting. The new standard was effective from 1 January 2018, with early application permitted. The main changes introduced by the new standard include, among other things, unified classification guidance for all types of financial instruments, including the requirements for recognition and measurement, impairment, derecognition and hedge accounting. Financial assets will therefore be classified as a whole and not subject to complex separation rules. The new classification criterion for financial instruments is based on the business model adopted by the Company to manage financial assets with reference to the collection of cash flows and to the characteristics of the contractual cash flows of the financial assets. As regards impairment, the model provided for in IAS 39 based on the criterion of incurred loss, which postponed the recognition of losses on receivables to the moment of occurrence of the trigger event, has been replaced, as it was considered a weakness. The new IFRS 9 provides for a model based on a prospective view, which requires the immediate recognition of losses on receivables expected over the life of the financial instrument, as a trigger event no longer needs to occur before the recognition of losses on receivables. The new standard has also completed the stage of the Hedge accounting project, except for the rules on macro hedge accounting, which will be published at a later date. It provides, among the other changes, for a substantial revision of hedge accounting so as to better reflect risk management activities in the financial statements.

Terna has applied the new standard retrospectively from 1 January 2018 with regard to classification and measurement, derecognition and impairment, with presentation of the cumulative effects of first-time adoption at the transition date in equity.

The following table shows changes in the consolidated statement of financial position at 1 January 2018 as a result of application of the two standards, IFRS 15 and IFRS 9.

(€)

	AT 31 DECEMBER 2017	IMPACT OF IFRS 9	IMPACT OF IFRS 15	RESTATED AT 1 JANUARY 2018
A - NON-CURRENT ASSETS				
1. Property, plant and equipment	11,705,228,618			11,705,228,618
2. Goodwill	190,228,231			190,228,231
3. Intangible assets	234,080,643			234,080,643
4 Deferred tax assets				
5. Non-current financial assets	1,009,659,871			1,009,659,871
6. Other non-current assets	3,526,176			3,526,176
Total non-current assets	**13,142,723,539**	**-**	**-**	**13,142,723,539**
B - CURRENT ASSETS				
1. Inventories	5,307,324			5,307,324
2. Trade receivables	1,142,545,872	(431,566)	-	1,142,114,306
3. Current financial assets	213,317			213,317
4. Cash and cash equivalents	1,678,217,732	(1,408,479)	-	1,676,809,253
5. Income tax assets	57,927,658			57,927,658
6. Other current assets	63,226,507			63,226,507
Total current assets	**2,947,438,410**	**(1,840,045)**	**-**	**2,945,598,365**
TOTAL ASSETS	**16,090,161,949**	**(1,840,045)**		**16,088,321,904**
C - EQUITY				
1. Share capital	442,198,240			442,198,240
2. Other reserves	825,639,778			825,639,778
3. Retained earnings/(accumulated losses)	1,916,706,986	(1,344,885)	-	1,915,362,101
4. Interim dividend	(149,268,036)			(149,268,036)
5. Profit for the year	640,042,878			640,042,878
Total equity	**3,675,319,846**	**(1,344,885)**	**-**	**3,673,974,961**
D - NON-CURRENT LIABILITIES				
1. Long-term borrowings	8,638,448,258			8,638,448,258
2. Employee benefits	12,744,530			12,744,530
3. Provisions for risks and charges	243,496,364	56,938	-	243,553,302
4. Deferred tax liabilities	17,258,091	(552,098)	-	16,705,993
5. Non-current financial liabilities	9,904,232			9,904,232
6. Other non-current liabilities	181,316,955			181,316,955
Total non-current liabilities	**9,103,168,430**	**(495,160)**	**-**	**9,102,673,270**
E - CURRENT LIABILITIES				
1. Short-term borrowings	90,000,000			90,000,000
2. Current portion of long-term borrowings	884,039,788			884,039,788
3. Trade payables	2,106,382,361			2,106,382,361
5. Current financial liabilities	105,682,938			105,682,938
6. Other current liabilities	125,568,586			125,568,586
Total current liabilities	**3,311,673,673**	**-**	**-**	**3,311,673,673**
TOTAL LIABILITIES AND EQUITYITY	**16,090,161,949**	**(1,840,045)**	**-**	**16,088,321,904**

(€)

		IAS 39		IFRS 9
		RECEIVABLES AND LOAN	HELD TO MATURITY	HELD TO COLLECT
	AT 1 JANUARY 2018	RECEIVABLES	ASSETS HELD TO MATURITY	FINANCIAL ASSETS MEASURED AT AMORTISED COST
A – NON-CURRENT ASSETS				
5. Non-current financial assets	1,009,659,871	-	1,009,659,871	1,009,659,871
B – CURRENT ASSETS				
2. Trade receivables	1,142,114,306	1,142,114,306	-	1,142,114,306
3. Current financial assets	213,317	-	213,317	213,317
4. Cash and cash equivalents	1,676,809,253	-	1,676,809,253	1,676,809,253
TOTAL ASSETS		**1,142,114,306**	**2,686,682,441**	**3,828,796,747**

(€)

		IAS 39		IFRS 9	
		OTHER FINANCIAL LIABILITIES	HEDGE ACCOUNTING	OTHER	HEDGE ACCOUNTING
	AT 1 JANUARY 2018	FINANCIAL LIABILITIES MEASURED AT AMORTISED COST	CASH FLOW HEDGES	FINANCIAL LIABILITIES MEASURED AT AMORTISED COST	CASH FLOW HEDGES
C – EQUITY ATTRIBUTABLE TO OWNERS OF THE PARENT					
2. Other reserves	825,639,778	813,388,910	12,250,868	813,388,910	12,250,868
E – NON-CURRENTLIABILITIES					
1. Long-term borrowings	8,638,448,258	8,638,448,258	-	8,638,448,258	-
5. Non-current financial liabilities	9,904,232	-	9,904,232	-	9,904,232
F – CURRENT LIABILITIES					
1. Short-term borrowings	90,000,000	90,000,000	-	90,000,000	-
2. Current portion of long-term borrowings	884,039,788	884,039,788	-	884,039,788	-
3. Trade payables	2,106,382,361	2,106,382,361	-	2,106,382,361	-
5. Current financial assets	105,682,938	105,682,938	-	105,682,938	-
TOTAL LIABILITIES AND EQUITY		**12,637,942,255**	**22,155,100**	**12,637,942,255**	**22,155,100**

The new amendments are not expected to have a material impact, with the main ones described below:

IFRIC 22: Foreign Currency Transactions and Advance Consideration

On 28 March 2018, the European Commission endorsed the interpretation of IAS 21 through Regulation 2018/519. The interpretation providing guidance in the selection of an exchange rate to be used when recording a transaction in a foreign currency, should the consideration in the foreign currency have been received or paid in advance of recognition of the related assets.

Amendment to IFRS 15: Clarifications to IFRS 15 Revenue from Contracts with Customers

On 31 October 2017, the European Commission endorsed the amendment to IFRS 15 through Regulation 2017/1987. This amendment provides clarifications on certain aspects of the standard's requirements and proposes transition relief for entities adopting the standard.

Amendment to IFRS 4: Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts

On 3 November 2017, the European Commission endorsed the amendment to IFRS 4 through Regulation 2017/1988. This amendment aims to remedy the temporary accounting impact of the different effective dates of IFRS 9 and of the new standard governing insurance contracts, IFRS 17, which replaces IFRS 4.

Amendment to IFRS 2: Classification and Measurement of Share-based Payment Transactions

On 26 February 2018, the European Commission endorsed the amendment to IFRS 2 through Regulation 2018/289. This amendment clarifies the classification and measurement of share-based payments.

Amendment to IAS 40: Transfers of Investment Property

On 14 March 2018, the European Commission endorsed the amendment to IAS 40 through Regulation 2018/400. This amendment regards the account impact of changes in the use of a property, and above all clarifies the cases in which an entity is authorised to classify a property as investment property.

International financial reporting standards endorsed but not yet effective

IFRS 16 - Leases

Endorsed on 31 October 2017, the new IFRS 16 governs accounting for leases, replacing the previous IAS 17. Among the changes, the new standard, in dispensing with the distinction between operating and finance leases, bases the accounting presentation on the "right-of-use" approach, which for the lessee makes the accounting uniform for any type of lease. The method of accounting applicable to lessors under IFRS 16 remains substantially unchanged with respect to the current accounting policy under IAS 17. Lessors will continue to classify all leases using the same classification rules applicable under IAS 17 and will distinguish between two types of lease: operating and finance. The standard also includes two recognition exemptions for lessees for leases where the underlying asset is of "low value" (for example, personal computers or assets with a unit value of below US$5,000) and short-term leases (lease arrangements with a lease term of less than or equal to 12 months). Under the accounting standard just described, at the inception date of a lease, the lessee must recognise a lease liability and an asset representing the right to sue the underlying asset during the lease term (the right of use). Lessees must recognise interest expense on the lease liability separately from the depreciation charge on the right-of-use asset.

Terna will adopt the standard from the mandatory effective date of 1 January 2019, retrospectively accounting for the cumulative effect of initial application of the standard at the date of initial application, in accordance with paragraph C8b). In the case of leases previously classified as operating leases (under IAS 17), the Group will recognise:

a) the lease liability at the date of initial application at the present value of the remaining lease payments, discounted using the lessee's incremental borrowing rate at the date of initial application;
b) the right-of-use asset at an amount equal to the lease liability adjusted by the amount of any prepaid or accrued lease payments relating to that lease recognised in the statement of financial position immediately before the date of initial application.

Terna will apply the exemptions put forward by the standard for lease arrangements expiring within 12 months of the initial date of application and for leases where the underlying asset is of low value.
Terna has elected to apply the practical expedient provided for in the standard, excluding leases for which the lease term ends within 12 months of the initial date of application from the calculation, when this term has been determined in application of the guidance provided by IFRS16. However, as required by the standard, Terna will provide a specific disclosure in this regard at the time of initial application and on a continuous basis.
Applying this model, Terna will recognise: (i) assets and liabilities for all leases with terms in excess of twelve months; (ii) depreciation of the recognised assets and interest expense on the lease liability separately in the income statement. The assessment process, which is close to completion, does not indicate that there will be a material impact on the Group's financial statements in 2019 as a result of application of this standard, limited essentially to recognition of the right-of-use assets and the lease liabilities.

Amendment to IFRS 9: Prepayment Features with Negative Compensation
Endorsed by the European Commission on 22 March 2018, with Regulation 2018/498, the amendment to IFRS 9 allows the measurement of certain financial assets with a prepayment option with negative compensation features at amortised cost or at fair value through comprehensive income. The amendment will come into effect from 1 January 2019.

IFRIC 23 - Uncertainty over Income Tax Treatments
Endorsed by the European Commission on 23 October 2018, with Regulation 2018/1595, IFRIC 23 will come into effect from 1 January 2019. The interpretation clarifies who to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. It also provides guidance on how to account for current and deferred tax assets and liabilities.

International financial reporting standards awaiting endorsement

For newly-issued amendments, standards and interpretations that have not yet been endorsed by the EU, but which address issues that affect or could affect the Terna Group, assessments are currently being conducted of the possible impact of their application on the financial statements, taking into account the date on which they will take effect. In particular:

IFRS 17 - Insurance Contracts
The new accounting standard for insurance contracts was published by the IASB on 18 May 2017, to replace the interim version of IFRS 4. The standard defines the new principles for the recognition, measurement, presentation and disclosure of insurance contracts. The General Model of reference is based on the discounting of expected cash flows, with the indication of a risk adjustment and upfront profits through the "contractual service margin", which cannot be negative, released to income over the term of the contract.

Amendment to IAS 28: Long-term Interests in Associates and Joint Ventures
Published by the IASB on 12 October 2017, the amendment to IAS 28 clarifies which long-term receivables are part of the net investment in the associate or joint venture.

Improvements to IFRSs (2015-2017 Cycle)
Published by the IASB on 12 December 2017, the annual improvements related to the 2015-2017 cycle contain minor amendments to IFRS 3, IFRS 11, IAS 12 and IAS 23.

Amendment to IAS 19: Plan Amendment, Curtailment or Settlement
Published by the IASB on 7 February 2018, the amendment to IAS 19 clarifies how pension costs should be calculated in the event of modifications to a defined-benefit plan.

References to the Conceptual framework in IFRS Standards

Published on 29 March 2018, this is an amendment to the Conceptual Framework for Financial Reporting. The main changes regard a new section on measurement, improved definitions and guidance, above all with reference to the definition of liabilities and clarification on concepts such as prudence and measurement uncertainties.

Amendment to IFRS 3: Definition of a Business

Published by the IASB on 22 October 2018, the amendment to IFRS 3 provides a clearer definition of a business, giving guidance and illustrative examples for identifying when a group of assets constitutes a business, thereby falling within the scope of application of IFRS 3.

Amendment to IAS 1 and IAS 8: Definition of Material

As part of the "Disclosure Initiative" project, the amendment to IAS 1 and IAS 8 was published on 31 October 2018. This modifies the definition of materiality in relation to the two standards, in order to standardise and clarify the definitions currently provided in the standards and in the Conceptual Framework.

B. Notes to the income statement

Revenue

1. REVENUE FROM SALES AND SERVICES - €1,892.9 MILLION

(€m)

	2018	2017	CHANGE
Transmission charges billed to grid users	1,657.4	1,674.6	(17.2)
Back-billing of transmission charges for previous years	0.1	(0.1)	0.2
Quality of service bonuses/(penalties)	7.4	7.4	-
Other energy-related revenue and from services performed under concession	168.6	133.0	35.6
Other sales and services	59.4	46.5	12.9
TOTAL	**1,892.9**	**1,861.4**	**31.5**

Transmission charges

This item, amounting to €1,657.5 million, includes revenue from the core business relating to the allowed return due to the Company for use of the National Transmission Grid.

The reduction in transmission revenue (down €17.0 million) broadly reflects revision of the related tariff to reflect completion, in 2017, of revenue from work in progress and a reduction in the volume of energy transported, offset by an increase in the portion of the NTG owned by the Company. The balance also includes the estimated impact of the revised contribution from international interconnections.

Quality of service bonuses/(penalties)

This item, amounting to €7.4 million in 2017, regards the RENS incentive mechanism introduced by Resolution 653/2015/r/eel, calculated on a pro rata basis taking into account the estimated overall results expected in the 2016-2019 regulatory period.

The figure is unchanged with respect to the previous year.

Other energy-related revenue

This item regards dispatching and metering revenue (€111.0 million for the dispatching component and €32.0 million regarding certain expenses not covered by the dispatching charge) and revenue from infrastructure construction and upgrade services performed under concession, recognised in application of IFRIC 12 (€25.5 million).

The increase of €35.6 million compared with the previous year is primarily linked to increases in the dispatching charge and the above expenses (up €31.2 million).

Other sales and services

The item, "Other sales and services", amounting to €59.4 million mainly regards revenue from administrative, support and consultancy services provided to subsidiaries (€22.5 million, including €18.4 million from services rendered to Terna Rete Italia S.p.A.), from connections to the NTG (€1.0 million) and from Non-regulated Activities (€34.2 million), primarily support and housing services for fibre networks (€22.5 million).

The increase of €12.9 million compared with the previous year primarily reflects the following:

- the new classification of revenue from support and housing services for fibre networks, totalling €22.5 million, essentially following the reclassification of this revenue - classified in other revenue and income in 2017 - in application if the new standard, IFRS 15;
- reduced revenue from connection services (down €4.2 million);
- reduced revenue from intercompany administrative, support and consultancy services provided to subsidiaries (down €3.9 million);
- a reduction in other revenue from (down €1.2 million).

Pass-through revenue/expenses

This item regards "pass-through" revenue and expenses (the balance of which amounts to zero). These items result from purchases and sales of electricity from electricity market operators carried out each day. Measurements for each point of injection and withdrawal are taken and the differences, with respect to energy market schedules are calculated. These differences, known as imbalances, are then measured using algorithms established by the regulatory framework. The net charge resulting from calculation of the imbalances and the purchases and sales, carried out by Terna, on the DSM, is billed on a pro rata basis to each end consumer via a specific uplift payment. This item also reflects the portion of the transmission charge that Terna passes on to other grid owners.
The components of these transactions are shown in greater detail below

(€m)

	2018	2017	CHANGE
Power Exchange-related revenue items	**3,860.1**	**4,039.8**	**(179.7)**
- Uplift	1,648.4	2,093.5	(445.1)
- Electricity sales	523.0	434.6	88.4
- Imbalances	506.2	543.6	(37.4)
- Congestion revenue	331.1	368.0	(36.9)
- Charges for right to use transmission capacity and market coupling	66.8	73.7	(6.9)
- Interconnectors/shippers	337.8	297.6	40.2
- Load Profiling for public lighting	75.2	75.1	0.1
- Other Power Exchange-related pass-through revenue items	371.6	153.7	217.9
Total over-the-counter revenue items	**1,443.4**	**1,389.4**	**54.0**
- Transmission revenue passed on to other NTG owners	136.5	135.1	1.4
- Charge to cover cost of essential plants	392.7	327.5	65.2
- Charge to cover cost of energy delivery capacity	277.5	208.9	68.6
- Charge to cover cost of interruptibility service	279.5	359.8	(80.3)
- Charge to cover cost of LV capacity and protection service	276.2	267.6	8.6
- Other pass-through revenue for over-the-counter trades	81.0	90.5	(9.5)
TOTAL PASS-THROUGH REVENUE	**5,303.5**	**5,429.2**	**(125.7)**
Total Power Exchange-related cost items	**3,860.1**	**4,039.8**	**(179.7)**
- Electricity purchases	2,496.5	2,322.9	173.6
- Imbalances	331.5	771.3	(439.8)
- Congestion revenue	217.1	280.6	(63.5)
- Charges for right to use transmission capacity and market coupling	80.6	81.1	(0.5)
- Interconnectors/Shippers	136.1	116.0	20.1
- Load Profiling for public lighting	366.8	330.8	36.0
- Other Power Exchange-related pass-through cost items	231.5	137.1	94.4
Total over-the-counter cost items	**1,443.4**	**1,389.4**	**54.0**
- Transmission costs passed on to other NTG owners	136.5	135.1	1.4
- Fees paid for essential units	392.7	327.5	65.2
- Fees paid for energy delivery capacity	277.5	208.9	68.6
- Fees paid for interruptibility service	279.5	359.8	(80.3)
- Fees paid for LV capacity and protection service	276.2	267.6	8.6
- Other pass-through costs for over-the-counter trades	81.0	90.5	(9.5)
TOTAL PASS-THROUGH COSTS	**5,303.5**	**5,429.2**	**(125.7)**

The total uplift cost in 2018 (including the portion to cover the cost of ITC: inter-TSO compensation and prior year recoveries) amounting to €1,648.4 million, is down €445.1 million on the figure for the previous year, primarily reflecting a reduction in the cost of demand- and supply-side imbalances, linked partly to the application of new regulations effective from September 2017.

