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ITALGAS  
2017  
FINANCIAL  
REPORT



## **ITALGAS IS WARMTH**

Behind simple gestures such as turning on the tap or the heater there are almost two centuries of history.

Italgas's contribute is a committed, reliable and innovative one which arrives into the houses of the Italians in order to bring natural gas warmth, for more then 180 years.

Flipping through these pages, you will find a visual translation of some of the daily moments alternating and being animated also thanks to our people's work.





## Values and Mission

Expertise, efficiency, innovation, reliability, security, proximity to the people.

Every day, for more than 180 years, the work of the men and women at Italgas has drawn inspiration from these values.

Italgas always accompanies the economic and social development of the country promoting sustainable growth.

It is currently the leading natural gas distributor in Italy and number three in Europe.

On these strong foundations, the Group is now looking forward and striving to strengthen its market presence.

Investments, quality of service and digitisation are the main channels of the strategy implemented to achieve these ambitious goals and to continue to generate value.

Italgas, over 180 years of history and a successful future yet to be written.

The names Italgas, Italgas Group or Group refer to Italgas S.p.A. and the companies comprised in the area of consolidation.

## Corporate bodies

### BOARD OF DIRECTORS<sup>(a)</sup>

#### Chairman

Lorenzo Bini Smaghi

#### Chief Executive Officer and General Manager

Paolo Gallo

#### Directors

Nicola Bedin

Federica Lolli <sup>(b)</sup>

Maurizio Dainelli

Cinzia Farisè

Yunpeng He

Paolo Mosa

Paola Annamaria Petrone

### CONTROL AND RISKS AND RELATED-PARTY TRANSACTIONS COMMITTEE <sup>(d)</sup>

Paola Annamaria Petrone (Chairman)

Nicola Bedin

Federica Lolli

### FINANCE AND SERVICE GENERAL MANAGER <sup>(g)</sup>

Antonio Paccioretti

### INDEPENDENT AUDITORS <sup>(i)</sup>

PricewaterhouseCoopers S.p.A.

### BOARD OF STATUTORY AUDITORS<sup>(a)</sup>

#### Chairman

Gian Piero Balducci

#### Standing auditors

Giandomenico Genta

Laura Zanetti

#### Alternate auditors

Barbara Cavalieri<sup>(c)</sup>

Walter Visco

### APPOINTMENTS AND REMUNERATION COMMITTEE <sup>(e)</sup>

Cinzia Farisè (Chairman)

Maurizio Dainelli

Federica Lolli

### SUSTAINABILITY COMMITTEE <sup>(f)</sup>

Nicola Bedin (Chairman)

Yunpeng He

Paolo Mosa

### SUPERVISORY BODY<sup>(h)</sup>

Carlo Piergallini (Chairman)

Eliana La Ferrara

Francesco Profumo

a) Appointed by the Shareholders' Meeting of 4 August 2016. In office until the date of the Shareholders' Meeting called for the approval of the financial statements for the year ending 31 December 2018.

(b) Director co-opted by the Board of Directors on 27 July 2017 to replace Barbara Borra.

(c) Appointed by the Shareholders' Meeting on 28 April 2017 to replace alternate auditor Marilena Cederna.

(d) Committee established by the Board of Directors on 4 August 2016. Members appointed by the Board of Directors on 23 October 2017.

(e) Committee established and members appointed by the Board of Directors on 23 October 2017.

(f) Committee established by the Board of Directors on 4 August 2016. Members appointed by the Board of Directors on 5 September 2016.

