

The introduction to this Sustainability Report, which coincides with the Company's **Non-Financial Statement**, provides essential information on the principles and methodology applied during preparation in accordance with the GRI-Standards and on the scope of the Report. Particular importance is given to the description of the **materiality analysis**, the results of which are shown in the matrix used as the basis for selecting and prioritising the topics covered in the document as a whole. This section also includes two synoptic tables: the first cross-references topics that are significant for Terna and its stakeholders with the potential impacts; the second links the Non-Financial Statement requirements with material topics, the risks generated and incurred and the policies adopted in order to minimise such risks.





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Methodological note

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Introduction

The 2018 Sustainability Report is Terna's fourteenth annual publication focusing on the Group's environmental, social and governance performance. As in the 2017 edition, the Report also has an additional role as the Group's "Non-Financial Statement", thus meeting the non-financial disclosure requirements set out in Legislative Decree 254/2016, as amended.

Reporting is based on the GRI Sustainability Reporting Standards published in October 2016 by the GRI-Global Reporting Initiative, applied in accordance with the "core" option.

In addition to the information that meets the "Non-Financial Statement" requirements, clearly identified in the table on page 16, the Report also contains additional voluntary disclosures in line with a general principle of maximum transparency.

As in previous years, the Report was approved by Terna S.p.A.'s Board of Directors and has undergone specific audit procedures.

The independent limited assurance report on the Non-Financial Statement, prepared by PricewaterhouseCoopers, is included on page 210.

The observation period is 2018 and all data refer to the year ended 31 December 2018. Significant events occurring up to 1 March 2019 are also included, with the sole exception being the changes to corporate governance on 20 March 2019.

Finally, any changes to the data published in previous editions are suitably indicated in the document.

Structure of the Report

The 2018 Sustainability Report has been partially reorganised in terms of the order of the various sections: the initial section, “Profile”, containing all the information on the organisational and ownership structure, the business model and the Group’s activities, is followed by the section on “Responsible business management”, focusing on the elements that constitute the Group’s approach to sustainability, including its commitment to stakeholder engagement.

The central section, “The electricity service and innovation”, deals with the various aspects of Terna’s core business - the transmission and dispatching of electricity - and putting them within the context of the relevant SDGs, namely 7 (“Affordable and clean energy”), 9 (“Industry, innovation and infrastructure”) and 13 (“Climate action”). The Report continues with two sections on “People” and “Environment”.

As usual, in order to aid the reader, information corresponding to specific GRI indicators is denoted by the respective abbreviation in the margins of the text in the relevant passages (an indicator’s abbreviation is placed next to the paragraph heading if the entire text is deemed relevant).

The focus on the subsidiary, Tamini Group, which operates in sectors different from those in which the rest of the Terna Group operates, reports on the results of the materiality analysis carried out at the beginning of 2019, and on the most significant environmental and social data (page 194).

The Report concludes with the “GRI Content Index”, followed by a table linking the GRI indicators with the ten Global Compact principles.

The following are also attached to the report:

- the “Green Bond Report 2018”, a document enabling Terna to comply with the commitment given, when issuing its green bond in July 2018, to report annually on the use made of the related proceeds and the environmental benefits resulting from the projects financed with those proceeds;
- a section that does not fall within the scope of the “Non-Financial Statement”, consisting of “Key indicator tables”, which reproduce the published GRI indicators, supplemented with additional ones.

Materiality

Regarding the selection of non-financial content to be disclosed, Legislative Decree 254/2016 provides for coverage of *“environmental, social, and personnel-related matters, respect for human rights, and the fight against active and passive corruption, which are deemed relevant taking into account a company’s activities and characteristics”*. Such matters should be reported *“insofar as is necessary to ensure understanding of a company’s activities, performance, results and impacts”*, thereby introducing a materiality criterion into the process of determining the topics to be reported and the extent to which they should be dealt with.

The Decree specifies that information should be provided *“in accordance with the methods and principles laid down by the reporting standard used”*. Having decided to adopt the GRI-Standards as a reference, Terna opted to follow the recommendations of the GRI 101 - Foundation standard, which contains the basic guiding principles regarding content definition and the quality of reporting. According to this standard, the *“material”* topics to be potentially included in reporting are those that reflect the significant impacts (positive and negative) of an organisation in the economic, environmental and social spheres, and which influence stakeholders’ decisions.