2. OTHER REVENUE AND INCOME - €74.7 MILLION

(€m)

	2018	2017	CHANGE
Lease of operations	35.0	33.6	1.4
Revenue from IRU contracts for fibre	10.3	11.0	(0.7)
Insurance proceeds as compensation for damages	8.6	3.2	5.4
Sundry grants	8.3	8.1	0.2
Gains on sale of components of plant	3.2	2.3	0.9
Rental income	3.0	25.3	(22.3)
Sales to third parties	2.4	2.5	(0.1)
Contingent assets	1.3	1.8	(0.5)
Other revenues	2.6	2.3	0.3
TOTAL	**74.7**	**90.1**	**(15.4)**

The most significant components of "Other revenue and income" primarily regard the revenue received from the subsidiary Terna Rete Italia S.p.A., under the agreement for the lease of certain operations (€35.0 million), revenue from IRU contracts for fibre (€10.3 million), insurance proceeds to cover damage to plant (€8.6 million), sundry grants (€8.3 million), primarily in relation to the re-routing of lines for third parties, and gains from the sale of components of plant (€3.2 million).
The reduction of €15.4 million is primarily due to the fact that the figure for 2017 included revenue from support and housing services for fibre networks, totalling €22.1 million, which from 2018 has been reclassified to revenue from sales and services in application of the new standard, IFRS 15, as described above.
The increase also benefitted from an increase in insurance proceeds of €5.4 million.

Operating costs

3. RAW AND CONSUMABLE MATERIALS USED - €5.3 MILLION

This item, amounting to €5.3 million, includes the value of the various materials and supplies, including fuel for the Company's vehicle fleet. The reduction of €4.8 million compared with the previous year is primarily due to materials used in the telecommunications business.

4. SERVICES - €364.6 MILLION

(€m)

	2018	2017	CHANGE
Intercompany services, including technical and administrative services	306.7	297.6	9.1
Maintenance and sundry services	35.7	32.0	3.7
Lease expense	11.7	9.6	2.1
Insurance	6.1	6.2	(0.1)
Remote transmission and telecommunications	0.4	0.3	0.1
IT services	2.7	2.4	0.3
Tender costs for plant	1.3	1.7	(0.4)
TOTAL	**364.6**	**349.8**	**14.8**

The item, "Intercompany services, including technical and administrative services" regards the accrued costs incurred under specific intercompany contracts (€306.7 million), largely regarding the subsidiary Terna Rete Italia S.p.A., which maintains and operates the infrastructure owned by the Company (€270.7 million), provides services relating to investment in the development of the Company's transmission and dispatching infrastructure (€22.9 million) and other activities and services relating to plant owned by third parties (€5.1 million). This item also includes bonuses relating to the quality of the transmission service attributable to Terna Rete Italia S.p.A. (€2.3 million).
Fees payable to members of the Board of Statutory Auditors amount to €0.2 million.
After the costs recognised in application of IFRIC 12 for the development of dispatching infrastructure (up €3.0 million), the increase in "Services" is €11.8 million. This primarily reflects a reduction in the cost of intercompany services under specific intercompany contracts and revised right-of-way fees in certain regions of Italy.
Under the Terna Group's current organisational structure, responsibility for the activities involved in investment in the development and upgrade of dispatching infrastructure lies with both Terna S.p.A. itself and the

subsidiary Terna Rete Italia S.p.A.. The related cost is charged in full to “Services” as a service received from the subsidiary. The following table shows details of the costs recognised in application of IFRIC 12 and within the scope of the item under review.

(€m)

	2018	2017	Δ
IT services	0.2	0.3	(0.1)
Tender costs for plant	0.2	0.3	(0.1)
Maintenance and sundry services	0.6	0.0	0.6
Cost of services relating to investment in dispatching infrastructure (IFRIC 12)	**1.0**	**0.6**	**0.4**
Cost of services recognised in application of IFRIC 12 - Services from Terna Rete Italia S.p.A.	19.7	17.1	2.6
TOTAL COST OF SERVICES RELATING TO INVESTMENT IN DISPATCHING INFRASTRUCTURE (IFRIC 12)	**20.7**	**17.7**	**3.0**

5. PERSONNEL EXPENSES - €63.9 MILLION

(€m)

	2018	2017	CHANGE
Salaries, wages and other short-term benefits	63.2	56.4	6.8
Directors’ remuneration	1.7	1.8	(0.1)
Termination benefits (TFR), energy discounts and other employee benefits	2.2	(8.8)	11.0
Early retirement incentives	-	19.6	(19.6)
Gross personnel expenses	**67.1**	**69.0**	**(1.9)**
Capitalised personnel expenses	(3.2)	(3.0)	(0.2)
TOTAL	**63.9**	**66.0**	**(2.1)**

Personnel expenses are down €2.1 million, primarily due to net provisions for early retirement schemes in 2017, partially offset by the increase in the average workforce as a result of the launch of the new initiatives envisaged in the Strategic Plan 2018-2022.

The following table shows the Company’s workforce by category at the end of the year and as the average for the year.

	AVERAGE WORKFORCE		WORKFORCE AT	
	2018	2017	31 DECEMBER 2018	31 DECEMBER 2017
Senior managers	37	33	36	34
Middle managers	208	173	221	175
Office staff	355	277	391	298
TOTAL	**600**	**483**	**648**	**507**

6. AMORTISATION, DEPRECIATION AND IMPAIRMENT LOSSES - €517.9 MILLION

(€m)

	2018	2017	CHANGE
Amortisation of intangible assets	46.5	46.3	0.2
- of which rights on infrastructure	*22.8*	*24.8*	*(2.0)*
Depreciation of property. plant and equipment	457.3	438.0	19.3
Impairment losses on current assets	13.4	9.3	4.1
Losses on trade receivables	0.7	1.6	(0.9)
TOTAL	**517.9**	**495.2**	**22.7**

The increase of €22.7 million primarily reflects the entry into service of new plant.

7. OTHER OPERATING COSTS - €18.2 MILLION

(€m)

	2018	2017	CHANGE
Indirect taxes and local taxes and levies	5.3	4.5	0.8
Quality of service costs	5.1	10.5	(5.4)
of which mitigation and sharing mechanisms	*3.1*	*7.7*	*(4.6)*
of which the Fund for Exceptional Events	*1.9*	*2.4*	*(0.5)*
of which compensation mechanisms for HV users	*0.1*	*0.4*	*(0.3)*
Net contingent liabilities	0.6	0.9	0.3
Adjustment of provisions for litigation and disputes	(2.8)	9.2	12.0
Losses on sales/disposal of plant	0.2	0.6	(0.4)
Other	9.8	13.3	(3.5)
TOTAL	**18.2**	**39.0**	**(20.8)**

The most significant components of this item regard indirect taxes and local taxes and levies (€5.3 million, including €3.2 million in Tosap, Tassa per l'Occupazione del Suolo Pubblico, a tax on the occupation of public land, and Tares, Tassa Rifiuti e Servizi, a tax on waste and municipal services), net quality of service costs (€5.1 million) and other costs (€9.8 million) which include membership dues and contributions to trade bodies and associations, donations and other expenses.

The reduction of €20.8 million in this item primarily reflects:
- adjustment to provisions for litigation and disputes (down €12.0 million), mainly as a result of the favourable outcomes to a number of disputes arising in previous years;
- the net costs resulting from the mechanisms designed to regulate the quality of service, broadly reflecting higher costs incurred in 2017, totalling €5.4 million, in relation to certain major events in central and southern Italy, with respect to outages in 2018 essentially due to events in northern Italy in October;
- a reduction in other costs (down €3.5 million), primarily regarding the recognition of higher expenses payable to ARERA in the previous year.

8. NET FINANCIAL INCOME/(EXPENSES) - (€78,5) MILLION

(€m)

	2018	2017	CHANGE
FINANCIAL EXPENSES			
Financial expenses paid to Cassa Depositi e Prestiti	(3.0)	(3.7)	0.7
Interest expense on medium/long-term borrowings and related hedges	(98.7)	(94.0)	(4.7)
Discounting of termination benefits (TFR) and other provisions for employee benefits	(0.2)	(0.4)	0.2
Capitalised financial expenses	15.1	12.3	2.8
Other financial expenses	(0.6)	(9.1)	8.5
Translation differences	(4.2)	(0.7)	(3.5)
Total expenses	**(91.6)**	**(95.6)**	**4.0**
FINANCIAL INCOME			
Dividends from associates	1.1	1.1	-
Financial income from subsidiaries	7.0	0.9	6.1
Restructuring of bond issues and related hedges	-	2.7	(2.7)
Interest income and other financial income	5.0	1.1	3.9
Total income	**13.1**	**5.8**	**7.3**
TOTAL	**(78.5)**	**(89.8)**	**11.3**

Net financial expenses for the year amount to €78.5 million, reflecting €91.6 million in financial expenses and €13.1 million in financial income. The reduction in net financial expenses compared with the previous year, amounting to €12.3 million, primarily reflects the following:

- an increase in capitalised financial expenses (€2.8 million) linked to an increase in the Company's capital expenditure during the year;
- an increase in interest income and other financial income (€3.9 million), primarily reflecting an increase in liquidity invested during the year and the improved return on that liquidity;
- an increase in financial income from intercompany transactions with subsidiaries (€6.1 million);
- an increase in financial expenses on medium/long-term borrowings and the related hedges (€4.7 million), primarily due to rising inflation recorded during 2018.

9. INCOME TAX FOR THE YEAR - €257.9 MILLION

(€m)

	2018	2017	CHANGE
Income tax for the year			
Current tax expense:			
- IRES (corporate income tax)	241.7	243.2	(1.5)
- IRAP (regional tax on productive activities)	51.9	54.0	(2.1)
Total current tax expense	***293.6***	***297.2***	***(3.6)***
New temporary differences:			
- deferred tax assets	(12.4)	(18.6)	6.2
Reversal of temporary differences:			
- deferred tax assets	19.4	15.9	3.5
- deferred tax liabilities	(31.1)	(30.0)	(1.1)
Total deferred tax (income)/expense	***(24.1)***	***(32.7)***	***8.6***
Adjustments of taxes for previous years	**(11.6)**	**(2.9)**	**(8.7)**
TOTAL	**257.9**	**261.6**	**(3.7)**

Current income tax expense for the year of €293.6 million is down €3.6 million compared with the previous year, essentially reflecting the impact of the tax relief designed to stimulate economic growth (ACE - *Aiuto alla Crescita Economica*), accelerated depreciation applied by the Company and a reduction in non-deductible items for the purposes of IRAP compared with the previous year.

Deferred tax income, amounting to €24.1 million, is down €8.6 million, primarily due to the effect on net deferred tax assets of movements in provisions for risks and charges.

Adjustments to taxes for previous years, amounting to €11.6 million, reflect the overpayment of tax in previous years and are up €8.7 million.

The effective tax charge for the year (€257.9 million) results in a tax rate of 28.1%, compared with a rate of 29.0% for 2017. For a clearer presentation of the differences between the theoretical and effective tax charges, the table below reconciles the theoretical and effective tax rates for the year.

(€m)

	TAXABLE INCOME	TAX	% CHANGE
Profit before tax	919.2		
IRES - Theoretical tax charge (rate of 24.0%)		220.6	
IRAP - Theoretical tax charge (rate of 5.10% on operating profit of €997.7 million)		50.9	
		271.5	
THEORETICAL TAX RATE			**29.5%**
Permanent differences in IRES			
Employee benefits		0.8	0.1%
Contingent assets and liabilities		0.7	0.1%
Impairments		0.5	0.1%
Membership dues		0.5	0.1%
Other increases/decreases		0.6	0.1%
Dividend		(0.2)	-
Single council tax (Imposta Municipale Unica, IMU)		(0.5)	(0.1%)
IRAP - art. 6 of Law 28/01/2009		(1.2)	(0.2%)
Accelerated depreciation		(3.2)	(0.4%)
Tax relief (ACE - Aiuto alla Crescita Economica)		*(3.7)*	*(0.4%)*
Permanent differences in IRAP			
Capitalised financial expenses		0.8	0.1%
Personnel expenses		0.2	-
Effective tax rate after adjustments of taxes for previous years			**29.0%**
Income tax for previous years		(3.9)	(0.4%)
One-off items		(7.7)	(0.8%)
Release of deferred tax assets on deductible bonuses and incentives		2.7	0.3%
Total income tax expense for the year		***257.9***	
EFFECTIVE TAX RATE			**28.1%**

C. Operating Segments

In line with the requirements of "IFRS 8 - Operating segments", companies that publish a Parent Company's consolidated financial statements in a single document, together with the Company's separate financial statements, only have to present segment information in the consolidated financial statements.

D. Notes to the statement of financial position

Assets

10. PROPERTY, PLANT AND EQUIPMENT - €12,035.0 MILLION

(€m)

	BUILDINGS	PLANT AND EQUIPMENT	INDUSTRIAL AND COMMERCIAL EQUIPMENT	OTHER ASSETS	ASSETS UNDER CONSTRUCTION AND PREPAYMENTS	BUILDINGS	TOTAL
COST AT 1 JANUARY 2018	**127.6**	**1,798.6**	**16,048.1**	**88.2**	**139.8**	**1,350.3**	**19,552.6**
Investments	0.4	0.9	4.9	3.0	3.6	821.5	834.3
Assets entering service	8.4	77.2	557.4	4.6	6.8	(654.4)	-
Intercompany additions	-	-	1.8	-	-	5.5	7.3
Other additions	-	-	1.5	-	-	(1.5)	-
Disposals and impairments	(0.1)	(0.3)	(37.5)	(0.1)	(0.2)	(13.1)	(51.3)
Other movements		-	(8.6)	-	-	(31.9)	(40.5)
Reclassifications	(0.5)	2.7	-	-	-	-	2.2
COST AT 31 DECEMBER 2018	**135.8**	**1,879.1**	**16,567.6**	**95.7**	**150.0**	**1,476.4**	**20,304.6**
ACCUMULATED DEPRECIATION AND IMPAIRMENTS AT 1 JANUARY 2018	**-**	**(516.1)**	**(7,155.5)**	**(70.7)**	**(105.1)**	**-**	**(7,847.4)**
Depreciation for the year	-	(44.1)	(397.6)	(4.3)	(11.3)	-	(457.3)
Intercompany additions	-	-	(0.7)	-	-	-	(0.7)
Disposals	-	0.1	35.7	0.1	0.2	-	36.1
Reclassifications	-	(0.3)	-	-	-	-	(0.3)
ACCUMULATED DEPRECIATION AND IMPAIRMENTS AT 31 DECEMBER 2018	**-**	**(560.4)**	**(7,518.1)**	**(74.9)**	**(116.2)**	**-**	**(8,269.6)**
Carrying amount							
AT 31 DECEMBER 2018	**135.8**	**1,318.7**	**9,049.5**	**20.8**	**33.8**	**1,476.4**	**12,035.0**
AT 31 DECEMBER 2017	**127.6**	**1,282.5**	**8,892.6**	**17.5**	**34.7**	**1,350.3**	**11,705.2**
Change	**8.2**	**36.2**	**156.9**	**3.3**	**(0.9)**	**126.1**	**329.8**

The category, "Plant and equipment", essentially includes the electricity transmission grid and transformer substations in Italy.
"Property, plant and equipment" is up €329.8 million compared with the previous year. This broadly reflects ordinary movements during the year as a result of investment (up €834.3 million), depreciation for the period (down €457.3 million), other movements (down €40.5 million) relating to grants related to assets (primarily for projects financed by the Ministry for Economic Development and the EU) and disposals and impairments (down €15.2 million). The change also reflects the following intercompany additions:

- the transfer, from the subsidiary, Rete S.r.l., on 7 December 2018, of 14 "Integrated Systems" used in the functional control of substations forming part of the National Transmission Grid, in return for a consideration of €5.5 million;
- the transfer, by the subsidiary, Terna Energy Solutions S.r.l., in December, of 2 rapid installation electricity substations for a consideration of €1.1 million.

The following information regards work on the principal projects during the year in relation to Regulated Activities: progress on construction of the various overseas interconnections, consisting of the power lines linking Italy and Montenegro (€26.5 million) and Italy and France (€56.1 million), extension of the fibre network as part of the "Fibre for the Grid" project (€42.5 million), the laying of cables in the Venetian lagoon (€23.6 million), construction of the Sorrento Peninsula interconnector (€17.5 million), restructuring of the grid serving the city of Naples (€16 million), continued work on devices to mitigate the risk of ice and snow (€11.1 million), construction of the Foggia-Benevento II power line (€10.8 million) and the upgrade of power lines in the north-west of the country (€10.7 million).

11. GOODWILL - €190.2 MILLION

Goodwill of €190.2 million regards the goodwill resulting from the mergers with the subsidiaries RTL (€88.6 million, merged into the Company in 2008) and Terna Rete Italia S.r.l. (€101.6 million) merged in 2017.
The balance is unchanged with respect to the previous year.

Impairment testing

CGU - Terna S.p.A.'s transmission activities

For impairment testing purposes, Terna S.p.A.'s Regulated Activities was considered to be a cash generating unit (CGU). Measurement of the recoverable value of the goodwill allocated to the transmission activities was based on fair value less costs of disposal. This was determined taking into account Terna's share price at 31 December 2018, after stripping out the estimated fair value of the assets and liabilities not attributable to the CGU represented by transmission activities.
The resulting value is significantly higher than the carrying amount inclusive of goodwill.

12. INTANGIBLE ASSETS - €237.5 MILLION

(€m)

	INFRASTRUCTURE RIGHTS	CONCESSIONS	OTHER ASSETS	ASSETS UNDER DEVELOPMENT AND PREPAYMENTS	TOTAL
Cost	411.0	135.4	221.0	34.3	801.7
Accumulated amortisation	(308.1)	(68.1)	(191.4)	-	(567.6)
BALANCE AT 31 DECEMBER 2017	**102.9**	**67.3**	**29.6**	**34.3**	**234.1**
Investments	-	-	-	51.8	51.8
Assets entering service	20.0	-	32.0	(52.0)	-
Amortisation for the year	(22.8)	(5.6)	(18.1)	-	(46.5)
Reclassifications	(1.9)	-	-	-	(1.9)
BALANCE AT 31 DECEMBER 2018	**98.2**	**61.7**	**43.5**	**34.1**	**237.5**
Cost	428.5	135.4	253.0	34.1	851.0
Accumulated amortisation	(330.3)	(73.7)	(209.5)	-	(613.5)
BALANCE AT 31 DECEMBER 2018	**98.2**	**61.7**	**43.5**	**34.1**	**237.5**
Change	**(4.7)**	**(5.6)**	**13.9**	**(0.2)**	**3.4**

Intangible assets amount to €237.5 million and include:

- the infrastructure used in provision of the dispatching service carried out under concession and accounted for in accordance with "IFRIC 12 - Service Concession Arrangements", with the carrying amount, at 31 December 2018, of infrastructure entering service during the year amounting to €98.2 million and of infrastructure under construction, included in the category "Assets under development and prepayments", amounting to €25.1 million (at 31 December 2017, the matching figures were €102.9 million and €20.3 million, respectively);
- the concession for electricity transmission and dispatching activities in Italy (with a carrying amount of €61.7 million at 31 December 2018); this 25-year concession was recognised in 2005, initially at fair value and subsequently at cost.