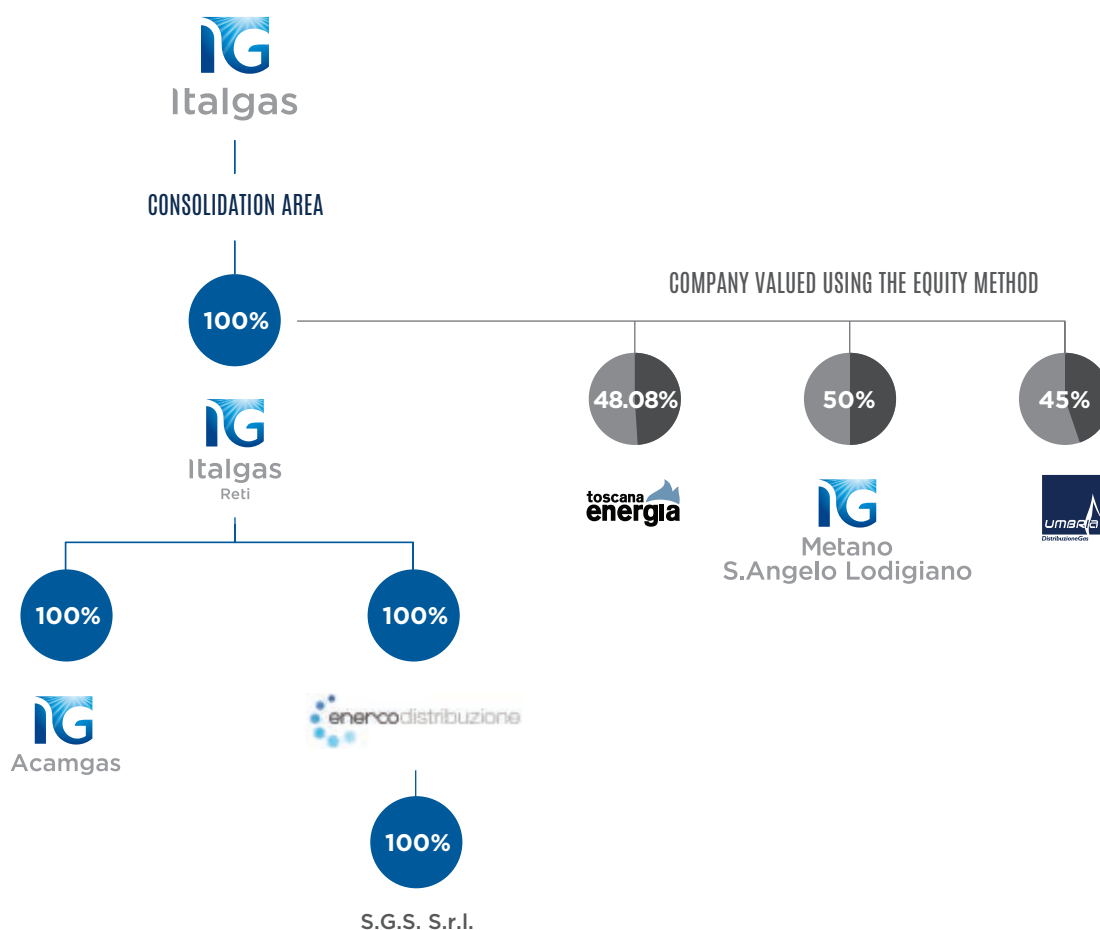
(g) Appointed by the Board of Directors on 26 September 2016 with effect from 7 November 2016.

(h) Appointed by the Board of Directors on 20 December 2016.

(i) Engagement assigned by the Shareholders' Meeting of 28 April 2017 for the period 2017-2025.

## Group structure as at 31 December 2017

The structure of the Italgas Group as at 31 December 2017 is shown below:



The changes in the scope of consolidation of the Italgas Group as at 31 December 2017 compared to 31 December 2016<sup>3</sup>, referred to the entry of Enerco Distribuzione and its subsidiary S.G.S. following the acquisition, effective 6 December 2017, of 100% of the share capital of Enerco Distribuzione.

<sup>3</sup> On 1 October 2017, Napoletanagas was merged into Italgas Reti after acquisition of the residual share capital (0.31%).



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*Disclaimer*

*The Annual Report contains forward-looking statements, specifically in the "Outlook" section, relating to: investment plans, future operating performance and project execution. The forward-looking statements, by their nature, involve risks and uncertainties as they depend on the occurrence of future events and developments. The actual results could therefore differ from those announced in relation to various factors, including: actual operating performance, general macro-economic conditions, geopolitical factors such as international tensions, the impact of energy and environmental regulations, the successful development and application of new technologies, changes in stakeholder expectations and other changes in business conditions.*





# **DIRECTORS'** **REPORT**





## Letter to Shareholders and Stakeholders

To our Shareholders and Stakeholders, Heartfelt thanks go to you, you who believe in Italgas, and a special thank you to all our men and women who every day invest energy, skills and expertise in the company's progress and development.