The choice of topics on which this Report is based reflects the updated materiality analysis conducted in 2016, which led to a complete revision of the topic tree compared with the previous version of 2013.

In updating the **significance for Terna** aspect, 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 contributors to the update of the internal survey of the 23 topics that make up the topic tree. This was conducted last year and involved the second-level heads of department. The results were then validated by senior management.

With regard to the **significance for stakeholder** aspect, understood to mean the degree to which a topic might influence decision-making, a number of documentary sources revealing stakeholders’ perception of significance were taken into account. These break down as follows:

- direct engagement, namely the outcomes of initiatives carried out directly by Terna and aimed at its stakeholders in order to understand their perception of significance with regard to topics (for example, for staff, local communities and the customers of the Non-regulated Activities);
- general sources, namely standards, publications, position papers, assessment tools and products produced by stakeholders that reflect their perception of significance in relation to topics.

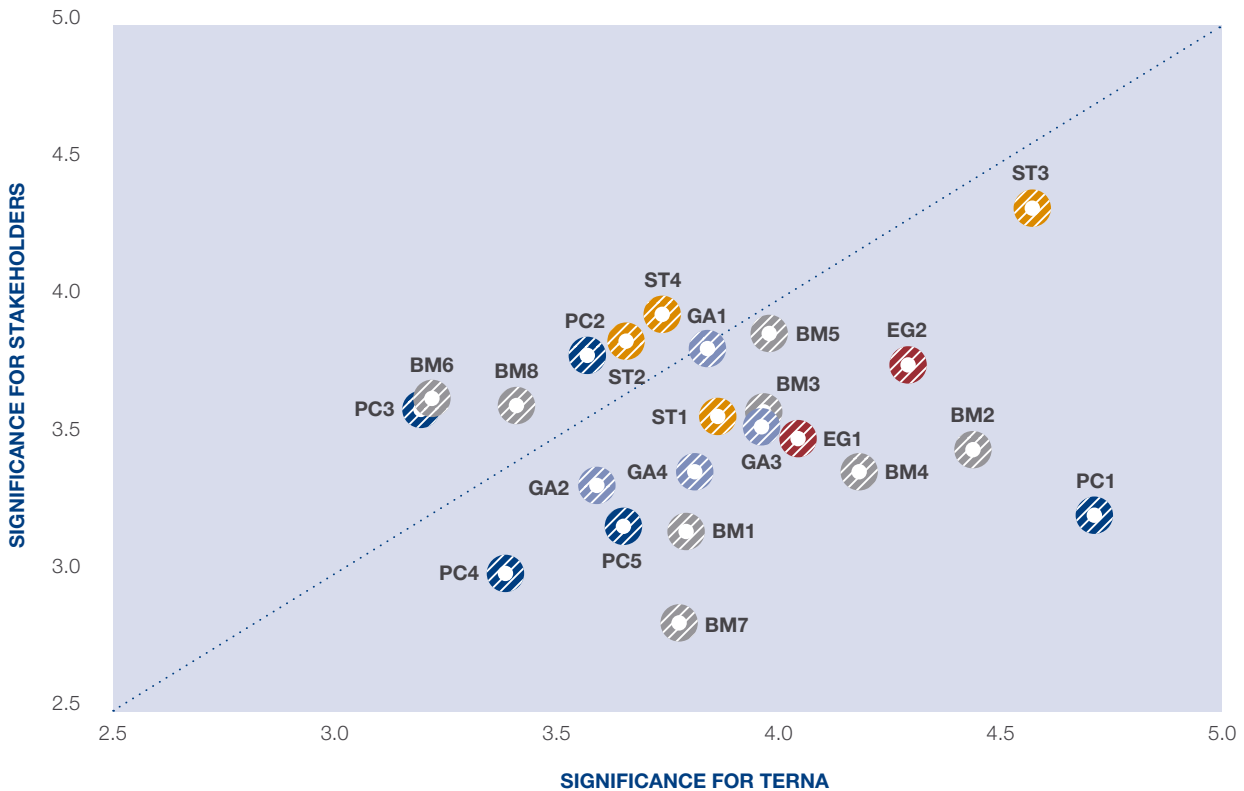
The score that summarises the significance of a topic for the majority of stakeholders was obtained by combining the assessments relating to each stakeholder category with the weighting of this category in terms of influence and mutual dependence in their relationship with the Group.