Other intangible assets primarily include software applications, either produced internally or purchased as part of systems development programmes. Investment in these assets during the year (€26.7 million) essentially regards internal development programmes.
The increase compared with the previous year (up €3.4 million) reflects the net effect of investment (€51.8 million, including €25.1 million in infrastructure rights) and amortisation (€46.5 million).

Investment in intangible assets during the year (€51.8 million) included expenditure on the development of software applications for the Remote Management System for Dispatching (€11.2) million), the Power Exchange (€4.1 million), the Metering System (€1 million) and for protection of the electricity system (€2.1 million), as well as software applications and generic licences (€24.6 million).

13. DEFERRED TAX ASSETS

(€m)

	31 DECEMBER 2017	RESTATEMENT OF OPENING BALANCES AT 1 JANUARY 2018	PROVISIONS	USES AND OTHER MOVEMENTS	EFFECTS RECOGNISED IN COMPRE-HENSIVE INCOME	31 DECEMBER 2018
DEFERRED TAX ASSETS						
Provisions for risks and charges	38.5	-	7.3	(10.8)	-	35.0
Allowance for doubtful accounts	2.9	-	-	-	-	2.9
Amounts due to employees	6.9	-	1.9	(2.9)	-	5.9
Cash flow hedges	3.8	-	-	-	10.6	14.4
Tax relief on goodwill	34.5	-	-	(5.5)	-	29.0
Other	-	-	3.2	-	-	3.2
Measurement of financial instruments - IFRS 9	-	0.6	-	-	-	0.6
TOTAL DEFERRED TAX ASSETS	**86.6**	**0.6**	**12.4**	**(19.4)**	**10.6**	**91.0**
DEFERRED TAX LIABILITIES						
Property. plant and equipment	(100.8)	-	-	31.1	-	(69.7)
Employee benefits and financial instruments	(3.1)	-	-	-	-	(3.1)
TOTAL DEFERRED TAX LIABILITIES	**(103.9)**	**-**	**-**	**31.1**	**-**	**(72.8)**
NET DEFERRED TAX ASSETS	**(17.3)**	**0.6**	**12.4**	**12.6**	**10.6**	**18.2**

The balance of this item, amounting to €18.2 million, includes the net impact of movements in the Company's deferred tax assets and liabilities.

Deferred tax assets (€91.0 million) are up by a net €4.4 million compared with the previous year, reflecting the following movements:

- net provisions that did not impact profit or loss, totalling €10.6 million, primarily reflecting the tax effect of movements in cash flow hedges;
- net uses of €3.5 million relating to movements during the year in provisions for risks and charges, primarily with regard to litigation and disputes (down €1.5 million) movements in provisions relating to quality of service (down €0.9 million);
- the use of €5.5 million representing the accrued portion recognised in relation to deferred tax assets on tax relief on the goodwill resulting from the merger with RTL and, from this year, goodwill resulting from the merger with Terna Rete Italia S.r.l..

Deferred tax liabilities (€72.8 million) are down €31.1 million compared with the previous year, due to the use of previous provisions for accelerated depreciation, including the net release for depreciation for the year.

14. FINANCIAL ASSETS

(€m)

	MEASUREMENT	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Investments in subsidiaries	at cost	975.5	916.5	59.0
Investments in associates	at cost	44.5	47.8	(3.3)
Loan to subsidiaries	amortised cost	10.0	-	10.0
Deposit in the Interconnector Guarantee Fund	amortised cost	61.1	42.2	18.9
Other non-current financial assets		-	3.2	(3.2)
NON-CURRENT FINANCIAL ASSETS		**1,091.1**	**1,009.7**	**81.4**
Short-term loan to subsidiaries	amortised cost	89.5	-	89.5
Government securities	FVTOCI	402.6	-	402.6
Cash flow hedges	Fair value	1.3	-	1.3
Other current financial assets		0.6	0.2	0.4
CURRENT FINANCIAL ASSETS		**494.0**	**0.2**	**493.8**

"Non-current financial assets" includes the items described below.

The value of "Investments in subsidiaries" (€975.5 million) regards investments in Terna S.p.A.'s direct subsidiaries and is up €59 million compared with 31 December 2017, reflecting the subscription for newly issued shares in the subsidiary, Terna Crna Gora d.o.o..
The value of "Investments in associates" (€44.5 million) regards the investments in CGES - CrnoGorski Elektroprenosni Sistem AD (€26.7 million), CESI S.p.A. (€17.6 million) and CORESO S.A. (€0.2 million). This item is down €3.3 million compared with the previous year, equal to the reduction in the investment in CGES due to the dividend declared at the end of 2018.
The following table shows key information on investments in subsidiaries, associates and joint ventures owned directly by Terna S.p.A. at 31 December 2018. Amounts relate to the latest approved financial statements.

The following table shows key information on investments in subsidiaries, associates and joint ventures owned directly by Terna S.p.A. at 31 December 2018. Amounts relate to the latest approved financial statements.

NAME	REGISTERED OFFICE	CURRENCY	SHARE CAPITAL	% INTEREST	CARRYING AMOUNT (€)
SUBSIDIARIES CONTROILLED DIRECTLY BY TERNA S.P.A.					
Terna Rete Italia S.p.A.	Rome	Euro	120,000	100%	3,120,000
Business	Design, construction, management, development, operation and maintenance of power lines and grid infrastructure and other grid-related infrastructure, plant and equipment used in the above electricity transmission and dispatching activities and in similar, related and connected sectors.				
Terna Crna Gora d.o.o.	Podgorica (Montenegro)	Euro	173,000,000	100%	173,000,000
Business	Authorisation, construction and operation of the transmission infrastructure forming the Italy-Montenegro interconnector on Montenegrin territory.				
Terna Plus S.r.l.	Rome	Euro	16,050,000	100%	16,861,553
Business	Design, construction, management, development, operation and maintenance of plant, equipment and infrastructure for grids and systems, including distributed storage and pumping and/or storage systems.				
Terna Interconnector S.r.l.	Rome	Euro	10,000	65%*	19,926
Business	Responsible for construction and operation of the private section of the Italy-France interconnector and civil works on the public section.				
Monita Interconnector S.r.l.	Rome	Euro	10,000	95%**	39,500
Business	Responsible for construction and operation of the private section of the Italy-Montenegro interconnector.				
Rete S.r.l.	Rome	Euro	387,267,082	100%	770,214,773
Business	Design, construction, management, development, operation and maintenance of high-voltage power lines.				
Difebal S.A.	Montevideo (Uruguay)	Pesos Uruguayano	140,000	100%	3,597
Business	Design, construction and maintenance of electricity infrastructure in Uruguay.				
Terna Energy Solutions S.r.l.	Rome	Euro	2,000,000	100%	12,282,156
Business	Design, construction, management, development, operation and maintenance of distributed energy storage systems, pumping and/or storage systems, plant, equipment and infrastructure, including grids; research, consultancy and assistance in matters relating to the core business; any other activity capable of improving the use and development of plant, resources and expertise.				
Resia Interconnector S.r.l.	Rome	Euro	10,000	100%	10,000
Business	Design, construction, management, development, operation and maintenance, including on behalf of third parties, of power lines and grid infrastructure and other infrastructure connected to such grids, plant and equipment for use in electricity transmission operations, or in similar, related or connected sectors, and has been established to fulfil the obligations assumed by the energy-intensive companies in relation to implementation of the interconnection with Austria.				

** 5% is held by Terna Rete Italia S.p.A. and 30% by Transenergia S.r.l..*

*** 5% is held by Terna Rete Italia S.p.A..*

NAME	REGISTERED OFFICE	CURRENCY	SHARE CAPITAL	% INTEREST	CARRYING AMOUNT (€)
ASSOCIATES					
Cesi S.p.A.	Milan	Euro	8,550,000	42.698%	17,563,381
Business	Experimental research and provision of services related to electro-technology.				
Coreso S.A.	Brussels (Belgium)	Euro	1,000,000	15.84%	210,742
Business	Technical centre owned by several electricity transmission operators, responsible for coordinating joint operations of TSOs, in order to improve and upgrade the security and coordination of the electricity system in central and western Europe.				
CGES A.D.	Podgorica (Montenegro)	Euro	155,108,283	22.0889%	26,694,419
Business	Provision of transmission and dispatching services in Montenegro.				
JOINT VENTURES					
ELMED Etudes S.a.r.l.	Tunis (Tunisia)	Dinaro Tunisino	2,700,000	50%	-
Business	Conduct of preparatory studies for construction of the infrastructure required to connect the Tunisian and Italian electricity systems.				

This item also includes the deposit in the Interconnector Guarantee Fund (€61.1 million), set up to fund investment in interconnections by art. 32 of Law 99/09 and up €18.9 million compared with the previous year, and the financing provided by Terna S.p.A. in 2018 to the subsidiary in Uruguay, totalling €10 million (including net debt).

“Current financial assets” are up €493.8 million compared with the previous year, primarily due to the purchase of government securities, totalling €400 million, and maturing in December 2019, loans granted during the year by Terna S.p.A. to the Brazilian subsidiaries, amounting to €89.5 million, and recognition of the related foreign currency derivative entered into to protect against the effects of the loans.

15. OTHER ASSETS

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Loans and advances to employees	3.6	3.0	0.6
Deposits with third parties	0.7	0.6	0.1
OTHER NON-CURRENT ASSETS	**4.3**	**3.6**	**0.7**
Amounts due from associates	3.3	-	3.3
Other tax credits	4.8	50.5	(45.7)
Other current assets - Interconnector Guarantee Fund	4.0	4.1	(0.1)
Prepayments to suppliers	1.2	0.8	0.4
Prepayments of operating expenses and accrued operating income	4.5	5.1	(0.6)
Amounts due from others	2.7	2.7	-
OTHER CURRENT ASSETS	**20.5**	**63.2**	**(42.7)**

“Other non-current assets” amount to €4.3 million, an increase of €0.7 million compared with the previous year, essentially due to loans and advances to employees.

"Other current assets" of €20.5 million are down €42.7 million compared with 31 December 2017, essentially reflecting:

- a reduction in "other tax credits" (down €45.7 million), primarily due to the decrease in refundable VAT (down €46.9 million), mainly due to increased payments on account in the previous year as a result of the Ministerial Decree of 27 June 2017;
- recognition of amounts due from the associate, CGES (€3.3 million) as a result of the dividend declared at the end of the year.

16. INVENTORIES - €0 MILLION

This item amounts to zero at 31 December 2018, having declined €5.3 million with respect to 31 December 2017. This reflects the fact that the item, "Property, plant and equipment" includes goods for sale through Indefeasible Rights of Use (IRU) contracts.

17. TRADE RECEIVABLES - €1,090.0 MILLION

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Energy-related receivables	743.7	772.8	(29.1)
Transmission charges receivable	310.8	312.2	(1.4)
Other trade receivables	17.6	34.0	(16.4)
Amounts due from subsidiaries	17.9	23.6	(5.7)
TOTAL	**1,090.0**	**1.142.6**	**(52.6)**

Trade receivables amount to €1,090.0 million and are accounted for less any losses on items deemed not to be recoverable and recognised in the allowance for doubtful accounts (€26.1 million for energy-related receivables and €11.9 million for other items in 2018, compared with €27 million for energy-related items and €11.3 million for other items in 2017). The carrying amount shown broadly approximates to fair value.

Energy-related/regulated receivables - €743.7 million

This item includes so-called "pass-through items" relating to the Parent Company's activities in accordance with Resolution 111/06 (€715 million) and receivables due from the users of dispatching services forming part of Regulated Activities (€13.9 million). It also includes the amount due from the Fund for Energy and Environmental Services (Cassa per i Servizi Energetici e Ambientali - CSEA), based on the RENS performance for the year (€14.8 million).

The balance is down €29.1 million overall compared with the previous year, essentially due to energy-related pass-through receivables (down €30.9 million), following a reduction of €68.9 million in the uplift, reflecting the reduction in net costs to be recovered linked to both the Dispatching Services Market (DSM) and to imbalances (the related receivables are up €32.2 and €20.3 million, respectively). The change also reflects the reduction in amounts due from the users of dispatching services in relation to the interruptibility service (€41.6 million), partly offset by amounts due from CSEA guaranteeing full coverage of the cost of this service (€28.3 million).

Transmission charges receivable - €310.8 million

Transmission charges receivable, amounting to €310.8 million, represent the amount due to the Parent Company and other grid owners from electricity distributors for use of the National Transmission Grid. The receivable is down €1.4 million compared with 31 December 2017, primarily due to the mechanism for recovering one-off payments recognised in 2017 for the early effect of the tariff adjustment linked to investment.

Other trade receivables - €17.6 million

Other trade receivables, totalling €17.6 million a reduction of €16.4 million compared with the previous year. This primarily reflects the Company's collection of prior year amounts due from customers of its Non-regulated Activities.

Amounts due from subsidiaries - €17.9 million

This item, totalling €17.9 million, primarily regards the amount receivable from the subsidiary, Terna Rete Italia S.p.A. (€13.9 million). This amount primarily regards services provided in the last part of the year under existing contracts, mainly with regard to the lease of certain operations (€10.0 million) and administrative services (€1.9 million). The item is down compared with the previous year (down €5.7 million), broadly due to a reduction of €64. million in amounts due from the subsidiary, Terna Rete Italia S.p.A., above all due to a reduction in amounts due for administrative services (down €4.2 million, largely reflecting the impact of the revised fee charged on the basis of the final assessment of the volume of services provided at the end of 2018) and quality of service (down €3.1 million) reflecting the amount receivable at 31 December 2017 compared with the impact for 2018 recognised in “Trade receivables”.

The amount for guarantees given by Group companies to third parties at 31 December 2018 amounts to €212.4 million and breaks down as follows: €104.1 million in the interests of Terna S.p.A., €39.2 million in the interests of Terna Interconnector S.r.l., €43.5 million in the interests of Terna Rete Italia S.p.A., €9.5 million in the interests of Terna Plus S.r.l., €11.2 million in the interests of Difebal S.A., €3.4 million in the interests of Rete S.r.l. and €1.5 million in the interests of Terna Energy Solutions S.r.l..

18. CASH AND CASH EQUIVALENTS - €945.1 MILLION

Cash amounts to €945.1 million at 31 December 2018, including €751.5 million in liquidity invested in readily convertible short-term deposits and €193.6 million in net deposits in bank current accounts (including a net balance of €-204.8 million on intercompany treasury accounts).

19. INCOME TAX ASSETS - €16.0 MILLION

Income tax assets, amounting to €16 million, are down €41.9 million compared with the previous year, essentially reflecting the assets recognised at the end of 2017 compared with the liabilities recognised at 31 December 2018 in “Tax liabilities”. This reflects higher payments on account made in the previous year under the tax consolidation arrangement (determined on the basis of a higher rate of IRES applied in 2016).

Equity and liabilities

20. EQUITY - €3,850.9 MILLION

Share capital - €442.2 million
Terna's share capital consists of 2,009,992,000 ordinary shares with a par value of €0.22 per share.

Legal reserve - €88.4 million
The legal reserve accounts for 20% of the Company's share capital and is unchanged with respect to the previous year.

Other reserves - €704.1 million
The other reserves have decreased €33.2 million, reflecting other comprehensive income in the form of fair value adjustments to the Company's cash flow hedges (down €31.3 million, taking into account the related tax asset of €10.0 million).

Retained earnings and accumulated losses - €2,113.1 million
The increase in "Retained earnings and accumulated losses", amounting to €196.4 million, primarily regards the remaining portion of profit for 2017, following payment of the dividend for that year (totalling €442.2 million).

Interim dividend for 2017
On 9 November 2018, the Company's Board of Directors, having obtained the Independent Auditor's opinion required by article 2433-*bis* of the Italian Civil Code, decided to pay an interim dividend of €0.0787 per share, amounting to a total payout of €158.2 million. The dividend was payable from 21 November 2018, with an ex-dividend date for coupon 29 of 19 November 2018.
The individual components of equity at the end of the year are shown below, specifying their origin, availability and distributability.

(€m)

	31 DECEMBER 2018	POTENTIAL USE	AVAILABLE AMOUNT
Share capital	442.2	-	-
Legal reserve	88.4	B	88.4
Other reserves			
- capital reserves	416.1	A, B, C	416.1
- actuarial gains (losses) on employee benefits and cash flow hedges. after taxation	(45.5)	-	-
- revenue reserves	333.5	A, B, C	333.5
Retained earnings	2,113.1	A, B, C	2,113.1
Interim dividend	(158.2)	A, B, C	-
TOTAL	**3,189.6**		

Key:
A - for capital increases
B - to cover losses
C - for distribution to shareholders

The available amount includes €538.8 million in untaxed revenue reserves.

21. BORROWINGS AND FINANCIAL LIABILITIES

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Bond issues	6,563.2	6,541.9	21.3
Bank borrowings	1,608.7	2,096.6	(487.9)
LONG-TERM BORROWINGS	**8,171.9**	**8,638.5**	**(466.6)**
Cash flow hedges	59.1	9.9	49.2
NON-CURRENT FINANCIAL LIABILITIES	**59.1**	**9.9**	**49.2**
SHORT-TERM BORROWINGS	**-**	**90.0**	**(90.0)**
Bond issues	616.7	749.9	(133.2)
Bank borrowings	613.1	134.1	479.0
CURRENT PORTION OF LONG-TERM BORROWINGS	**1,229.8**	**884.0**	**345.8**
TOTAL	**9,460.8**	**9,622.4**	**(161.6)**

Borrowings and financial liabilities have decreased by €161.6 million compared with the previous year to €9,460.8 million.
The reduction in bond issues (down €111.9 million) reflects the repayment of bonds issued on 16 October 2012, totalling €750 million, and the green bond issue of 23 July 2018 (€750 million), as well as the downward adjustment of €111.9 million to these instruments to reflect their amortised cost.
The latest official prices at 31 December 2018 and 31 December 2017 for the bonds listed on the Luxembourg Stock Exchange are detailed below:

(€m)

	PRICE AT 31 DECEMBER 2018	PRICE AT 31 DECEMBER 2017
bond maturity 2024:	120.51	128.98
bond maturity 2023:	127.61*	135.46
bond maturity 2019:	103.62	108.74
bond maturity 2026:	103.52	102.85
bond maturity 2021:	109.79	114.80
bond maturity 2022:	100.64	102.50
bond maturity 2028:	89.83	96.16
bond maturity 2027:	94.53	100.51
bond maturity 2018:	-	100.38
bond maturity 2023 (Green Bond):	100.17	-

** Source: BNP Paribas, in the absence of up-to-date prices sourced from Reuters and Bloomberg.*

Compared to the previous year, bank borrowings are down €8.9 million, due primarily to:
- the drawdown of new EIB loans, totalling €130.0 million;
- repayments made to the EIB at maturity and on outstanding leases, totalling €132.4 million.