180 years after it was founded and just over a year since our return to the stock market, the facts speak for themselves. From 7 November 2016 onwards the company upped its pace, accelerating all its core and non-core activities: the investments made, the corporate acquisitions carried out, the operational reorganisation completed, the corporate restructuring in progress and the economic and financial results achieved all tell of the significant work undertaken.

Italgas is the no. 1 operator in Italy and the third ranked in Europe. With a market share of 34% for municipal gas distribution, it manages over 66 thousand km and 7.5 million gas delivery points spanning 1,609 concessions<sup>2</sup>.

The increased workforce, market consolidation and digitisation of the network and processes are the pillars of the 2017-

2023 Strategic Plan presented in June 2017. First and foremost the investments in the networks, our key asset, where maintenance and completion of the new networks (34 municipalities now with gas in Calabria, Sicily and Campania), the total investment came to over €250 million.

In 2017, 1.66 million smart meters were installed (primary enabler for network digitisation), with the average number of installations even reaching 12,000 per day, with a total investment of €230 million.

The total investments in the workforce amounted to €521.9 million, up 38.1% on 2016.

In 2017 and the first few months of 2018, Italgas carried out a series of corporate transactions designed, on the one hand, to consolidate and strengthen its presence in the areas of interest and, on the other, to invest in areas of Italy not yet benefiting from natural gas distribution infrastructures. Included in this scenario are the acquisitions of Enerco Distribuzione (27 concessions in the provinces of Padua and Vicenza), a business unit of Amalfitana Gas (12

<sup>2</sup> The figures also include unconsolidated investees.

concessions in as many municipalities in Campania), the distribution network of Portopalo di Capo Passero (Syracuse) and 6 companies previously controlled by CPL Concordia, which hold a total of 7 concessions to be implemented in 16 municipalities on the islands of Ischia and Procida, in Calabria and in Sicily, for which a binding purchase agreement has been signed. A very important step on this path to consolidation was marked by the Group's entry to Sardinia, the only region in Italy that still does not benefit from an interconnected gas distribution infrastructure: Italgas acquired Ichnusa Gas, holder of 12 concessions for the installation and operation of gas distribution networks in 81 municipalities in Sardinia, from CPL Concordia. It has also signed a binding agreement with Hera for the purchase of Medea, gas distribution and sale concession holder in the city of Sassari.

These acquisitions, for a total enterprise value of € 135 million, include a portfolio of 70,000 active users with a growth potential of 150,000 and will require additional

investments to complete the networks and systems for a gross figure of around €240 million (of which €80 million in public grants already agreed by the competent bodies). These form part of the €2 billion investment dedicated to tenders and acquisitions.

The digitisation of corporate networks and processes is the main challenge the company will face in the coming years: on the one hand, completion of the smart meters installation plan and, on the other, the installation of sensors covering the entire Italian network that will allow management of the network using innovative methods, criteria and algorithms that will make it unique in Europe.

The future migration to the Public Cloud and adoption of Infrastructure as a Service (IaaS), as an infrastructural solution for the application map, is the first step and the element that will allow simplification and full digitisation of the corporate processes, so we can confirm that your company has implemented an innovation process that is unique in the gas distributors panorama.

To overcome the market and technological

challenges, Italgas has adopted a new standard Operations model based on more streamlined, more efficient local entities, also creating teams of professionals acting as true skills and know-how centres. An in-depth corporate simplification has also commenced, and will be completed in 2018, with further optimisation of the area operations structures, technical management and staff departments.

The Company's shares closed 2017 with an official price of €5.1085, up 36.9% with respect to the official price recorded at the end of 2016 (€3.731), reaching the maximum official price for the period of €5.3305 on 8 December. Considering the dividend of €0.2 per share paid out on 22 May, the Total Shareholder Return (TSR) on the share was 42.3%.

In 2017, Italgas issued bonds for a total nominal value of €2,650 million, with demand far outweighing the number offered. In addition, on 23 January 2018 Italgas successfully arranged reopening of €250 million of the previous bond issue maturing January 2029. Through these bond issues,

the Company achieved a financial structure as at 31 December 2017 that envisages a fixed rate of 71.3% for the total net financial debt amounting to €3,720.3 million.

In terms of economic results, a careful cost containment policy brought the adjusted EBIT for 2017 to €422.9 million, up 17.9% on 2016.

The adjusted net profit was €296.4 million, recording a 34% increase compared to 2016. The cash in flows from operating activities for €549.4 million allowed full coverage of the funding needs for net investments for the period and the generation of free cash flow before M&A transactions of €109.2 million.