The summary of the points of view of the Company and stakeholders is expressed in the **Materiality Matrix**, which enables the identification of *“material”* topics, namely those that are most significant for Terna and stakeholders. It also highlights any differences between the viewpoints of stakeholders and of the Company on each topic. In the matrix, the most significant topics are those furthest away from the origin; the most important topics in absolute terms are the ones furthest from the origin and, at the same time, closer to the bisector.

Terna’s Sustainability Report has always aimed to provide transparent and full disclosure. The same approach has also been adopted in this document, which serves to meet the requirements of Legislative Decree 254/16. However, given the emphasis placed by the standard on materiality, it should be pointed out that some of the topics shown in the matrix are not among those that are strictly necessary *“to ensure understanding of a company’s activities, performance, results and impact”*. This regards in particular: business development

and diversification; the promotion of wellbeing within the Company; and the promotion of diversity and equal opportunities. These topics have been identified as falling below a minimum materiality threshold because: 1) by adding up the significance scores for stakeholders and Terna, the total materiality score is less than 7; and 2) the significance for Terna is less than 3.5. These topics - like all the significant ones - are also included in the Sustainability Report, but by virtue of the Company having opted for **voluntary disclosure**, rather due to the regulatory requirements of Legislative Decree 254/2016.

MATERIALITY MATRIX



Ethics and governance model

EG1: Alignment with best governance practices

EG2: Business integrity



Transmission service

ST1: Sustainable NTG planning

ST2: Electricity market integration

ST3: Quality, security and service continuity

ST4: Reduction in cost of service



Management of environmental impacts

GA1: Mitigation of visual impact

GA2: Protection of biodiversity

GA3: Management of electromagnetic fields

GA4: Reduction of environmental footprint



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: Sustainable supply chain management

BM8: Innovation and research



People and community

PC1: Health and safety

PC2: HR development

PC3: Promotion of wellbeing

PC4: Promoting diversity and equal opportunities

PC5: Social responsibility and impact on local communities

Risks and impacts

The significance of the various topics for Terna and its stakeholders is based on the impacts, both positive and negative, that are connected to them. In line with the requirement in Legislative Decree 254/2016 to explain “the main risks, generated or incurred, in connection with” the significant topics in terms of materiality, for each of the topics identified, the table below shows an example of the risk involved and the type of impact for Terna and for the specific categories of stakeholder affected. In the classification of impacts for Terna, the categories used in the Company’s application of the Enterprise Risk Management model have been adopted, whilst the impacts for stakeholders are broken down into:

- Service quality
- Economic
- Health and safety
- Human rights
- Quality of life, wellbeing

TOPIC	EXAMPLE OF RISK MANIFESTATION	POTENTIAL IMPACT ON TERNA	STAKEHOLDERS POTENTIALLY IMPACTED	POTENTIAL IMPACT ON STAKEHOLDERS
Quality, security and electricity service continuity	Increase in malfunctions, grid inadequacy	- Strategic/operational - Reputational - Economic/financial	Community	<i>Service quality, economic</i>
Compliance with economic and financial objectives	Economic and financial performance below expectations	- Strategic/operational - Economic/financial	Shareholders, Lenders, Suppliers, Business partners, Personnel, Community	<i>Economic</i>
Business integrity	Behaviours in breach of statutory requirements	- Compliance - Reputational - Economic/financial	Shareholders / Other stakeholders who are damaged by Terna’s conduct	<i>Shareholders: economic Other stakeholders: human rights, health and safety, economic</i>
Alignment with best governance practices	Below par governance	- Strategic/operational - Reputational	Shareholders, Lenders, Suppliers, Business partners, Personnel	<i>Economic (indirect)</i>
Reduction of electricity service costs	Increase in service costs (due to Terna)	- Reputational - Economic/financial in medium term - Strategic/operational	Community	<i>Economic</i>
Mitigation of visual, landscape and acoustic impacts	Insufficient consideration given to reducing visual impact	- Reputational	Local communities affected by the presence of Terna’s infrastructure	<i>Quality of life, wellbeing</i>