Long-term borrowings

(€m)

	MATURITY	AT 31 DECEMBER 2017	AT 31 DECEMBER 2018*	PORTION FALLING DUE WITHIN 12 MONTHS	PORTION FALLING DUE AFTER 12 MONTHS	2020	2021	2022	2023	2024	BEYOND	COUPON INTEREST	AVERAGE NET INTEREST RATE ON HEDGES AT 31 DECEMBER 2018
Bonds	2024	1,013.4	982.9	-	982.9	-	-	-	-	982.9	-	4.90%	0.86%
IL bonds	2023	692.9	679.2	-	679.2	-	-	-	679.2	-	-	2.73%	0.30%
PP bonds	2019	638.7	616.7	616.7		-	-	-	-	-	-	4.88%	1.14%
PP bonds	2026	78.8	78.9	-	78.9	-	-	-	-	-	78.9	1.60%	1.79%
1250 bonds	2021	1,388.7	1,345.9	-	1,345.9	-	1,345.9	-	-	-	-	4.75%	1.20%
1250 bonds	2022	996.8	997.6	-	997.6	-	-	997.6	-	-	-	0.88%	0.95%
1000 bonds	2018	749.9		-		-	-	-	-	-	-	2.88%	2.99%
750 bonds	2028	740.1	740.9	-	740.9	-	-	-	-	-	740.9	1.00%	1.19%
750 bonds	2027	992.5	993.2	-	993.2	-	-	-	-	-	993.2	1.38%	1.45%
1000 bonds	2023	-	744.6	-	744.6	-	-	-	744.6	-	-	0.00%	1.16%
EIB	2039	238.6	368.6	-	368.6	-	-	4.6	20.5	20.5	323.0	1.44%	1.44%
Total fixed rate		**7,530.4**	**7,548.5**	**616.7**	**6,931.8**	**-**	**1,345.9**	**1,002.2**	**1,444.3**	**1,003.4**	**2,136.0**		
EIB	2030	1,488.3	1,355.9	111.3	1,244.6	116.1	116.7	128.6	112.7	112.7	657.8	0.25%	1.12%
CDP	2019	500.0	500.0	500.0	-	-	-	-	-	-	-	0.93%	1.04%
Leases	2019-2021-2022	3.8	1.9	1.8	0.1	0.1	-	-	-	-	-	0.88%	0.88%
Total variable rate		**1,992.1**	**1,857.8**	**613.1**	**1,244.7**	**116.2**	**116.7**	**128.6**	**112.7**	**112.7**	**657.8**		
TOTAL		**9,522.5**	**9,406.3**	**1,229.8**	**8,176.5**	**116.2**	**1,462.6**	**1,130.8**	**1,557.0**	**1,116.1**	**2,793.8**		

** The balance does not include fees of €4.6 million.*

At 31 December 2018, Terna's borrowings amount to €9,406.3 million (€1,229.8 million maturing within 12 months and €8,176.5 million maturing after 12 months), of which €2,793.8 million maturing after five years. The table below shows movements in long-term debt during the year, including also the nominal amount:

(€m)

	AT 31 DECEMBER 2017			REPAYMENTS AND CAPITALISATIONS	DRAWDOWNS	OTHER	CHANGE IN CARRYING AMOUNT	AT 31 DECEMBER 2018		
	NOMINAL DEBT	CARRYING AMOUNT	FAIR VALUE					NOMINAL DEBT	CARRYING AMOUNT	FAIR VALUE
Bonds maturing 2024	800.0	1,013.4	1,031.8			(30.5)	(30.5)	800.0	982.9	964.1
IL bonds	570.5	692.9	677.3			(13.7)	(13.7)	579.0	679.2	638.1
Private Placement 2019	600.0	638.7	652.4			(22.0)	(22.0)	600.0	616.7	621.7
Private Placement 2026	80.0	78.8	82.3			0.1	0.1	80.0	78.9	82.8
Bonds maturing 2021	1,250.0	1,388.7	1,435.0			(42.8)	(42.8)	1,250.0	1,345.9	1,372.4
Bonds maturing 2022	1,000.0	996.8	1,025.0			0.8	0.8	1,000.0	997.6	1,006.4
Bonds maturing 2018	750.0	749.9	752.8	(750.0)		0.1	(749.9)			
Bonds maturing 2028	750.0	740.1	721.2			0.8	0.8	750.0	740.9	673.7
Bonds maturing 2027	1,000.0	992.5	1,005.2			0.7	0.7	1,000.0	993.2	945.3
Bonds maturing 2023					750.0	(5.4)	744.6	750.0	744.6	751.3
Total bond issues	**6,800.5**	**7,291.8**	**7,383.0**	**(750.0)**	**750.0**	**(111.9)**	**(111.9)**	**6,809.0**	**7,179.9**	**7,055.8**
Bank borrowings	2,230.7	2,230.7	2,235.5	(132.4)	130.0	(6.5)	(8.9)	2,285.3	2,221.8	2,301.2
Total borrowings	**2,230.7**	**2,230.7**	**2,235.5**	**(132.4)**	**130.0**	**(6.5)**	**(8.9)**	**2,285.3**	**2,221.8**	**2,301.2**
Total debt	**9,031.2**	**9,522.5**	**9,618.5**	**(882.4)**	**880.0**	**(118.4)**	**(120.8)**	**9,094.3**	**9,401.7**	**9,357.0**

At 31 December 2018, Terna has access to additional financing of €2,450.0 million, represented by three revolving credit facilities entered into in December 2015, July 2016 and September 2018. In addition, the Company has uncommitted bank credit lines totalling approximately €806 million and approximately €46 million in loans agreed but not yet disbursed.

In addition, as provided for in IFRS 7, the table shows the fair value of borrowings. In the case of bond issues, this is market value based on prices at the reporting date.

Non-current financial liabilities

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Cash flow hedges	59.1	9.9	49.2
TOTAL	**59.1**	**9.9**	**49.2**

Non-current financial liabilities, amounting to €59.1 million, reflect the fair value of cash flow hedges at 31 December 2018.
Fair value was measured by discounting the expected cash flows using the market yield curve at the reporting date. The increase of €49.2 million compared with 31 December 2017 reflects the change in the market interest rate curve and the change in the notional value of the derivatives portfolio.

Short-term borrowings

"Short-term borrowings", amounting to zero at 31 December 2018, are down €90.0 million compared with the previous year following repayment of the various credit lines used by the Company.

Current financial liabilities

Current financial liabilities at 31 December 2018 include the value of net interest expense accrued on financial instruments and not yet paid. This item is down €15.6 million compared with the previous year.

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
DEFERRED LIABILITIES ON:			
Hedging derivatives	2.3	1.8	0.5
Bond issues	85.9	101.9	(16.0)
Borrowings	1.9	2.0	(0.1)
TOTAL	**90.1**	**105.7**	**(15.6)**

Net debt

Pursuant to the CONSOB Communication of 28 July 2006 and in compliance with ESMA Recommendation no. 319 of 2013, the Company's net debt is as follows:

(€m)

	31 DECEMBER 2018
A. Cash	398.4
B. Term deposits	751.5
C. Net balance on intercompany treasury account	(204.8)
D. Cash and cash equivalents (A) + (B) + (C)	**945.1**
E. Current portion of non-current borrowings	1,229.8
of which from related parties	*500.0*
F. Other net financial liabilities	89.5
of which from related parties	*0.5*
G. Current financial assets	403.9
H. Short-term loan to subsidiaries	89.5
I. Current debt (E) + (F) - (G) - (H)	**825.9**
L. Current net debt (I) - (D)	**(119.2)**
M. Non-current borrowings	1,608.7
N. Bond issues	6,563.2
O. Derivative financial instruments held in portfolio	59.1
P. Long-term loan to subsidiaries	10.0
Q. Non-current net debt (M) + (N) + (O) - (P)	**8,221.0**
R. Net debt (L) + (Q)	**8,101.8**

Information on the provisions in outstanding loan agreements at 31 December 2018 is provided in the notes to the consolidated financial statements.

22. EMPLOYEE BENEFITS - €11.8 MILLION

Terna provides its employees with benefits during their period of employment (loyalty bonuses), on termination of employment (*TFR*, additional months' pay and payment in lieu of notice) and after termination in the form of post-employment benefits (energy discounts and ASEM health cover).
Loyalty bonuses are payable to the Company's employees and senior managers once certain requirements have been met regarding length of service (on completing 25 and 35 years of service).
Termination benefits (*TFR*) are payable to all employees, whilst employees hired by 30 June 1996 receive energy discounts, senior managers recruited or appointed before 28 February 1999 receive payment in lieu of notice and employees (blue-collar workers, office staff and middle managers) employed prior to 24 July 2001 are due additional months' pay on termination.
Post-employment benefits consist of a form of supplementary health cover in addition to that provided by the Italian national health service, as provided for in the national collective contract for industrial managers (the ASEM health plan).

The following table shows the composition of provisions for *TFR* and other employee benefits and movements during the year ended 31 December 2018.

(€m)

	31 DECEMBER 2017	PROVISIONS	INTEREST COST	USES AND OTHER MOVEMENTS	ACTUARIAL GAINS/	31.12.2018
Benefits during the period of employment						
Loyalty bonuses	0.6	-	-	0.1	-	0.7
Total	**0.6**	**-**	**-**	**0.1**	**-**	**0.7**
Termination benefits						
Deferred compensation benefits (TFR)	3.8	-	0.1	0.3	-	4.2
Energy discounts	1.8	-	-	(1.5)	-	0.3
Additional months' pay	0.4	-	-	0.2	-	0.6
Payment in lieu of notice	0.1	-	-	(0.1)	-	-
Total	**6.1**	**-**	**0.1**	**(1.1)**	**-**	**5.1**
Post-employment benefits						
ASEM health cover	6.0	0.2	0.1	(0.3)	-	6.0
Total	**6.0**	**0.2**	**0.1**	**(0.3)**	**-**	**6.0**
Total	**12.7**	**0.2**	**0.2**	**(1.3)**	**-**	**11.8**

This item, amounting to €11.8 million at 31 December 2018, is down €0.9 million compared with the previous year, attributable primarily to the release of provisions for the energy discounts (down €1.5 million).

The following table shows the current service cost and interest income and expense.

(€m)

	LOYALTY BONUSES	*TFR*	ADDITIONAL MONTHS' PAY	PAYMENT IN LIEU OF NOTICE AND OTHER SIMILAR	ENERGY DISCOUNTS	ASEM HEALTH COVER	TOTAL
Net impact recognised in profit or loss							
- current service cost	-	-	-	-	-	0.2	**0.2**
- curtailment (revenue) and other costs				(0.1)	(1.9)	(0.3)	**(2.3)**
- interest income and expense	-	0.1	-	-	-	0.1	**0.2**
TOTAL RECOGNISED IN PROFIT OR LOSS	**-**	**0.1**	**-**	**(0.1)**	**(1.9)**	**-**	**(1.9)**

Revaluation of the net liability for employee benefits had no material impact at 31 December 2018.

Finally, the following tables show the main actuarial assumptions applied, a sensitivity analysis of movements in the assumptions and the payment schedule for the plan. In line with 2017, the interest rate used to determine the present value of the obligation was calculated on the basis of the yield on the Iboxx Eurozone Corporates AA index at 31 December 2018, matching the duration of the relevant group of plan participants.

	LOYALTY BONUSES	*TFR*	ADDITIONAL MONTHS' PAY	ENERGY DISCOUNTS	ASEM HEALTH COVER
Discount rate	1.57%	1.53%	0.77%	1.13%	1.57%
Inflation rate	1.50%	1.50%	0.00%	1.50%	3.00%
Duration (in years)	12.29	10.50	5.79	9.07	9.64

(€m)

	LOYALTY BONUSES	*TFR*	ADDITIONAL MONTHS' PAY	PAYMENT IN LIEU OF NOTICE AND OTHER SIMILAR	ENERGY DISCOUNTS	ASEM HEALTH COVER	TOTAL
Discount rate +0.25%	0.7	4.1	0.6	-	0.3	5.8	**11.5**
Discount rate -0.25%	0.8	4.3	0.6	-	0.3	6.0	**12.0**
Inflation rate +0.25%	0.8	4.3	n/a	n/a	n/a	n/a	**5.1**
Inflation rate -0.25%	0.7	4.1	n/a	n/a	n/a	n/a	**4.8**
Annual rate of increase in health costs +3%	n/a	n/a	n/a	n/a	n/a	7.9	**7.9**
Annual rate of increase in health costs -3%	n/a	n/a	n/a	n/a	n/a	5.0	**5.0**
Conversion rate for KW/h +5%	n/a	n/a	n/a	n/a	n/a	n/a	**-**
Conversion rate for KW/h -5%	n/a	n/a	n/a	n/a	n/a	n/a	**-**

(€m)

	LOYALTY BONUSES	*TFR*	ADDITIONAL MONTHS' PAY	ENERGY DISCOUNTS	ASEM HEALTH COVER	TOTAL
By the end of 2019	-	0.2	0.1	0.4	0.2	0.9
By the end of 2020	-	0.1	0.1	0.5	0.2	0.9
By the end of 2021	0.1	0.3	0.1	0.5	0.2	1.2
By the end of 2022	-	0.2	0.1	0.7	0.2	1.2
By the end of 2023	-	0.2	0.1	0.7	0.2	1.2
After 5 years	0.6	3.2	0.1	(2.5)	5.0	6.4
TOTAL	**0.7**	**4.2**	**0.6**	**0.3**	**6.0**	**11.8**

23. - PROVISIONS FOR RISKS AND CHARGES - €243.5 MILLION

(€m)

	PROVISIONS FOR LITIGATION AND DISPUTES	PROVISIONS FOR SUNDRY RISKS AND CHARGES	PROVISIONS FOR EARLY RETIREMENT INCENTIVES	TOTAL
Amount at 31 December 2017	**23.4**	**157.1**	**63.0**	**243.5**
New provisions	3.6	29.7	-	33.3
Uses and other movements	(8.7)	(44.8)	(9.6)	(63.1)
Restatement of opening balances	-	0.1	-	0.1
Amount at 31 December 2018	**18.3**	**142.1**	**53.4**	**213.8**

Provisions for litigation and disputes - 18.3 million

These provisions, set aside to cover outstanding liabilities that, at the end of the year, could result from court judgements and out-of-court settlements regarding the activities of Group companies, have been assessed partly on the basis of recommendations from internal and external legal advisors. The balance of €18.3 million at 31 December 2018 is down €5.1 million compared with the previous year, reflecting an increase in net uses during the year following positive outcomes to a number of disputes arising in previous years.

Provisions for sundry risks and charges - €142.1 million

These provisions amount to €142.1 million at 31 December 2018, a reduction of €15.0 million compared with the previous year), reflecting:

- net provisions for staff incentive plans, totalling €7.7 million;
- a net decrease of €7.3 million due to the higher value of provisions made in the previous year for urban and environmental redevelopment schemes;
- a reduction of €6.6 million following the payment of expenses by ARERA;
- a reduction of €3.9 million due to an adjustment to the provisions for taxation;
- a net reduction of €3.1 million in provisions linked to regulation of the quality of the electricity service (the mitigation and sharing mechanism introduced by ARERA Resolution 653/2015/R/eel) which, after provisions for estimated penalties linked to outages during the year, reflects payments to distribution companies and releases following final determination of the penalties due to previous years.

Provisions for early retirement incentives - €53.4 million

Provisions for early retirement incentives reflect the estimated extraordinary expenses linked to the early retirement of the Company's employees who have reached pensionable age. This item has decreased by €9.6 million, reflecting payments during the year in relation to the existing plan for generational turnover.

24. OTHER NON-CURRENT LIABILITIES - €196.1 MILLION

This item, amounting to €196.1 million at 31 December 2018, regards the amount payable to Terna Rete Italia S.p.A., resulting from the transfer of net liabilities included in the operations leased to this subsidiary (€39.9 million), accrued grants related to assets receivable (€90.9 million) and the Interconnector Guarantee Fund (€65.3 million), set up by the 2016 Stability Law, in order to fund investment in interconnections by art. 32 of Law 99/09.

The increase of €14.8 million compared with the previous year essentially reflects a combination of movements in the Interconnector Guarantee Fund (up €21.9 million), offset by the settlement of a part of the liabilities included in the leased operations (down €1.9 million), referring to the termination benefits (TFR) payable to personnel participating in the generational turnover plan, and the release of portions of grants related to assets (a reduction of €5.2 million).

25. CURRENT LIABILITIES

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Short-term borrowings *	-	90.0	(90.0)
Current portion of long-term borrowings *	1,229.8	884.0	345.8
Trade payables	2,113.4	2,106.4	7.0
Tax liabilities	8.1	-	8.1
Current financial liabilities *	90.1	105.7	(15.6)
Other current liabilities	196.9	125.6	71.3
TOTAL	**3,638.3**	**3,311.7**	**326.6**

(*) Information on these items is provided in note 21, "Borrowings and financial liabilities.

TRADE PAYABLES - €2,113.4 MILLION

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Suppliers:			
- Energy-related payables	1,540.2	1,624.3	(84.1)
- Non-energy-related payables	124.3	100.7	23.6
Non-energy-related payables due to subsidiaries	447.1	377.0	70.1
Amounts due to associates	1.0	3.6	(2.6)
Payables resulting from contract work in progress	0.8	0.8	-
TOTAL	**2,113.4**	**2,106.4**	**7.0**

Suppliers

- *Energy-related/regulated payables - €1,540.2 million*

The reduction of €84.1 million in this item compared with the previous year essentially reflects energy-related pass-through payables (down €105.6 million). This is primarily due to:

- payables related to provision of the dispatching service (down €81 million), primarily due to a significant reduction during the year in the cost of both demand- and supply-side imbalances;
- payables linked to plants that are essential for the security of the electricity system - UESS (down €113.9 million), reflecting increased payments at the end of the year;
- amounts due from final customers linked to the interruptibility service (down €24.7 million) and amounts due to the Fund for Energy and Environmental Services (Cassa per i Servizi Energetici e Ambientali - CSEA) to cover the cost of the protection service (down €12.6 million);

in part offset by

- payables relating to capacity payments (up €124.7 million), the increase reflecting the cost of the capacity obtained after one single payment made during the year (in accordance with ARERA Resolution 248/2018).

The change also reflects the payable (€22.2 million) resulting from the difference between the amount collected from CSEA for the RENS bonus for 2016 and the related receivable recognised in the financial statements, calculated on a pro-rata basis taking into account the overall results expected in the regulatory period 2016-2019.

- *Non-energy-related payables*

The exposure to suppliers regards invoices received and to be received for contract work, services and purchases of materials and equipment.

The increase compared with the previous year (up €23.6 million) is largely due to increased capital investment towards the end of the year.

Non-energy-related payables due to subsidiaries

This item, totalling €447.1 million, is up €70.1 million compared with the previous year, primarily due to the increased amount payable to Terna Rete Italia S.p.A. (up €64.8 million) as a result of the greater volume of capital expenditure carried out towards the end of the year, compared with the same period of 2017.

Amounts due to associates

This item, amounting to €1.0 million, is down €2.6 million compared with the previous year, reflecting the reduced amount payable to the associate CESI S.p.A., for services provided to the Company, relating to electro technical studies and research.

The commitments assumed by the Company towards suppliers amount to approximately €414.3 million and regard purchase commitments linked to the normal "operating cycle" projected for the period 2019-2023.