The positive results for the period allow the Company to propose the distribution of a dividend of 20.8 Eurocents per share, in line with the dividend increase rate disclosed to the market.

Without reneging on the expectations of its shareholders and stakeholders, Italgas is committed to a sustainable approach to business, also creating social

and environmental value. In 2017 the company established the guidelines for its first Sustainability Plan, the result of a process that involved all the Company's management. The Plan defines the strategic guidance, commitments and actions that are consistent and integrated with issues in the business plan.

The Italgas share has been included in the FTSE4Good series of indices. The Company has satisfied the strict criteria of the independent FTSE Environmental, Social and Governance (ESG) methodology and

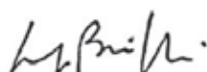
was identified by the CDP (Carbon Disclosure Project) as among the international leaders for strategies and actions undertaken to combat climate change, achieving inclusion in the "Climate Change A-List".

There are still many challenges to face in 2018 and in the coming years. Thanks to its people, the company is ready to face them. To all of you who believe in Italgas, we again wish to thank you for everything we have achieved and will continue to achieve together.

12 March 2018

for the Board of Directors

Chairman  
Lorenzo Bini Smaghi



Chief Executive Officer  
Paolo Gallo







## Highlights 2017

### Financial highlights

- **Adjusted EBITDA, €781.2 million**, up 14.1% on the adjusted figure for 2016;
- **Adjusted EBIT, €422.9 million**, up 17.9% on the adjusted figure for 2016;
- **Adjusted net profit, €296.4 million**, up 34% on the corresponding value in 2016;
- **Investments, €521.9 million** (+38.1% compared to 31 December 2016);
- **Net cash flow from operating activities, €549.4 million**, fully covering funding needs for net investments for the year;
- Fixed rate **bond issues** arranged for a total nominal value of **€2,650 million**;
- **EIB loan for €360 million** finalised to support the Group's investments plan;
- **Official closing price of the Italgas share** on the Milan Stock Exchange as at 31 December 2017 of **€5.109** (€3.731 as at 31 December 2016; +36.93%);
- **Proposed dividend of €0.208 per share.**

**781.2**  
€mn

ADJUSTED EBITDA  
+14.1%

**296.4**  
€mn

ADJUSTED  
NET PROFIT +34%



**ELECTRONIC METERS INSTALLED**

# 1.66mn

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**Operating highlights**

- **1.66 million new electronic meters** installed to replace traditional meters;
- **Distribution network** extended by 975 km (of which 838 km from the acquisition of Enerco);

**INCREASE OF THE DISTRIBUTION NETWORK**

# 975Km

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- **Gas distribution service concessions** risen to 1,500 municipalities (1,472 as at 31 December 2016), of which 1,484 operative (1,422 as at 31 December 2016), also due to the acquisition of Enerco on 6 December 2017 and the operational start-up of new networks in 34 municipalities in Campania, Calabria and Sicily;
- **New Operations organisation** completed through the setup of 14 regional hubs and the continuous improvement programme “**Migliora**” launched;
- **Italgas Acqua S.p.A.** established on 1 January 2018 following the proportional partial demerger of Italgas Reti to a newco through assignment to the latter of the former Napoletanagas water business unit.



## Italgas and the financial markets

The Italgas share closed 2017 with an official price of €5.1085, up 36.9% with respect to the official price recorded at the end of 2016 (€3.731), reaching the maximum official price for the period of €5.3305 on 8 December 2017. Taking into account the dividend of €0.2 per share paid out on 22 May, the Total Shareholder Return (TSR) of the share was 42.3% in 2017.



In 2017, the average daily trading volume of the Italgas stock on the electronic market of the Italian Stock Exchange was 2.3 million shares, with a greater concentration of trades in the first half of the year, particularly around the time of the announcement of the 2016 annual results at the end of March and the Strategic Plan in late May.

The Eurozone stock markets recorded consistent upward trends in 2017, sustained by the general improvement in macroeconomic data, extension of the ECB's quantitative easing (QE), approval of the US tax reform and the reduced political risk following the election results in France, the Netherlands and Germany. Adjusted for the dividend, the Euro Stoxx share index closed 2017 up by 13.4% compared to the end of 2016; amongst the main indices, the FTSE Mib had the best performance (+16.9%), essentially driven by the improvement in a number of industries and in the banking sector, which benefited from expectations of better profitability due to the stronger macroeconomic scenario and growing bond yields. This is followed by the Frankfurt DAX and the Paris CAC 40 at +12.5%. London's FTSE 100 saw a 12.0% increase. This index was bolstered at the end of the year by expectations of an unblocking of Brexit negotiations.