TOPIC	EXAMPLE OF RISK MANIFESTATION	POTENTIAL IMPACT ON TERNA	STAKEHOLDERS POTENTIALLY IMPACTED	POTENTIAL IMPACT ON STAKEHOLDERS
Optimal management of engagement with local stakeholders	Tensions with local communities affected by grid development	<ul style="list-style-type: none"> - Reputational - Economic/financial - Strategic/operational 	Local communities	Quality of life, wellbeing
Workers' health and safety and correct working practices	Occupational injuries	<ul style="list-style-type: none"> - Reputational - Economic/financial - Compliance 	Personnel, Suppliers	Health and safety, human rights
Selective investment and on-time delivery	Failure to deliver infrastructure construction projects to budget and on time	<ul style="list-style-type: none"> - Economic/financial - Reputational - Strategic/operational 	Shareholders, Community	Shareholders: Economic The Community: Service quality
Integration of electricity markets	Slowdown in European integration and interconnections	<ul style="list-style-type: none"> - Economic/financial - Reputational - Compliance 	Community, Electricity sector operators	Community: Service quality (security of supply); economic (service costs) Operators: economic
Prudent risk management	Lack of risk management preparedness	<ul style="list-style-type: none"> - Economic/financial - Reputational - Strategic/operational 	All (regarding the impact of related risks)	Service quality; Health and safety; Human rights; Indirect economic
Sustainable planning of NTG development	Planning with insufficient attention paid to environmental aspects	<ul style="list-style-type: none"> - Reputational - Compliance - Strategic/operational 	Local communities, Environmental organisations	Quality of life, wellbeing
Management and monitoring of electromagnetic fields	Failure to comply with pertinent regulations	<ul style="list-style-type: none"> - Compliance - Reputational - Economic/financial 	Local communities affected by the construction or presence of Terna infrastructure	Health and safety
Development of human resources	Inadequate human capital	<ul style="list-style-type: none"> - Strategic/operational - Economic/financial in medium to long term - Reputational 	Shareholders; Terna's people	The community: Service quality Shareholders and suppliers: Economic in the medium to long term
Reduction of the Group's environmental footprint	Negative environmental externalities	<ul style="list-style-type: none"> - Reputational 	Community	Quality of life, wellbeing
Innovation and Research	Insufficient innovation capacity for the energy transition and business growth	<ul style="list-style-type: none"> - Strategic/operational - Economic/financial in medium to long term - Reputational 	Community, Shareholders, Suppliers	Shareholders: Economic The Community: Service quality
Strategic approach to stakeholder management	Failure to consider stakeholders' expectations	<ul style="list-style-type: none"> - Reputational - Strategic/operational 	All	- Reputational - Strategic/operational
Monitoring of environmental and social aspects of the supply chain	Suppliers' behaviour not in line with Terna's sustainability policies	<ul style="list-style-type: none"> - Reputational - Economic/financial 	Suppliers	Human rights; Health and safety

The following table links the Legislative Decree 254/2016 ("Non-Financial Statement") topics to the topics deemed to be material during Terna's materiality analysis and by the adopted reporting standard. In line with the changes to the above Legislative Decree 254/2016 introduced by Law 145/2018, the following table includes a new column showing exact references to how the Group manages the various risks generated or incurred.