Tax liabilities - €8.1 million

This item amounts to €8.1 million at 31 December 2018, compared with a balance of zero last year. This essentially reflected higher payments on account made in the previous year (determined on the basis of a higher rate of IRES in 2016) and an increase in tax payable for 2018 (essentially due to the increase in pre-tax profit).

OTHER CURRENT LIABILITIES - €196.9 MILLION

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Prepayments	64.8	15.9	48.9
Other tax liabilities	26.9	1.6	25.3
Social security payables	7.4	7.1	0.3
Amounts due to personnel	11.5	12.5	(1.0)
Amounts due to subsidiaries	3.9	1.7	2.2
Other amounts due to third parties	82.4	86.8	(4.4)
TOTAL	**196.9**	**125.6**	**71.3**

Prepayments

This item (€64.8 million) regards grants related to assets collected by the Company to fund the construction of non-current assets in progress at 31 December 2018.
Compared with the balance at 31 December 2017 (€15.9 million), the balance is up €48.9 million, essentially due to new prepayments from third parties (up €61.6 million, primarily the Ministry for Economic Development) and other grants received for the re-routing of power lines (up €16.2 million), after the impact of grants deducted directly from the carrying amount of the related assets, totalling €40.5 million.

Other tax liabilities

Other tax liabilities, amounting to €26.9 million, regard withholding tax payable on salaries paid at the end of the year, in addition to the balance of the Group's VAT at the end of the year.
Compared with the balance at 31 December 2017 (€1.6 million), this item is up €25.3 million, broadly reflecting increased payments on account in the previous year as a result of the Ministerial Decree of 27 June 2017, after refundable VAT accruing on the greater volume of purchases by subsidiaries towards the end of the year.

Social security payables

Social security payables, essentially relating to employee contributions payable to INPS (the National Institute of Social Security), amount to €7.4 million, in line with the figure for the previous year.

Amounts due to personnel

Amounts due to personnel, amounting to €11.5 million, primarily regard:

- incentives for personnel and early retirement incentives payable in the subsequent year (€7.7 million);
- amounts due to employees in the form of accrued and unused annual leave and bank holiday entitlements (€2.1 million).

The reduction compared with the previous year (€1.0 million) primarily reflects the higher amount recognised in 2017 for payments to be made to personnel participating in the existing generational turnover plan (€1.2 million).

Other payables due to third parties

Other payables due to third parties, amounting to €82.4 million, essentially relate to guarantee deposits (€67.0 million) received from electricity market operators to guarantee their contractual obligations under dispatching and virtual interconnection contracts. This item also includes deferred income (€7.9 million, primarily attributable to Non-regulated Activities).

The reduction of €4.4 million compared with the previous year primarily reflects a reduction in guarantee deposits (down €4.0 million).

E. Commitments and risks

Risk management

Terna S.p.A.'s financial risk

In the course of its operations, Terna is exposed to different financial risks: market risk, liquidity risk and credit risk.

This section provides information regarding Terna's exposure to all the above risks, along with a presentation of the objectives, policies and processes for managing those risks and the methods used to assess them, with further quantitative disclosures concerning the separate financial statements for 2018.
Terna's risk management policies seek to identify and analyse the risks that the Company is exposed to, establishing appropriate limits and controls and monitoring the risks and compliance with such limits. These policies and the related systems are reviewed on a regular basis, in order to take account of any changes in market conditions or in the Company's operations.

As a part of the financial risk management policies approved by the Board of Directors, Terna S.p.A. has established the responsibilities and operating procedures for financial risk management, specifically as concerns the instruments to be used and the precise operating limits to apply in managing them.

(€m)

	31 DECEMBER 2018		31 DECEMBER 2017	
	RECEIVABLES AT AMORTISED COST	HEDGING DERIVATIVES	RECEIVABLES AT AMORTISED COST	HEDGING DERIVATIVES
Assets				
Derivative financial instruments	-	1.3	-	-
Cash on hand and deposits	945.1	-	1,678.2	-
Trade receivables	1,090.0	-	1,142.6	-
TOTAL	**2,035.1**	**-**	**2,820.8**	**-**

(€m)

	31 DECEMBER 2018			31 DECEMBER 2017		
	PAYABLES AT AMORTISED COST	HEDGING DERIVATIVES	TOTAL	PAYABLES AT AMORTISED COST	HEDGING DERIVATIVES	TOTAL
Liabilities						
Long-term debt	9,401.7	-	9,401.7	9,522.5	-	9,522.5
Derivative financial instruments	-	59.1	59.1	-	9.9	9.9
Trade payables	-	-	-	2,106.4	-	2,106.4
TOTAL	**9,401.7**	**59.1**	**9,460.8**	**11,628.9**	**9.9**	**11,638.8**

Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument may fluctuate as a result of changes in financial market conditions. Market risk includes three types of risk: exchange rate risk, interest rate risk and inflation risk.
Risk management must be performed with the objective of minimising the related risks by selecting counterparties and instruments compatible with the Company's Risk Management Policy. Speculative activity is not form part of the Company's activities.
Terna S.p.A. seeks to adopt a dynamic approach to financial risk management. This approach is characterised by risk aversion, aimed at minimising risk through continuous monitoring of financial markets in order to carry out the planned hedging transactions in favourable market conditions. The dynamic approach enables the Group to intervene in order to improve existing hedges should there be a change in market conditions or changes in the hedged item, making the hedges inappropriate or excessively costly.

The fair value of financial instruments is determined in accordance with the fair value hierarchy envisaged under IFRS 7 (Level 2), by means of appropriate valuation techniques for each category of financial instrument, using market data at the closing date (such as interest rates, exchange rates and volatility) and discounting projected cash flows on the basis of the market yield curve at the reporting date.

Interest rate risk

Interest rate risk is represented by the uncertainty associated with interest rate fluctuations. This is the risk that a change in market interest rates may produce effects on the fair value or future cash flows of financial instruments.
In the course of its operations, Terna is exposed to the risk of fluctuations in interest rates. Its main source of interest rate risk is associated with its borrowings and the related hedges in the form of derivative instruments that generate financial expenses. Terna's borrowing strategy focuses on long-term borrowings, whose term reflects the useful life of the Company's assets. It pursues an interest rate risk hedging policy that aims to guarantee that the percentage of debt represented by fixed rate liabilities is at least 40%, as provided for in the relevant policies. Considering the low level of interest rates and the new regulatory review, all debt is now fixed rate.

At 31 December 2018, interest rate risk is hedged by cash flow hedges, which hedge the risk connected with movements in interest rates relating to long-term borrowings.
Below are the notional amounts and fair values of the derivative financial instruments entered into by Terna:

(€m)

	31 DECEMBER 2018		31 DECEMBER 2017		CHANGE	
	NOTIONAL	FAIR VALUE	NOTIONAL	FAIR VALUE	NOTIONAL	FAIR VALUE
Cash flow hedges	3,225.7	(59.1)	2,546.3	(9.9)	679.4	(49.2)

The notional amount of outstanding cash flow hedges at 31 December 2018, amounting to €3,225.7 million, breaks down as follows:
- €1,325.7 million (fair value loss of €14.7 million) maturing 2021;
- €150.0 million (fair value loss of €3.8 million) maturing 2026;
- €800.0 million (fair value loss of €19.6 million) maturing 2027;
- €950.0 million (fair value loss of €21.0 million) maturing 2028;

Sensitivity to interest rate risk

As regards the management of interest rate risk, following the restructuring of its portfolio, Terna has floating-to-fixed interest rate swaps (cash flow hedges) in place to hedge the risk associated with the expected future cash flows.
Since the hedging relationship between the derivative and the hedged item is formally documented and the effectiveness of the hedge, as verified initially and periodically over its life, is high, the Company has elected to use hedge accounting to ensure a perfect match between the maturities of the hedge and the hedged item. The aim of hedge accounting is to recognise the effects of the hedges and the hedged items in profit or loss at the same time. Accordingly, in the case of cash flow hedges, changes in the fair value of the derivative must be recognised in "Other comprehensive income" (recognising any ineffective portion immediately through profit or loss) and then recycled through profit or loss in the same period in which the cash flows of the hedged instrument materialise. The characteristics of cash flow hedges mirror those of the underlyings, with the timing of the related cash flows matching the timing of interest payments on the debt, without changes in fair value having any impact on profit or loss.

The following table reports the amounts recognised through profit or loss and in "Other comprehensive income" for positions that are sensitive to changes in interest rates, in addition to the theoretical value of the positions following a positive or negative shift in the yield curve and the differential impact of such changes recognised through profit or loss and in "Other Comprehensive Income". A hypothetical 10% movement in interest rates with respect to market interest rates at the reporting date was assumed:

(€m)

	OCI		
	CURRENT RATES 10%	CURRENT VALUES	CURRENT RATES -10%
31 December 2018			
Positions sensitive to interest rate variations (bond issues, CFHs)	(48.8)	**(59.1)**	(69.4)
Hypothetical change	*10.3*	-	*(10.3)*
31 December 2017			
Positions sensitive to interest rate variations (bond issues. CFHs)	(9.1)	**(9.9)**	(10.7)
Hypothetical change	*0.8*	-	*(0.8)*

Inflation risk

As regards inflation risk, the rates established by the regulator to provide a return on Terna S.p.A.'s activities are determined so as to cover the allowed costs. Such cost components are updated on an annual basis to take into account the impact of inflation. Having used an inflation-linked bond issue in 2007, the Company has put in place a partial hedge of net income; in fact, any decrease in expected revenue due to a decrease in the inflation rate would be offset by lower financial expenses.

Exchange rate risk

The management of exchange rate risk must aim to protect a company's earnings from the risk of currency fluctuations by keeping a close eye on market movements and constantly monitoring the existing exposures. In managing this risk, Terna from time to time selects hedging instruments with structures and durations matching the Company's exchange rate exposure. The instruments used by Terna are of limited complexity, highly liquid and easy to price, such as forwards and options. Such contracts have a notional amount and maturity date less than or equal to that of the underlying financial liability, or the expected cash flows, so that any change in the fair value and/or estimated cash flows deriving from a rise or fall in the euro against other currencies is fully offset by a corresponding change in the fair value and/or estimated cash flows of the underlying position.
At 31 December 2018, the component of financial instruments associated with exchange rate risk is residual in nature and attributable to the investments in Latin America. This exposure is managed, at 31 December 2018, via currency hedges with a notional value of €368.9 million and a fair value gain of €1.3 million.

Liquidity risk

Liquidity risk is the risk that Terna might encounter difficulty in discharging its obligations in respect of its financial liabilities and operating cycle. Liquidity risk management seeks to ensure adequate coverage of borrowing requirements by obtaining adequate lines of credit and appropriate management of any surplus liquidity. At 31 December 2018, Terna has available short-term credit lines of approximately €789.9 million and revolving credit lines of €2,450 million.

Credit risk

Credit risk is the risk a customer or one of the counterparties to a transaction in financial instruments could cause a financial loss by failing to discharge an obligation. It is mainly generated by the Company's trade receivables and financial investments.
The credit risk originated by open positions on transactions in derivatives is considered to be marginal since the counterparties, in compliance with the financial risk management policies adopted, are leading international banks with high ratings.

Terna provides its services essentially to counterparties considered solvent by the market, and therefore with a high credit standing, and does not have high concentrations of credit risk.
Credit risk management is driven by the provisions of ARERA Resolution 111/06, which, in art. 49, introduced instruments designed to limit the risks related to the insolvency of dispatching customers, both on a preventive basis and in the event of an actual insolvency. In particular, the Resolution establishes three instruments to safeguard the electricity market: a guarantee system (bank guarantees provided by individual dispatching customers, based on their turnover); the option of terminating dispatching contracts (in the event of insolvency or failure to replace enforced guarantees); and, finally, the possibility of recovering uncollected debts, after having taken all other possible collection actions, through a specific fee to be fixed by the regulator.

The following table summarises the exposure to such risk at the reporting date:

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017	CHANGE
Cash and cash equivalents	945.1	1,678.2	(733.1)
Trade receivables	1,090.0	1,142.6	(52.6)
TOTAL	**2,035.1**	**2,820.8**	**(785.7)**

The total value of the exposure to credit rate risk at 31 December 2018 is represented by the carrying amount of trade receivables and cash and cash equivalents.

The following tables provide qualitative information on trade receivables regarding the geographical distribution and type of customers.

GEOGRAPHICAL DISTRIBUTION

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017
Italy	1,059.3	1,085.8
Euro-area countries	14.0	56.1
Other countries	16.7	0.7
TOTAL	**1,090.0**	**1,142.6**

CUSTOMER TYPE

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017
Distributors	309.8	311.2
CSEA	114.0	95.3
Dispatching customers for injections	200.8	195.9
Dispatching customers for withdrawals	408.9	465.3
Parties which have signed virtual import contracts and virtual import services (interconnectors and shippers)	13.7	13.2
Sundry receivables	42.8	61.7
TOTAL	**1,090.0**	**1,142.6**

The following table breaks down customer receivables by due date, reporting any potential impairment.

(€m)

	31 DECEMBER 2018		31 DECEMBER 2017	
	IMPAIRMENT	GROSS	IMPAIRMENT	GROSS
Current	(0.4)	949.7	-	1,057.7
0-30 days past due	(0.1)	0.8	-	32.4
31-120 days past due	(0.4)	4.6	-	27.9
Over 120 days past due	(37.1)	172.9	(38.3)	62.9
TOTAL	**(38.0)**	**1.128.0**	**(38.3)**	**1,180.9**

Movements in the allowance for doubtful accounts in the course of the year were as follows.

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017
Balance at 1 January*	(38.7)	(37.4)
Release of provisions	1.4	0.5
Impairments for the year	(0.7)	(1.4)
Balance	**(38.0)**	**(38.3)**

** The opening balance at 1 January 2018 was adjusted by €0.4 million following application of the new standard, IFRS9.*

The value of guarantees received from eligible electricity market operators is illustrated below.

(€m)

	31 DECEMBER 2018	31 DECEMBER 2017
Dispatching - injections	233.7	236.6
Dispatching - withdrawals	1,099.6	1,185.2
Transmission charges due from distributors	305.0	302.4
Virtual imports	84.0	81.1
Balance	**1,722.3**	**1,805.3**

In addition, Non-regulated Activities are exposed to "counterparty risk", in particular in relation to the entities with which sales contracts are entered into, in consideration of the credibility and solvency of the parties in question and the impact that their possible insolvency could have on the financial strength of the business. Counterparty risk is mitigated by implementing special procedures to assess counterparties, measuring operating, financial and reputational aspects of the counterparties in question.

Default risk and debt covenants

This risk is associated with the possibility that the loan agreements or bond terms and conditions to which the Company is a party may contain provisions authorising counterparties to call in such loans immediately upon the occurrence of certain events, thereby generating liquidity risk. More information on the contractual provisions of outstanding borrowings at 31 December 2018 is provided in the section, "Borrowings and financial liabilities" in the notes to Terna S.p.A.'s consolidated financial statements.

Parent company guarantees issued in favour of subsidiaries' suppliers

The Company has issued parent company guarantees in favour of third parties to guarantee fulfilment of a number of contractual obligations assumed by the subsidiaries Terna Interconnector S.r.l., Terna Rete Italia S.p.A., Difebal S.A. and Terna Crna Gora d.o.o.. The Company's maximum exposure at 31 December 2018 amounts to €533,5 million, including €452.4 million relating to the private Italy-France Interconnector project. With regard to the long-term borrowing arranged by the Uruguayan subsidiary, Difebal, on 14 July 2017, Terna S.p.A. signed a Sponsor Support Agreement that includes a parent company commitment to inject contingent equity of up to US$50 million.

Litigation

The main commitments and risks not disclosed in the statement of financial position at and for the year ended 31 December 2018, relating to the Company are described below.

Environmental and urban planning litigation

Part of environmental litigation deriving from the construction and operation of Terna's power plants, consists of legal actions taken against the alleged negative effects of electric and magnetic fields generated by power lines. In general, this litigation necessarily involves the Company, which owns the infrastructure in question.
Moreover, it cannot be ruled out that the parties concerned may also initiate legal proceedings against the subsidiary Terna Rete Italia S.p.A., as the electromagnetism generated by power lines relates not only to ownership of the plant, but also to its operation and the quantity and quality of electricity it transports.
Regarding this matter, it should be noted that the issue of the Cabinet Office Decree of 8 July 2003 - which specifically set the values of the three parameters (exposure limits, safety thresholds and quality targets) provided for in Framework Law 36 of 22 February 2001, which electricity infrastructure must comply with - led to a significant reduction in any such litigation.
Other environmental and urban planning disputes, which do not relate to electromagnetic fields, are also pending with regard to Terna S.p.A.. These disputes are connected with the operation of certain Terna-owned plant, which in the event of an unfavourable outcome could also generate immediate effects for Terna Rete Italia S.p.A. (to date unforeseeable and therefore not included in "Provisions for litigation and sundry risks"), both as the entity appointed by Terna S.p.A. to build the related infrastructure and as the entity responsible for its operation. In particular, charges may arise for the subsidiary Terna Rete Italia S.p.A., connected with changes to the infrastructure involved in such disputes and its temporary unavailability. However, after examination of the disputes in question by Terna S.p.A. and external counsel appointed by the Company, it appears that the possibility of any negative outcomes is remote.

Litigation regarding the legitimacy of construction permits and plant operations

Another aspect of litigation connected with the plant owned by the Company derives from legal actions brought before the competent administrative courts, aimed at obtaining the annulment of decisions granting consent for the construction and operation of infrastructure.

Litigation relating to activities carried out under concession

As the operator of transmission and dispatching activities since 1 November 2005, the Company has been a party in a number of court cases, most of which have contested determinations adopted by ARERA (Italy's Regulatory Authority for Energy, Networks and the Environment), and/or the Ministry for Economic Development, and/or Terna, in relation to these activities. In cases in which the plaintiffs have, in addition to inherent defects in the contested determinations, alleged violation of the regulations laid down by the aforementioned authorities, or in cases in which the determination has had an impact on Terna, the Company has also taken action to defend its interests through the legal system. Within the scope of such litigation - even though some cases have been concluded, at first and/or second instance, with the annulment of ARERA's resolutions and, when applicable, of the consequent determinations adopted by Terna - any negative outcomes for the Company itself may be deemed unlikely, as these disputes normally relate to pass-through items.

Litigation regarding supply contracts

In the opening months of 2019, Terna initiated the necessary liability actions against certain suppliers, in response to their violation of article 101 of the Treaty on the Functioning of the European Union, prohibiting anti-competitive behaviour. Such behaviour was confirmed by the European Commission in 2014 in decision C (2014) 2139 of 2 April 2014, as upheld in full by the court at first instance ruling of 18 July 2018. The Company's actions aim to obtain redress for the inefficiencies caused by the illegal conduct of the above external suppliers.

F. Business combinations

There were no business combinations in 2018.

G. Related party transactions

Given that Terna S.p.A. is subject to the *de facto* control of Cassa Depositi e Prestiti S.p.A., a situation ascertained in 2007, related party transactions entered into by Terna during the year include transactions with subsidiaries, associates (Cesi S.p.A., Coreso S.A. and CGES) and employee pension funds (Fondenel and Fopen), as well as transactions with Cassa Depositi e Prestiti itself, with CDP Reti S.p.A. and with the companies directly or indirectly controlled by the Ministry of the Economy and Finance ("MEF").
Given that Terna S.p.A. and the above companies meet the definition for classification as "government-related entities", in accordance with IAS 24 - Related Party Disclosures, the Group has elected to adopt the partial exemption - permitted by the standard - from the disclosure requirements in respect of other companies controlled, influenced or jointly controlled by the same government entity. The remainder of this section provides qualitative and quantitative disclosures on transactions with government-related entities having a significant impact on the Group's results. Amounts relating to pass-through items are not included in these disclosures.
Related party transactions in 2018 broadly regard the provision of services in the course of ordinary activities and conducted on an arm's length basis.
Under the Terna Group's current organisational structure, the subsidiary, Terna Rete Italia S.p.A., which has entered into an agreement with the Company covering the lease of certain operations and a number of related intercompany agreements. In accordance with the these arrangements, the subsidiary is responsible for the traditional activities involved in operation and routine and extraordinary maintenance of the owned portion of the NTG, and for management and implementation of the grid development initiatives included in the related concession arrangement for transmission and dispatching operations, as set out in Terna's Development Plan.
Terna is responsible for managing the operations of all its subsidiaries under specific service agreements which, in addition to covering administrative and financial coordination and the coordination of relations with government bodies and other institutions, give the Company the right to act on behalf of its subsidiaries, or in their name and on their behalf.
The Company's Non-regulated Activities are conducted in Italy and overseas through the subsidiaries, Terna Energy Solutions S.r.l. and Terna Plus S.r.l. under existing intercompany service agreements.

From a financial viewpoint, Terna is responsible for subsidiaries' cash management in accordance with specific treasury management arrangements. These cover the conduct and coordination of all the transactions carried out from time to time, in order to manage financial resources and meet subsidiaries' cash and treasury requirements, and the execution of any other related transaction.

The following table shows the contractual terms and conditions governing financial relations with subsidiaries.

	DEPOSITS*	WITHDRAWALS
Terna Rete Italia S.p.A.	monthly average 1-month Euribor +0.30%	monthly average 1-month Euribor +0.80%
Rete S.r.l.	monthly average 1-month Euribor +0.30%	monthly average 1-month Euribor +0.80%
Terna Energy Solutions S.r.l.	monthly average 1-month Euribor +0.30%	monthly average 1-month Euribor +0.80%
Terna Plus S.r.l.	monthly average 1-month Euribor +0.30%	monthly average 1-month Euribor +0.80%
Resia Interconnector S.r.l.	monthly average 1-month Euribor +0.30%	monthly average 1-month Euribor +0.80%
Monita Interconnector S.r.l.	monthly average 1-month Euribor +0.30%	monthly average 1-month Euribor +0.80%
Difebal S.A.	0.01%	monthly average 3-month Libor +1.30%
Rete Verde 17 S.r.l.	monthly average 1-month Euribor +0.30%	monthly average 1-month Euribor +0.80%
Rete Verde 18 S.r.l.	monthly average 1-month Euribor +0.30%	monthly average 1-month Euribor +0.80%
Rete Verde 19 S.r.l.	monthly average 1-month Euribor +0.30%	monthly average 1-month Euribor +0.80%
Rete Verde 20 S.r.l.	monthly average 1-month Euribor +0.30%	monthly average 1-month Euribor +0.80%

** If the sum of average 1-month Euribor and the spread of 0.30% is negative, the interest rate applied will be 0.01%.*

Existing intercompany agreements at 31 December 2018 are summarised below.

COUNTERPARTY	TYPE	ANNUAL FEE
Terna Rete Italia S.p.A.	**Service agreement:**	
	Operation & Maintenance	€270,703,680
	Upgrade and development	equal to costs incurred + 5.82% of personnel expenses incurred
	Administrative, support and consultancy services	
	- from Terna S.p.A. to Terna Rete Italia S.p.A. (revenue-generating)	€18,384,832
	- from Terna Rete Italia S.p.A. to Terna S.p.A. (cost-generating)	€4,952,851
	Rental of workstations for staff	
	- from Terna S.p.A. to Terna Rete Italia S.p.A. (revenue-generating)	€1,840,148
	- from Terna Rete Italia S.p.A. to Terna S.p.A. (cost-generating)	€396,124
	Lease of operations	€35,046,653
Rete S.r.l.	**Service agreement:**	
	Upgrade and development	equal to costs incurred + 5.82% of personnel expenses incurred
	Admin., support and consultancy service agreement (revenue-generating)	€1,083,506
Terna Plus S.r.l.	**Service agreement:**	
	Terna's Non-regulated Activities (cost-generating)	€129,164
	Management fee (revenue-generating)	€1,123,052
	Rental of workstations for staff (revenue-generating)	€132,532
Terna Energy Solutions S.r.l.	**Service agreement:**	
	Terna's Non-regulated Activities (cost-generating)	*€125,243*
	Management fee (revenue-generating)	*€364,275*
	Rental of workstations for staff (revenue-generating)	€239,603
Tamini Group	**Administrative service agreement (revenue-generating)**	€510,381
Terna Interconnector S.r.l.	**Administrative service agreement (revenue-generating)**	€630,687
	Management and coordination of civil works for Italy-France Interconnector (cost-generating)	equal to costs incurred + 5.82% of personnel expenses incurred
Monita Interconnector S.r.l.	*Administrative, operational support and project preparation services*	€144,396
Difebal S.A.	**Service agreement**	
	Administrative services	€104,835
	Technical services	variable based on volume of services effectively rendered. "Transportation stub" costs.
Terna Crna Gora d.o.o.	**Service agreement:**	
	Technical services	equal to costs incurred + 5.82%
	Administrative services	€42,973
Avvenia The Energy Innovator S.r.l.	**Administrative service agreement (revenue-generating)**	€99,233
Rete Verde 17 S.r.l.	*Management fee (revenue-generating)*	€4,686 for each counterparty company
Rete Verde 18 S.r.l.		
Rete Verde 19 S.r.l.		
Rete Verde 20 S.r.l.		

Terna S.p.A. is the consolidating entity in a tax consolidation arrangement for the purposes of corporation tax (IRES), in which the following subsidiaries participate: Terna Rete Italia S.p.A., Rete S.r.l., Terna Plus S.r.l., Terna Energy Solutions S.r.l. and Tamini Trasformatori S.r.l..

The nature of sales to and purchases from related parties[1] by the Company is shown below, followed by details of the revenue and costs resulting from such transactions during the year, and the related receivables and payables outstanding at 31 December 2018.

RELATED PARTY	REVENUE-GENERATING TRANSACTIONS	COST-GENERATING TRANSACTIONS
Parent		
Cassa Depositi e Prestiti S.p.A.		Credit facilities.
Related parties: subsidiaries operating in Regulated Activities		
Terna Rete Italia S.p.A.	Rental for leased operations, administrative services, rental of workstations and other services	Maintenance and other technical services, grid upgrade and development, quality of service allowance, administrative services, rental of workstations for staff
Rete S.r.l.	Provision of technical and administrative services	Transmission charge
Terna Crna Gora d.o.o.	Administrative services, services provided by seconded personnel and staff on temporary transfers	
Related parties: subsidiaries operating in Non-regulated Activities		
Terna Energy Solutions S.r.l.	Technical, administrative and financial services, rental of spaces and workstations	Operation of Non-regulated Activities
Terna Plus S.r.l.	Technical, administrative and financial services, rental of spaces and workstations	Operation of Non-regulated Activities
Gruppo Tamini	Administrative and other services	
Terna Interconnnector S.r.l.	Administrative and consultancy services, loan agreements	Management and coordination of performance of civil works for Italy-France interconnector
Monita Interconnector S.r.l.	Administrative, operational support and preparation services in relation to interconnector project	
Santa Maria Transmissora de Energia S.A. (Brazil)	Financial services	Loans
Santa Lucia Transmissora de Energia S.A. (Brazil)	Financial services	Loans
Difebal S.A.	Administrative and legal services	
Rete Verde 17 S.r.l.	Administrative services	
Rete Verde 18 S.r.l.		
Rete Verde 19 S.r.l.		
Rete Verde 20 S.r.l.		
Associates		
Cesi S.p.A.	Rental income on laboratories and other similar facilities for specific uses, dividends	Technical studies and consultancy, research, design and experimentation.
CORESO S.A.		Technical coordination service for the TSO.
CGES	Dividends	
Other related parties		
GSE Group	Metering charge, dispatching charge	Rental of spaces and workstations.
Enel Group	Transmission charge and aggregation of meter readings, dispatching charge, leases and rentals, power line maintenance, movement / re-routing of power lines, housing of fibre cable and maintenance of communications carried over proprietary power lines	Recovery of energy discount, building services, MV power to new substations, specialist services for connection to Terna's control and protection systems.
Ferrovie Group	Dispatching charge, movement of power lines	Right-of-way fees.
Snam Rete Gas	Dispatching charge	Contributions for NTG connections, sundry services.
ENI Group		Sundry services.
Poste Italiane	Movement /re-routing of power lines	Right-of-way fees.
ANAS S.p.A.		Sundry services.
Other related parties of the MEF		Pension contributions payable by the Terna Group.
Fondenel and Fopen	Metering charge, dispatching charge	Rental of spaces and workstations.

[1] The nature of the items related to centralised treasury management and the tax consolidation already described above are excluded from the table.

REVENUE AND COSTS

(€m)

	REVENUE COMPONENTS		COST COMPONENTS	
	TRANSMISSION CHARGE AND OTHER REVENUE FROM REGULATED ACTIVITIES	NON-ENERGY-RELATED ITEMS	DIVIDENDS	NON-ENERGY-RELATED ITEMS
Subsidiaries				
Terna Rete Italia S.p.A.	-	56.1	-	306.5
Santa Maria Transmissora de Energia S.A. (Brazil)	-	1.7	-	-
Santa Lucia Transmissora de Energia S.A. (Brazil)	-	5.0	-	-
Terna Crna Gora d.o.o.	-	0.6	-	-
Terna Plus S.r.l.	-	1.8	-	0.1
Tamini Group	-	0.6	-	-
Terna Energy Solutions S.r.l.	-	0.7	-	0.1
Rete S.r.l.	-	1.3	-	-
Terna Interconnector S.r.l.	-	0.8	-	-
Monita Interconnector S.r.l.	-	0.2	-	-
Avvenia The Energy Innovator S.r.l.	-	0.1	-	-
Difebal S.A.	-	1.0	-	-
Total subsidiaries	**-**	**69.9**	**-**	**306.7**
De facto parent				
Cassa Depositi e Prestiti S.p.A.	-	-	-	3.1
Total de facto parent	**-**	**-**	**-**	**3.1**
Associates:				
Cesi S.p.A.	-	0.2	1.1	0.3
CORESO S.A.	-	-	-	1.6
Total associates	**-**	**0.2**	**1.1**	**1.9**
Other related parties:				
GSE Group	19.0	-	-	0.1
Enel Group	1,564.1	15.5	-	0.1
Eni Group	6.8	-	-	0.3
Ferrovie Group	2.4	0.3	-	0.2
ANAS S.p.A.	-	-	-	0.2
SNAM Rete e Gas		0.2	-	-
Total other related parties	**1,592.3**	**16.0**	**-**	**0.9**
Pensions funds:				
Fondenel	-	-	-	0.3
Fopen	-	-	-	0.4
Total pension funds	**-**	**-**	**-**	**0.7**
TOTAL	**1,592.3**	**86.1**	**1.1**	**313.3**

ASSETS AND LIABILITIES

(€m)

	PROPERTY, PLANT AND EQUIPMENT	RECEIVABLES AND OTHER ASSETS		PAYABLES AND OTHER LIABILITIES		BALANCE ON INTER-COMPANY TREASURY ACCOUNT	GUARANTEES**
	CAPITALISED COSTS	OTHER	FINANCIAL	OTHER	FINANCIAL		
Subsidiaries							
Terna Rete Italia S.p.A.*	56.2	13.9	-	477.4	-	(247.9)	-
Santa Maria Transmissora de Energia S.A. (Brazil)	-	-	22.3	-	-	-	-
Santa Lucia Transmissora de Energia S.A. (Brazil)	-	-	67.2	-	-	-	-
Terna Crna Gora d.o.o.	-	0.1	-	-	-	-	-
Terna Plus S.r.l.*	-	0.8	-	2.2	-	32.1	-
Tamini Group*	13.8	0.7	-	2.4	-	-	-
Terna Energy Solutions S.r.l.*	-	0.5	-	1.6	-	28.7	-
Rete S.r.l.*	-	0.4	-	6.2	-	(19.7)	-
Terna Interconnector S.r.l.	1.5	0.2	-	4.2	-	-	-
Monita Interconnector S.r.l.	-	0.1	-	-	-	0.6	-
Avvenia The Energy Innovator S.r.l.	-	0.1	-	-	-	-	-
Terna Chile S.p.A.	-	0.2	-	-	-	-	-
Difebal S.A.	-	0.9	9.9	-	-	-	-
Rete Verde 17 S.r.l.	-	-	-	-	-	0.2	-
Rete Verde 18 S.r.l.	-	-	-	-	-	0.1	-
Rete Verde 19 S.r.l.	-	-	-	-	-	0.6	-
Rete Verde 20 S.r.l.	-	-	-	-	-	0.5	-
Total subsidiaries	**71.5**	**17.9**	**99.4**	**494.0**	**-**	**(204.8)**	**-**
De facto parent							
Cassa Depositi e Prestiti S.p.A.	-	-	-	-	500.5	-	-
Total de facto parent	**-**	**-**	**-**	**-**	**500.5**	**-**	**-**
Associates:							
Cesi S.p.A.	1.0	0.2	-	0.9	-	-	1.2
CORESO S.A.	-		-	0.1	-	-	-
CGES	-	3.3	-		-	-	-
Total associates	**1.0**	**3.5**	**-**	**1.0**	**-**	**-**	**1.2**
Other related parties:							
GSE Group	-	3.1	-	0.1	-	-	-
Enel Group	0.5	399.3	-	2.2	-	-	586.2
Eni Group	-	1.4	-	1.2	-	-	32.8
Ferrovie Group	0.1	0.4	-	9.4	-	-	24.2
ANAS S.p.A.	0.2	0.1	-	0.2	-	-	-
Snam Rete Gas S.p.A.	-	-	-	0.7	-	-	-
Other related parties of MEF	-	-	-	-	-	0,1	-
Total other related parties	**0.8**	**404.3**	**-**	**13.8**	**-**	**0.1**	**643.2**
Pension funds:							
Fopen	-	-	-	0.3	-	-	-
Total pension funds	**-**	**-**	**-**	**0.3**	**-**	**-**	**-**
TOTAL	**73.3**	**425.7**	**99.4**	**509.1**	**500.5**	**(204.7)**	**644.4**

* *The balances for the item, "Other", include receivables and payables relating to the tax consolidation arrangement for IRES.*
** *Guarantees regard surety bonds received from contractors.*

H. Significant non-recurring, atypical or unusual events and transactions

With the exception of the instances described above, no significant non-recurring, atypical or unusual events or transactions, involving either third or related parties, took place in 2018.

I. Notes to the statement of cash flows

Cash flow from **continuing operations** amounts to €1,208.1 million, with approximately €1,537.7 million in operating cash flow and an outflow of approximately €329.6 million generated by changes in net working capital.

The cash outflow for **investing activities** totals approximately €888.0 million and above all regards €793.8 million relating to investment in property, plant and equipment, €58.4 million invested in intangible assets and €15.1 million in capitalised financial expenses, in addition to the subscription for new shares issued by Terna Crna Gora d.o.o., totalling €59 million.
The net cash outflow for **shareholder transactions** amounts to €452.5 million, primarily reflecting payment of the final dividend for 2017 (€292.9 million) and the interim dividend for 2018 (€158.2 million).
As a result, net cash used in investing activities and to provide a return on equity during the year amounted to €1,340.5 million, for the most part covered by cash flow from continuing operations of €1,208.1 million. The remainder was funded through the use of cash reserves. Net debt has risen by €55.3 million compared with the previous year.

The following table shows the reconciliation of liabilities deriving from financing activities in the statement of cash flows:

(€m)

	31 DECEMBER 2017	CASH FLOW FROM FINANCING ACTIVITIES	CHANGE IN FV AND OTHER	31 DECEMBER 2018
- Long-term borrowings (including current portion)	9,522.5	(9.7)	(111.1)	9,401.7
- Short-term borrowings	90.0	(90.0)	-	-
- Loans to subsidiaries *	-	(99.5)	-	(99.5)
- Government securities *	-	(401.5)	(1.1)	(402.6)
Net change deriving from financing activities	**9,612.5**	**(600.7)**	**(112.2)**	**8,899.6**

** Included in "Non-current financial assets" and "Current financial assets" in the statement of financial position.*

L. Government grants

Article 1, paragraphs 125 to 129, of Law 124 of 4 August 2017 (the annual markets and competition law) has introduced a number of measures designed to ensure the transparency of the government grants system. These measures include an obligation for the relevant companies to disclose the grants received (paragraph 125) and those disbursed (paragraph 126) in their annual financial statements.

In accordance with Circular 5 of 22 February 2019 "Transparency in the government grants system: an assessment of the regulations and interpretation guidance", published by Assonime in February 2019, the Terna Group has adopted the following basis of reporting for government grants:
- the regulations only apply to entities resident in Italy;
- grants have the nature of grants or donations, and represent incentives or subsidies designed to give beneficiaries a recognised economic advantage; the grants therefore take the form of donations or giving and public aid for specific purposes, and are not awarded under a general aid regime;
- the public resources used are exclusively "national";
- grants are reported on a cash basis and if the amount is not less than €10,000 (with reference to each individual beneficiary) in the reporting period.