LEGISLATIVE DECREE 254/2016 TOPIC	TERNA MATERIAL TOPIC	RISKS IDENTIFIED	POLICIES ADOPTED AND HOW THE RISKS GENERATED OR INCURRED ARE MANAGED	TOPIC- SPECIFIC STANDARD	TOPIC- SPECIFIC STANDARD	NOTE
Environmental	Mitigation of visual, landscape and acoustic impact	See materiality risks table (page 14).	<p>"Environment" section: Power lines and local communities (km of lines demolished, power lines with reduced visual impact, underground lines, mitigation and natural engineering - pages 169-173); Demolition targets in the Strategic Plan - page 169 Reports and complaints regarding environmental concerns - page 176</p> <p>"Electricity service and innovation" section: Principal construction work carried out and expected benefits (Benefits for the country as a whole and local communities - page 124)</p>	304; 413	304-1; 413-2; EU13	
	Management and monitoring of electromagnetic fields	See materiality risks table (page 15).	<p>"Responsible business management" section: Compliance with legislation - page 70 55001 certification - page 61</p> <p>"Electricity service and innovation" section: Asset management (Inspection of lines - page 133)</p> <p>"Environment" section: Monitoring and supervision of electromagnetic fields - page 176 Reports and complaints regarding environmental concerns - page 176</p>	n/a	n/a a qualitative description of the actions taken is provided	
	Reduction of the Group's environmental footprint	See materiality risks table (page 15).	<p>"Electricity service and innovation" section: 2019 Development Plan (Reduction of CO₂ emissions in the electricity system; Cuts in CO₂ emissions in 2018; Progress in implementing previous Development Plans - pages 119-125)</p> <p>"Environment" section: Direct and indirect CO₂ emissions (Containment of direct emissions: SF₆, SF₆ leakage containment targets in Strategic Plan - pages 181-184) Energy management system, energy efficiency in substations and offices - pages 186-187, Other indirect CO₂ emissions (Grid losses; LCA studies on power lines - pages 188-189)</p>	305; 201 301; 302	305-1; 305-2 305-4; 201-2 301-1; 302-1 302-3	

LEGISLATIVE DECREE 254/2016 TOPIC	TERNA MATERIAL TOPIC	RISKS IDENTIFIED	POLICIES ADOPTED AND HOW THE RISKS GENERATED OR INCURRED ARE MANAGED	TOPIC-SPECIFIC STANDARD	TOPIC-SPECIFIC STANDARD	NOTE
Social	Quality, security and service continuity	See materiality risks table (page 14).	"Profile" section: Electricity transmission (pages 36-38) Dispatching of electricity (pages 40-42) "Responsible business management" section: Opportunities and risks connected with climate change - pages 68-69 "The Electricity service and innovation" section: Continuity and quality of service - pages 114-115 Grid development; Development Plan - pages 119-120; Progress in implementing previous Development Plans- principal works carried out - pages 122-123; Connecting new plants - pages 126-127; Overseas interconnections - pages 128-131; Asset Management - pages 132-137; Innovation (factories - pages 139-141)	203	203-1; EU28; EU29	
	Optimal management of engagement with local stakeholders	See materiality risks table (page 15).	"Responsible business management" section: Sustainability objectives and targets - page 62; Local stakeholders (Local stakeholders z, Sustainability objectives and targets - page 62; landowners affected by NTG development; Dialogue with local communities overseas; Dialogue with local communities: the most difficult cases and shared solutions - pages 84-91) "Environment" section: Planning and consultation - page 170.	413	413-1; 413-2	
	Sustainable planning of NTG development	See materiality risks table (page 15).	"Electricity service and innovation" section: Investment and innovation for the SDGs - pages 116-117 Grid development - page 118 2019 Development Plan - page 119; emissions in the electricity system pages - pag. 120-121; Overseas interconnections - pages 128-131 Innovation (factories - pages 138-141 "Environment" section: Power lines and local communities - page 169-173	413	413-1; 413-2	
Pertaining to personnel	Workers' health and safety and correct working practices	See materiality risks table (page 15).	"Responsible business management" section: Respect for human rights - pages 74-75 "People" section: Protecting employees' safety - pages 160-161; Health and Safety target in Strategic Plan - page 163	403	403-1; 403-2	
	Development of human resources	See materiality risks table (page 15).	"People" section: Development; People for Performance target in Strategic Plan - page 157	401; 404	401-1; 404-1; EU15	
Respect for human rights Fighting corruption	Workers' health and safety and correct working practices/ Monitoring of environmental and social aspects of the supply chain	See materiality risks table (page 15).	"Responsible business management" section: Guaranteeing safety, the environment, and human rights at contractors' construction sites - pages 80-81; Procurement and suppliers - page 76-78; Target for use of ESG criteria in tenders in Strategic Plan - pages 78	406; 407 408; 409 412	406-1; 407-1 408-1; 409-1 412-1	
	Business integrity	See materiality risks table (page 14).	"Responsible business management" section: Prevention of corruption (Anti-corruption, 37001 Certification and Global Compliance programme - pages 71-73	205; 206	205-1; 205-3 206-1	