In line with the above, the following table shows government grants collected/disbursed by the Company in 2018:

GRANTS RECEIVED (PARAGRAPH 125)

	GRANTOR					
BENEFICIARY ENTITY	NAME	TAX CODE	VAT NUMBER	TYPE OF TRANSACTION	AMOUNT (€)	NOTE
TERNA S.p.A.	Ministry for Economic Development	80230390587	80230390587	State aid*	47,053,290.76	Advance on grants awarded for Terna S.p.A. projects financed by government grants, with funding provided under the National Operational Programme (NOP) for Enterprises and Competitiveness 2014 - 2020 ERDF - AXIS IV - investment priority 4d - Action 4.3.1
TERNA S.p.A.	Sicily Regional Authority	80012000826	02711070827	State aid*	14,499,449.49	Advance on grants awarded for Terna S.p.A. projects financed by government grants, with funding provided under the Regional Operational Programme (ROP) ERDF Sicily 2014 - 2020 - OT4 - Action 4.3.1
TOTAL					**61,552,740.25**	

** This transaction is covered by the obligation to publish in the National State Aid Register.*

GRANTS DISBURSED (PARAGRAPH 126)

	BENEFICIARY					
GRANTOR	NAME	TAX CODE	VAT NUMBER	TYPE OF TRANSACTION	AMOUNT (€)	NOTE
TERNA S.p.A.	ISTITUTO NAZIONALE PER L'ASSICURAZIONE CONTRO GLI INFORTUNI SUL LAVORO		00968951004	Giving	12,000	The first edition of the Biennial Masters in "Integrated Safety and Health Management in a Changing Workplace"
TERNA S.p.A.	Fondazione Bambino Gesù Onlus	97531780589		Giving	40,000	Financial support for the provisions of accommodation for children's families
TOTAL					**52,000**	

M. Proposal for appropriation of profit for the year

Terna S.p.A.'s Board of Directors proposes to pay a total dividend of €468,730,134.40 for 2018, equal to €0.2332 per share, of which €0.0787 per share was declared in the form of an interim dividend on 9 November 2018.
The Board of Directors thus proposes to appropriate Terna S.p.A.'s profit for 2018, amounting to €661,291,201.83, as follows:

- €158,186,370.40 to cover payment of the interim dividend payable from 21 November 2018;
- €310,543,764.00 to pay a final dividend of €0.154500 to the holders of each of the 2,009,992,000 ordinary shares outstanding at the date of this Board of Directors' meeting. The final dividend will be payable on 26 June 2019, with an ex-dividend date for coupon 30 of 24 June 2019 and a record date (as defined by art.83-terdecies of Legislative Decree 58 of 24 February 1998, the Consolidated Law on Finance of 25 June 2019);
- €192,561,067.43 to be taken to retained earnings.

N. Events after 31 December 2018

Transfer of a business unit

With effect from **1 January 2019**, Terna S.p.A. transferred a business unit to Terna Rete Italia S.p.A. under the transfer deed executed on 20 December 2018. The unit consists of the personnel, assets and service agreements involved in the provision of building management, maintenance and support services and facility management for a number of properties owned by Terna S.p.A..
The parties have established a value for the business unit, based on a specific expert appraisal, of €17,949,501.00, including €180,000.00 in the form of new shares issued by Terna Rete Italia S.p.A..
Under the above service agreement, Terna S.p.A. pays Terna Rete Italia S.p.A. an annual fee of €224,000.00 (plus VAT at the statutory rate), in addition to the reimbursement of documented expenses.

Revised zonal configuration for Brindisi, Foggia and Priolo

From **1 January 2019**, the new zonal configuration came into force. Compared to the past, the new arrangement has combined the production nodes with limited capacity in Brindisi, Foggia and Priolo with neighbouring zones (the South and Sicily zones, respectively), as well as transferring the Gissi node from the South to the Central-South zone. This change was made in accordance with the European CACM Regulation, which all the regulatory authorities and TSOs of European Union member states must comply with. In particular, the changes made are aimed at ensuring safe operation of the transmission system, as well as boosting the efficiency and cost-effectiveness of the electricity market. In Resolution 386/2018/R/eel, ARERA has approved Terna's proposed revision of the zonal configuration following the review process carried out in 2018 pursuant to the European CACM Regulation and ARERA Resolution 22/18/R/eel.

Private placement of green bond issue

On **10 January 2019**, Terna S.p.A. launched a fixed-rate green bond issue in the form of a private placement, amounting to €250 million. The issue was assigned ratings of "BBB+" by Standard and Poor's, "(P)Baa2" by Moody's and "BBB+" by Fitch. The proceeds will be used to finance the Company's eligible green projects, thus confirming the Group's strategy oriented towards combining sustainability with growth, in order to promote the ongoing energy transition and generate ever increasing benefits for Italy and its stakeholders.

Bloomberg Gender Equality Index

On **16 January 2019**, Terna was included for the first time in the Bloomberg Gender Equality Index (GEI), an international index that measures companies' performance regarding gender equality issues and the quality and transparency of their public reporting, a decisive factor in the overall assessment. For 2019, Bloomberg analysed over 9,000 companies listed on leading world financial markets, including only 230 of them in the GEI index (in total, there are three Italian companies), from 36 countries and representing 10 different sectors (including energy, industry, utilities and finance).

Veneto Regional Authority and Terna: Investment programme

On **21 January 2019**, the Governor of the Veneto Region, Luca Zaia, and Terna's Chief Executive Officer, Luigi Ferraris, signed a planning agreement regarding extraordinary works relating to the security of the electricity system and development of the region, with the aim of promoting sustainable development in the Veneto region and helping local society and the economy to recover from the exceptional weather events of November 2018 by rebuilding and developing regional electricity infrastructure. In this sense, Veneto Regional Authority and Terna have committed to adopting the most advanced forms of cooperation, with local authorities and communities to be closely and fully involved in deciding on the works and initiatives to be undertaken in the various areas. The agreement provides for substantial investment in the implementation of vital works on the Veneto electricity grid, the most significant being an upgrade between Venice and Padua at a cost of over €400 million.

Co-optation of a new Director on to the Board of Directors

Following the resignation of the non-executive Director, Stefano Saglia, on **15 February 2019**, Terna S.p.A.'s Board of Directors co-opted a new non-executive Director, Paolo Calcagnini (the Chief Financial Officer of Cassa Depositi e Prestiti S.p.A.), on to the Board in response to the invitation from the Cassa Depositi e Prestiti Group which, in a letter dated 6 February 2019, submitted Mr Calcagnini's candidacy for the Company's appropriate and independent evaluation.

Establishment of PI.SA. 2 S.r.l.

A new wholly owned subsidiary of Terna S.p.A., named PI.SA. 2 S.r.l., was established on **15 February 2019**. The company's purpose is the design, construction, management, development, operation and maintenance, including for third parties, of power lines and grid infrastructure and other infrastructure connected to the grid, in addition to plant and equipment used in the electricity transmission sector. The company will also engage in research, consulting and support on matters relating to the core business, conduct any form of activity enabling the improved use and deployment of the networks, structures, resources and expertise employed.

Terna and Genoa's electricity grid

As part of the planned rationalisation of the electricity grid in the city of Genoa, on **18 February 2019**, Terna completed the laying of underground cables for the 132kV power lines linking the Fiera and Central primary substations and the Genoa T. and Fiera primary substations. The works are necessary to support the increase in port activities, thanks to the modernisation of the local grid, and for the implementation of strategic projects for the development and urban renewal of the city of Genoa, which was badly hit by the collapse of the Morandi road bridge last August.

New electricity line in Brazil to drive development of renewable sources

The new high-voltage power line extending 158 km in Rio Grande do Sul, which will enable full integration of large quantities of energy produced from renewable sources, above all from wind, into the Brazilian national grid, was inaugurated on **19 February 2019**. Terna, through its subsidiary Santa Maria Transmissora de Energia, activated the new "Santa Maria 3 - Santo Angelo 2" 230 kV power line in the south-east of Brazil, considered of significant importance for the Rio Grande do Sul region, as it will allow for the integration of energy generated by wind farms in the south of Brazil into the Brazilian national transmission grid. With over 80% of electricity produced from clean sources and wind production having increased by 20% in the last year, Brazil currently represents the largest Latin American energy market and is among the top five in the world for its development potential.

Restructuring in the Venetian Lagoon

The underground and submarine cables for the 132kV power lines between the Sacca Serenella Primary Substation - Cavallino Primary Substation entered service on **21 February 2019**. This date also marks the start of work on other projects, such as demolition of the Fusina 2 - Sacca Fisola overhead power line, covering a distance of 6.5 km, and the removal of 24 electricity pylons, most of which located in the lagoon area, in order to boost the efficiency and security offered by the electricity grid in the area of the Venetian Lagoon.
Terna has also embarked on preparations for the demolition of a section of the Villabona - Fusina 2 line where it interferes with the area known as the Vallone Moranzani. Once the removal of the conductors has been completed, it will possible to begin the dismantling of approximately 2 km of power lines and 9 pylons. The work will lead to the demolition of a further 3.6 km of lines, making a total of 15 lines located in the Malcontenta and Venice Ro-Ro port areas.

Restructuring of the Rimini - Riccione electricity grid

On **27 February 2019**, Terna presented its plan for the restructuring of the grid in the Rimini area, aimed at boosting the security and efficiency of the area's electricity system, above all during the summer season, when electricity consumption rises significantly, with the consequent risk of outages. A total of 8 municipalities are covered by the plan: Rimini, Riccione, Coriano, Sant'Arcangelo di Romagna, San Mauro Pascoli, Savignano sul Rubicone, Gatteo and Gambettola.
In Rimini, 84 pylons and around 21 km of power lines will be demolished, to be replaced with approximately 9 km of new underground lines and two new pylons. The city centre will benefit from the large area of land that removal of the old infrastructure will free up, above all two elementary schools, the “Padulli” and “Rodari”, located in the area in which the restructuring will take place.

Operation Mato Grosso

On **27 February 2019**, an Implementation Agreement was signed by the Parish of Chacas and Terna Plus S.r.l. for the construction of over 16 km of high-voltage power line at a record altitude of 4,100 metres in the Andes. The new line will connect Peru's national grid with the Huallin hydroelectric plant located 500 km to the north of the capital Lima, significantly increasing the production and transmission of renewable energy for the benefit of both the local community and all the other communities in need that Operation Mato Grosso is designed to help.
For Terna, the Agreement falls within the wider scope of its “business solidarity” projects and voluntary activities already implemented for several years to support the well-being of the populations most in need in areas where it operates. This includes support for voluntary and non-profit organisations through charitable and social initiatives, again in the context of environmental sustainability.

Snam and Terna: research and innovation partnership and electricity-gas convergence

On **1 March 2019**, Snam and Terna signed a memorandum of understanding with the aim of defining and implementing joint initiatives, in particular regarding research, development and innovation and the potential for convergence between the electricity and gas systems.
The areas of activity covered by the agreement include the development of shared national and European energy scenarios with the aim of exploiting convergence between the gas and electricity systems, as part of Snam's plan for converting its compression and storage plants into “dual energy” gas-electric plants with significant benefits in terms of increased flexibility of the services rendered and reduction of environmental impact.
In addition, research and development initiatives will have great importance, with particular reference to the use of programmable renewable sources for electricity generation and to the new coupling sector technologies, aimed at ever-better use of resources, as well as the testing and development of innovative technological solutions for the analysis and monitoring of infrastructure, hydrogeological analysis, the monitoring of worksites and joint optimisation of the electricity and gas networks.

Restructuring of the electricity grid between Catanzaro and Calusia

On **4 March 2019**, Terna arranged 3 meetings open to residents in the province of Catanzaro and Crotone, during which the Company will provide information on the planned construction of a new 150kV power line in the local area. The project will involve the municipalities of Catanzaro, Soveria Simeri, Simeri Crichi, Zagarise, Sellia Marina, Belcastro, Andali, Cerva, Petronà, Sersale Cropani, Mesoraca, Cotronei, Petilia Policastro and Caccuri. The work aims to guarantee the increased stability and reliability of the local electricity system, to improve the quality of the service and the efficiency of the grid and to encourage increased production from renewables.
The 150kV power line, to be installed between the Catanzaro and Calusia Electrical Substations, with connections to the Belcastro substation and the primary transformer room at Mesoraca, will enable the demolition of around 90 km of overhead power lines.

New composition of Board committees

On **21 March 2019**, the Board of Directors modified the composition of the Company's Board committees, in order to ensure continued compliance with the recommendations in the Corporate Governance Code and remain in line with best governance practices. Gabriella Porcelli has taken on the chair of the Nominations Committee, whose other members continue to be Fabio Corsico and Yunpeng He. The Audit, Risk, Corporate Governance and Sustainability Committee, which continues to be chaired by Luca Dal Fabbro since his appointment on 9 November 2018, will continue to include Paola Giannotti and Elena Vasco. The latter has also been appointed a member of the Remuneration Committee, whose other members continue to be Fabio Corsico (as Chair) and Gabriella Porcelli. Finally, Paola Giannotti has been appointed Chair of the Related Party Transactions Committee, of which Luca Dal Fabbro and Gabriella Porcelli continue to be members.

Green bond launch

On **3 April 2019** TERNA S.p.A. launched a green bond addressed to institutional investors. The issuance is made under Terna's Euro 8,000,000,000 Medium Term Notes Programme (EMTN), which has been rated "BBB+" by Standard & Poor's, "(P)Baa2" by Moody's and "BBB+" by Fitch for an aggregate amount of 500 million Euro. The green bond has been issued with a tenor of 7 years and a maturity date falling on 10 April 2026, will pay a coupon of 1.000%, with an issue price equal to 99.886%, a spread of 78 basis points over the midswap and an indicative spread of approximately 100 basis points lower than the Italian BTP having same maturity. The actual cost for Terna, in respect of such issuance, is therefore equal to 1.02% as opposed to the aggregate average cost of the consolidated debt equal to 1.6% over the new Strategic Plan period.
The net proceeds from the issuance will be used to finance the company's eligible green projects of the Company.

Disclosure

pursuant to art. 149-*duodecies* of the CONSOB Regulations for Issuers

The following table, prepared pursuant to art. 149-*duodecies* of the CONSOB Regulations for Issuers, shows the fees paid for audit and other services provided by Terna S.p.A.'s independent auditors in 2018.

(€)

	ENTITY PROVIDING SERVICE	FEES DUE FOR THE YEAR
Audit of the accounts	PwC	356,001
Attestation and other services	PwC	160,613
TOTAL		**516,614**

Attestation

of the separate financial statements pursuant to art. 81-*ter* of CONSOB Regulation 11971 of 14 May 1999, as amended

Terna
TERNA GROUP

"Terna S.p.A."

1. The undersigned, Luigi Ferraris, as Chief Executive Officer, and Agostino Scornajenchi, as Manager responsible for Terna S.p.A.'s financial reporting, having also taken account of the provisions of art.154-*bis*, paragraphs 3 and 4 of Legislative Decree 58 of 24 February 1998, attest to:
   - the adequacy with regard to the nature of the Company, and
   - the effective application of the administrative and accounting procedures adopted in preparation of the separate financial statements during the year ended 31 December 2018.

2. The administrative and accounting procedures adopted in preparation of the separate financial statements for the year ended 31 December 2018 were drawn up, and their adequacy assessed, on the basis of the regulations and methods adopted by Terna S.p.A. in accordance with the Internal Control-Integrated Framework model issued by the Committee of Sponsoring Organizations of the Treadway Commission. This Commission has established a body of general principles providing a standard for internal control and risk management systems that is generally accepted at international level.

3. We also attest that:
   3.1 the separate financial statements for the year ended 31 December 2018:
      a. have been prepared in compliance with the International Financial Reporting Standards endorsed by the European Union through EC Regulation 1606/2002, issued by the European Parliament and by the Council on 19 July 2002 and the statutory requirements implementing the provisions of art. 9 of Legislative Decree 38/2005;
      b. are consistent with the underlying accounting books and records;
      c. provide a true and fair view of the financial position and results of operations of the issuer.

   3.2 the Directors' report on operations includes a reliable analysis of the operating and financial performance and situation of the issuer, as well as a description of the main risks and uncertainties to which it is exposed.

Rome, 21 March 2019

Chief Executive Officer	Manager responsible for financial reporting
Luigi Ferraris	**Agostino Scornajenchi**
(original signed)	*(original signed)*

Report
of the Board of Statutory Auditors to the Annual General Meeting of Terna S.p.A.’s shareholders

Board of Statutory Auditors' Report to the Annual General Meeting of Terna S.p.A.'s shareholders pursuant to article 153 Legislative Decree 58 of 24 February 1998 (the Consolidated Law on Finance) and article 2429, paragraph three of the Italian Civil Code

Dear Shareholders,

During the year ended 31 December 2018, the Board of Statutory Auditors di Terna S.p.A. (also the "Company") fulfilled its statutory duties in accordance with the law, complying with the code of conduct for the Statutory Auditors of listed companies issued by the Italian Accounting Profession (*Consiglio Nazionale dei Dottori Commercialisti e degli Esperti Contabili*), the recommendations of the CONSOB (the *Commisione Nazionale per le Società e la Borsa*, Italy's Securities and Exchange Commission) regarding corporate controls and the activities of the Board of Statutory Auditors and the guidelines in the Corporate Governance Code published by Borsa Italiana (the "Corporate Governance Code").

Responsibility for the statutory audit required by Legislative Decree 39 of 27 January 2010 (Legislative Decree 39/2010) has been assigned to the independent auditors, PricewaterhouseCoopers S.p.A., appointed by the Annual General Meeting of 13 May 2011 for nine years from 2011 to 2019.

The Board, which also took into account the indications contained in CONSOB announcement DEM/1025564 of 6 April 2001, as amended, reports the following.

- We verified compliance with the law and the By-laws.
- We attended the meetings of the Board of Directors and specific preparatory meetings regarding the agenda items, as well as meetings of the Audit and Risk, Corporate Governance and Sustainability Committee. We periodically obtained information from the Directors on the overall operating performance, the outlook for the Company and on the most significant transactions, in terms of their impact on the results of operations and financial position, carried out by the Company, satisfying ourselves

that the decisions taken and implemented were compliant with the law and the By-laws and were not manifestly imprudent, risky or in potential conflict of interest or in contrast with resolutions approved by General Meeting, or such as to compromise the value of the Company. In the course of our activities, we found no evidence of transactions of an atypical and/or unusual nature. In carrying out our duties, we analysed information flows from the various departments and also conducted interviews with the Company's senior management, with the independent auditors and with the oversight bodies of subsidiaries.

- At the meetings of 20 and 21 March 2019, the Board of Directors, on the recommendation of the Remuneration Committee, approved the "Annual Remuneration Report", prepared in accordance with article 123-ter of the Consolidated Law on Finance and in compliance with the provisions of article 6 of the Corporate Governance Code.
- We monitored compliance with and effective application of the "Procedure for Related Party Transactions", recently revised by the Board of Directors on 15 December 2016 and compliant with article 4 of the CONSOB Regulation referred to in Resolution 17221 of 12 March 2010, as amended.
- The Company has prepared the financial statements for the year ended 31 December 2018 in compliance with International Financial Reporting Standards (IFRS). These financial statements were audited by PricewaterhouseCoopers S.p.A., which issued its report on 11 April 2019 without any qualification or emphasis of matter. The financial statements, together with the Directors' report on operations, was made available to us within the deadline required by law and we have no particular comments in this regard.

- The Company also prepared the consolidated financial statements for the year ended 31 December 2018 in compliance with International Financial Reporting Standards (IFRS). These financial statements were also audited by PricewaterhouseCoopers S.p.A., which issued its report on 11 April 2019 without any qualification or emphasis of matter.
- Among the most significant transactions carried out in 2018, we note the following, referring you to the report on operations for more detailed information:
  - the issue of green bonds with a five-year term and a value of €750 million at a rate of 1% as part of the Company's €8 billion Euro Medium Term Notes (EMTN) programme;
  - the arrangement of a five-year revolving credit facility of €1,150 million at a rate of EURIBOR plus a variable spread of between 0.60% and 1.45% based on Terna's credit rating (at the same time, the Company cancelled a €750 million line of credit expiring on 11 December 2019).
- We oversaw, within the scope of our responsibilities, the adequacy of the Company's organisational structure, compliance with the principles of good governance and the adequacy of the instructions issued by the Company to its subsidiaries pursuant to article 114, paragraph 2 of the Consolidated Law on Finance, by obtaining information from the heads of the relevant departments, through meetings with the independent auditors and with the oversight bodies of the most important subsidiaries in terms of size. With regard to the provisions of article 15, paragraph one of the Markets Regulation adopted by CONSOB Resolution 20249 of 28 December 2017, the Company's non-EU subsidiaries are not of material importance as defined by the articles in Chapter II, Section VI, Part III of the Regulations for Issuers adopted by CONSOB Resolution 11971 of 14 May 1999, as amended.

- We monitored the adequacy of the administrative and accounting system, assessing its reliability in providing a true and fair view of operations; this activity was carried out by obtaining information from the heads of the various departments, by examining company documents and analysing the results of the work carried out by the independent auditors. The Chief Executive Officer and the Manager responsible for the Company's financial reporting have, with in reports attached to the financial statements for 2018, attested to: a) the adequacy and effective application of accounting and administrative procedures; b) the compliance of the financial reports with international financial reporting standards; c) the consistency of the documents with the underlying accounting books and records and their ability to provide a true and fair view of the financial position and results of operations of the Company. A similar attestation is attached to the Terna Group's consolidated financial statements.
- We assessed and oversaw the adequacy of the internal audit system through: a) examination of the report prepared by the Head of Internal Audit on the internal audit system; b) examination of the Internal Audit reports, as well as information on the results of monitoring; c) meetings with the oversight bodies of the most important subsidiaries pursuant to the first and second paragraphs of article 151 of the Consolidated Law on Finance; d) participation in the meetings of the Audit and Risk, Corporate Governance and Sustainability Committee and acquisition of the relevant documents; e) meetings with the Manager responsible for financial reporting and the Chief Risk Officer. Attending the Audit and Risk, Corporate Governance and Sustainability Committee meetings allowed the Board of Statutory Auditors to coordinate its activities with those of this Committee in performing our functions as the "Internal Audit and Accounting Committee", assigned to us on the basis of article 19 of Legislative Decree 39/2010 and, in particular, to oversee: a) the financial reporting process; b) the effectiveness of the internal quality control, risk management and internal audit systems; c) the statutory audit of the accounts; and d) matters relating to the independence of the audit firm.

On the basis of the activities carried out and considering the evolving nature of the Internal Audit System, in the view of the Board of Statutory Auditors the system is adequate overall and we have no observations to report to shareholders.

The independent auditors have notified their overall fees for auditing Terna S.p.A.'s separate and consolidated financial statements for the year ended 31 December 2018, and for their review of the half-year report, assessment of the regular nature of accounting systems, and for the other tasks assigned to them; the fees for these other tasks (inclusive of expenses) amount to €300,983, as follows:

– audit of the unbundling for ARERA	35,200
– audit of the reporting packages	17,600
– opinion on payment of the interim dividend	35,200
– assurance of the sustainability report/non-financial statement	87,570
– issue of the EMTN comfort letter and other documents	121,525
– other tasks	3,888

Moreover, the independent auditors have notified us that, based on the best information available, and taking into account the regulatory and statutory requirements for auditors, it has, in the period in question, maintained a position of independence and objectivity towards Terna S.p.A. and that there have been no changes regarding the absence of any form of incompatibility with reference to the situations and persons provided for in article 17 of Legislative Decree 39/2010 and the articles referred to in Chapter I-*bis* of Section VI of the Regulations for Issuers.

- We held periodic meetings with representatives of the independent auditors pursuant to article 150, paragraph 3 of the Consolidated Law on Finance, and there are no matters worthy of mention in this Report. We also note that on 11 April 2019 the independent auditors issued its report pursuant to the third paragraph of article 19 of Legislative Decree 39/2010, and the additional report required by article 11 of the European Regulation (EU) 537/2014, in which the auditors do not report on significant issues or shortcomings relating to the system of internal controls over financial reporting and which we have submitted to the Board of Directors without observation.
- On 11 April 2019, the independent auditors issued their report on the consolidated non-financial statement prepared pursuant to article 3, paragraph ten of Legislative Decree 254 of 30 December 2016 and article 5 of CONSOB Regulation adopted with Resolution 20267 of 18 January 2018, which states that no matters have been brought to the attention of the independent auditors that would cause them to conclude that the Terna Group's consolidated non-financial statement for the year ended 31 December 2018 has not been prepared, in all material aspects, in compliance with the requirements of articles 3 and 4 of the above decree and the Global Reporting Initiative Standards (GRI Standards).
- The Terna Group's consolidated non-financial statement constitutes a separate report with respect to the Directors' report on operations, as permitted by article 5, paragraph three of the above decree.

- We monitored the procedures adopted to ensure effective implementation of the Corporate Governance Code adopted by the Company, as set forth in the Report on Corporate Governance and Ownership Structures approved by the Board of Directors on 20 and 21 March 2019. With reference to the recommendations falling within the purview of the Board of Statutory Auditors, we state that:
  - we have verified the correct application of the criteria and procedures for assessing independence, adopted by the Board of Directors;
  - with regard to the self-assessment of the independence requirements for members of the Board of Statutory Auditors, we have verified their existence during our meeting of 1 March 2019, in keeping with the procedures adopted by the Directors;
  - we have complied with the provisions of the regulation governing the management and handling of confidential and privileged company information.

  Finally, it should be noted that the independent auditors have expressed its opinion regarding the consistency of the information provided, in accordance with paragraph 4 of article 123-*bis* of the Consolidated Law on Finance, in the Report on Corporate Governance and Ownership Structures with the separate and consolidated financial statements.

- With reference to Legislative Decree 231 of 8 June 2001, the Company has, for some time, adopted an organisational and management model, which is regularly revised and which is compliant with best practices. Similar models have been adopted by the subsidiaries. During the year, the Board of Statutory Auditors regularly exchanged information with members of the Supervisory Board. The information gathered did not reveal any critical issues with respect to the proper implementation of the organizational model, requiring mention in this report.

- We have not received any complaints pursuant to article 2408 of the Italian Civil Code, nor are we aware of any events or petitions requiring mention during the Annual General Meeting.
- We have verified compliance with the laws regarding the preparation of separate and consolidated financial statements and the report on operations, directly and with the collaboration of the heads of departments and through information obtained from the independent auditors, and we have nothing significant to report.
- We expressed the opinion required from the Board of Statutory Auditors by the third paragraph of article 2389 of the Italian Civil Code (the remuneration of executive Directors).
- The independent auditors issued the opinion referred to in paragraph 5 of article 2433-*bis* of the Italian Civil Code (the interim dividend).
- The members of the Board of Statutory Auditors have complied with the obligation to notify directorships and appointments as statutory auditors in Italian companies within the deadlines and according to the procedures provided for in article 148-*bis* of the Consolidated Law on Finance and the articles in Chapter II, Section V-*bis*, Part III of the Regulations for Issuers.
- During 2018, the Board of Statutory Auditors met seven times, attended the ten meetings of the Board of Directors, the seven meetings of the Audit and Risk, Corporate Governance and Sustainability Committee and the Annual General Meeting of shareholders held on 4 May 2018.

On the basis of our activities and the information obtained, the Board of Statutory Auditors is not aware of any omissions, shortcomings, irregularities or any other circumstances that require reporting to the supervisory authorities or mention in this report.

Having reviewed the financial statements for the year ended 31 December 2018, the Board of Statutory Auditors has no objections to raise as regards the proposed resolutions submitted by the Board of Directors.

Rome, 11 April 2019

For the Board of Statutory Auditors
The Chairman
Riccardo Schioppo

Independent auditor's report

in accordance with article 14 of Legislative Decree 39 of 27 January 2010 and article 10 of Regulation (EU) 537/2014

Independent auditor's report

in accordance with article 14 of Legislative Decree 39 of 27 January 2010 and article 10 of Regulation (EU) 537/2014

To the shareholders of Terna SpA

Report on the Audit of the Separate Financial Statements

Opinion

We have audited the separate financial statements of Terna SpA (the Company), which comprise the statement of financial position as of 31 December 2018, the income statement, the statement of comprehensive income, the statement of changes in equity, the statement of cash flows for the year then ended and notes to the separate financial statements, including a summary of significant accounting policies.

In our opinion, the separate financial statements give a true and fair view of the financial position of the Company as of 31 December 2018, and of the result of its operations and cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union, and with the regulations issued to implement article 9 of Legislative Decree 38/05.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISA Italia). Our responsibilities under those standards are further described in section Auditor's Responsibilities for the Audit of the Separate Financial Statements of this report. We are independent of the Company pursuant to the regulations and standards on ethics and independence applicable to audits of financial statements under Italian law. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the separate financial statements of the current period. These matters were addressed in the context of our audit of the separate financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key Audit Matters	*Auditing procedures performed in response to key audit matters*
Capital expenditure for the development and operation of the transmission grid *Section D – Notes to the statement of financial position – Note 10 Property, plant and equipment and Note 12 Intangible assets* Costs capitalised during the year as property, plant and equipment and intangible assets amount to Euro 886 million and mainly relate to capital expenditure for the development and operation of the transmission grid. Revenue from transmission and dispatching activities (regulated activities) is determined each year in accordance with the approved regulatory tariffs which are based on a pre-established return on capital invested, plus amortisation and depreciation and operating costs recognised. The capitalisation of costs for the operation and development of the transmission grid therefore represented a key matter in the audit of the separate financial statements, also considering the magnitude and the high number of transactions.	We performed an understanding and evaluation of the system of internal control over the capital expenditure cycle, with particular reference to identification of the key controls and the verification of their effectiveness. We assessed that the capitalisation of costs complied with the international accounting standards. We also performed substantive procedures analysing, on a sample basis, the supporting documentation of capitalised costs in order to verify that these costs were accurate, complete and pertaining to the reporting period. Our tests also included the analysis of the notes to the separate financial statements to verify the adequacy and completeness of the disclosures therein.

Key Audit Matters	*Auditing procedures performed in response to key audit matters*
Derivative financial instruments	
Section D – Notes to the statement of financial position – Note 21 Borrowings and financial liabilities and Section E – Commitments and risks	
The amount of borrowings in the separate financial statements at 31 December 2018 is Euro 9,402 million. In accordance with the risk management policies, the group mitigates its exposure to the change in interest rates by entering into derivative financial instruments for hedging purposes. The notional amount of derivatives at 31 December 2018 is Euro 3,226 million. Considering the magnitude of values, the degree of complexity of both the fair value measurement process and the recognition rules provided for by the new IFRS 9 "Financial Instruments", the verification of derivative financial instruments was considered as key matter in the audit of the separate financial statements.	We performed an understanding and evaluation of the system of internal control over the measurement process of the derivative financial instruments and related accounting treatment. We recalculated, on a sample basis and involving the experts of the PwC network, the fair value of derivatives and we verified the hedge effectiveness in accordance with the provisions of IFRS 9 and with the corporate procedures. Our tests also included the analysis of the notes to the separate financial statements to verify the adequacy and completeness of the disclosures therein.

Responsibilities of the Directors and the Board of Statutory Auditors for the Separate Financial Statements

The directors are responsible for the preparation of separate financial statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the European Union, and with the regulations issued to implement article 9 of Legislative Decree 38/05 and, in the terms prescribed by law, for such internal control as they determine is necessary to enable the preparation of separate financial statements that are free from material misstatement, whether due to fraud or error.

The directors are responsible for assessing the Company ability to continue as a going concern and, in preparing the separate financial statements, for the appropriate application of the going concern basis of accounting, and for disclosing matters related to going concern. In preparing the separate financial statements, the directors use the going concern basis of accounting unless they either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

The board of statutory auditors is responsible for overseeing, in the terms prescribed by law, the Company's financial reporting process.

Auditor's Responsibilities for the Audit of the Separate Financial Statements

Our objectives are to obtain reasonable assurance about whether the separate financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with International Standards on Auditing (ISA Italia) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the separate financial statements.

As part of an audit conducted in accordance with International Standards on Auditing (ISA Italia), we exercised our professional judgment and maintain professional scepticism throughout the audit. Furthermore:

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

We communicated with those charged with governance, identified at an appropriate level as required by ISA Italia regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identified during our audit.

We also provided those charged with governance with a statement that we complied with the regulations and standards on ethics and independence applicable under Italian law and communicated with them all relationships and other matters that may reasonably be thought to bear on our independence and, where applicable, related safeguards.

From the matters communicated with those charged with governance, we determined those matters that are of most significance in the audit of the separate financial statements of the current period and are therefore the key audit matters. We described these matters in our auditor's report.

Additional Disclosures required by article 10 of Regulation (EU) 537/2014

We were appointed by the shareholders of Terna SpA at the general meeting held on 13 May 2011 to perform the audit of the Company separate and consolidated financial statements for the years ending 31 December 2011 through 31 December 2019.

We declare that we did not provide any prohibited non-audit services referred to in article 5, paragraph 1, of Regulation (EU) 537/2014 and that we remained independent of the Company in conducting the audit.

We confirm that the opinion on the separate financial statements expressed in this report is consistent with the additional report to the board of statutory auditors, in its capacity as audit committee, prepared pursuant to article 11 of the aforementioned Regulation.

Report on Compliance with other Laws and Regulations

Opinion in accordance with article 14, paragraph 2, letter e), of Legislative Decree 39/2010 and article 123-bis, paragraph 4, of Legislative Decree 58/1998

The directors of Terna SpA are responsible for preparing a report on operations and a report on the corporate governance and ownership structure of Terna SpA as of 31 December 2018, including their consistency with the relevant separate financial statements and their compliance with the law.

We have performed the procedures required under auditing standard (SA Italia) 720B in order to express an opinion on the consistency of the report on operations and of the specific information included in the report on corporate governance and ownership structure referred to in article 123-bis, paragraph 4, of Legislative Decree 58/1998, with the separate financial statements of the Company as of 31 December 2018 and on their compliance with the law, as well as to issue a statement on material misstatements, if any.

In our opinion, the report on operations and the specific information included in the report on corporate governance and ownership structure mentioned above are consistent with the separate financial statements of the Company as of 31 December 2018 and are prepared in compliance with the law.

With reference to the statement referred to in article 14, paragraph 2, letter e), of Legislative Decree 39/2010, issued on the basis of our knowledge and understanding of the Company obtained in the course of the audit, we have nothing to report.

Rome, 11 April 2019

PricewaterhouseCoopers SpA

Signed by

Luca Bonvino
(Partner)

This report has been translated from the original version which was issued in Italian language, solely for the convenience of international readers.

Annual Report
Integrated Report

Sustainability Report
Non-Financial Statement

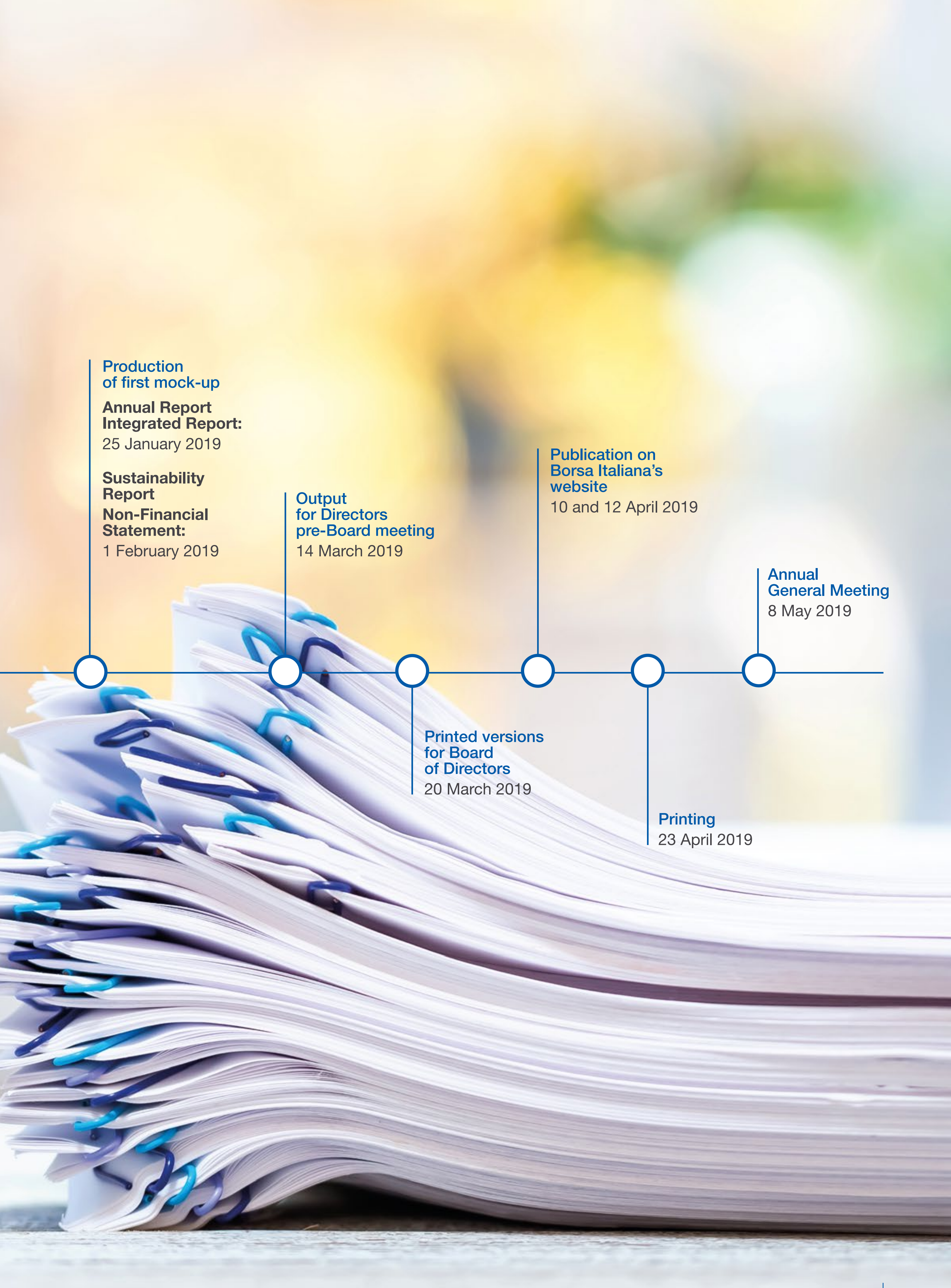
REPORTING PROCESS 2018

The purpose of the reports is to provide Terna's internal and external stakeholders with an understanding and overview of the Company and its businesses and operations.

They are the end result of a series of deliberate choices in terms of transparency, communication, accuracy, completeness and the linking of disclosures, and mark the culmination of a sequence of complex processes involving a large number of people from across the Company.

Report on Corporate Governance and Ownership Structures

Annual Remuneration Report



Production of first mock-up

Annual Report Integrated Report:
25 January 2019

Sustainability Report Non-Financial Statement:
1 February 2019

Output for Directors pre-Board meeting
14 March 2019

Printed versions for Board of Directors
20 March 2019

Publication on Borsa Italiana's website
10 and 12 April 2019

Printing
23 April 2019

Annual General Meeting
8 May 2019

All pictures are property of Terna.

www.terna.it

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