Scope and indicators

The data and disclosures in the Sustainability Report 2018 refer to the Terna Group, meaning the scope that includes Terna S.p.A. and the companies consolidated on a line-by-line basis in its consolidated financial statements for the year ended 31 December 2018. Tamini Group companies, unless otherwise indicated, are excluded from the scope given that the Tamini Group's activities are not comparable with those of the rest of the Terna Group. Data for the Tamini Group are not consistent with the data for the Terna Group and the two sets of data cannot be aggregated, as this would not fully represent the specific nature of Tamini itself and assessment of the performance of the rest of the Group would be influenced by elements that would not permit a clear and realistic reading of the data. The Tamini Group's environmental and social indicators, which are useful in helping to understand its activities, performance, results and impact on the Group, are therefore presented in a specific section on page 194. This section reports on the initial results emerging from the materiality analysis conducted by the Tamini Group in 2018. The Terna Group acquired Avvenia (see page 27), a subsidiary of Terna Energy Solutions, in its turn controlled by Terna, in 2018. Data for Avvenia (16 staff at 31 December 2018) has not been consolidated for 2018, but work on their inclusion by the end of 2019 has already begun.

In accordance with the materiality principle, the data presented in the Sustainability Report cover all the companies with a significant impact on sustainability (for example, in terms of their size or number of personnel, their potential impact on the environment and the community or the number of transactions/activities that took place during the year), and where Terna directly or indirectly exercises control or has the power to govern their financial and operating policies. There are no joint ventures, other subsidiaries or leased assets that might significantly influence the scope or the comparability of the environmental and social data.

In 2018, information on the 232 electricity substations formerly owned by RFI (172 at the end of 2017) was included in the scope of the environmental data. Only the substations that, by 31 December 2018, had been integrated into the Terna Group's scope of operations have been consolidated. The remaining 122 electricity substations formerly owned by RFI were operated under an O&M (Operation & Maintenance) contract entered into with the previous owner.

The main impacts of the activities of the Group's overseas subsidiaries have been included in the Report. This data is reported separately from the information for the Parent Company due to the different impact of the related regulatory environment. Data for the Montenegro-based subsidiary, Terna Crna Gora d.o.o., has been included in the scope of the sustainability indicators, unless otherwise indicated.

The data has been calculated on the basis of Terna's general accounts and other information systems. Where estimates have been used in calculating the indicators, the method used has been described.

All the GRI indicators published are listed below in the "GRI content index", in which eventual limitations with respect to the relevant requirements are noted (see page 203).

Comparative analysis of sustainability performance

In the belief that a comparison of environmental, social and governance performance should not only concern the Company but also its stakeholders, as in previous years, this Report also includes comparisons between Terna's results and those of other companies. The comparative sustainability indicators regard the following topics: carbon intensity (new in the 2018 Sustainability Report), the SF₆ leakage rate, per capita hours of training and the staff turnover rate.

The main criteria adopted in the analysis, as a premise for reading and interpreting the comparisons of each of the indicators in the Report, are set out below:

- three company peer groups were chosen: the first consists of the leading European and non-European Transmission System Operators in terms of the number of kilometres of line operated;
- the second, covering a range of sectors, comprises large Italian companies (the 40 companies listed on the FTSE MIB on 8 September 2018);
- and the third consists of the international best performers in the Electric Utilities - ELC sector (identified by the sustainability rating agency, RobecoSAM, and included in the Dow Jones Sustainability World Index in September 2018).

The purpose of the three peer groups - also in connection with the type of indicator examined - is to provide a comparison between companies with the same operating characteristics, including an Italian comparison and one with the top international performers from the same sector. Among the companies in the three peer groups, consideration has been given to the ones that publish useful information for comparison on their websites via their Sustainability Report (even if it has not been drawn up in accordance with the GRI guidelines) or via other documents (integrated reports, HSE reports, financial reports, etc.). This led to a reduction in the sample compared with the number of companies in the peer group at the outset. The comparative analysis necessarily refers to data for 2017, as the comparisons were made whilst the 2018 reports were being prepared, as was also the case for Terna.

It should be noted that, despite the exclusion of explicitly non-homogeneous data, in many cases doubts remain regarding the actual comparability between companies, especially in situations where significant discrepancies were found between the data reported by some companies and the average figure for the peer group.