**€5.1085 OFFICIAL CLOSING PRICE OF THE ITALGAS SHARE AS AT 31 DECEMBER 2017**

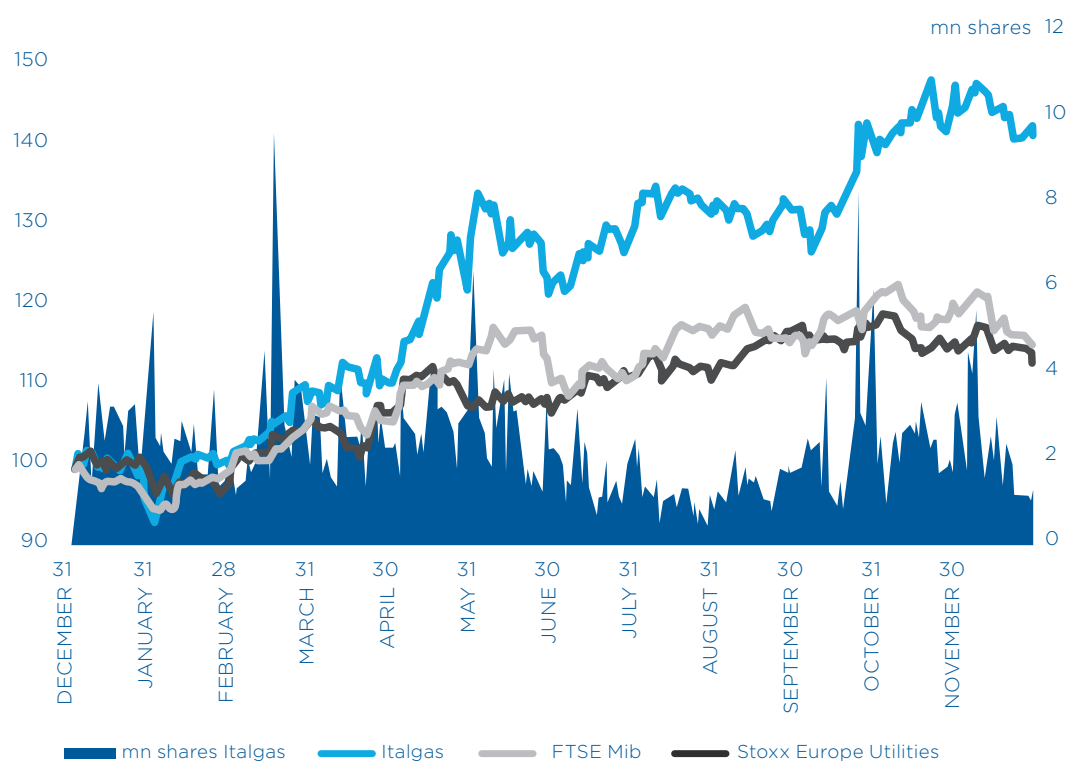
# +36.9%

With a 21.1% increase, Euro Stoxx Utilities achieved one of the best sector-specific performances of the year, essentially sustained by the securities of integrated companies, which benefited from rising electricity prices based on the higher prices of commodities and forecasts of sector consolidation, with particular reference to Central European operators.

Within a context characterised by considerable volatility triggered by fluctuations in oil prices and the evolution in the political scenario mentioned above, core Eurozone sovereign bond yields showed a general rise in 2017 due to the improved economic scenario, a factor partly mitigated by the ECB's decision to extend QE to 2018, and the containment of inflation forecasts as a result of appreciation of the EUR/USD exchange rate. The yield of German 10-year government bonds (Bund) rose by 22 bps to 0.43%, while the spread between the Italian 10-year government bond (BTP) and the Bund remained largely unchanged at 159 bps. The EUR/USD exchange rate appreciated by 14.1%, reflecting the trend for sovereign

returns and diverging expectations in terms of monetary policy developments from the respective central banks, with the FED ahead of the ECB in the gradual withdrawal of monetary stimuli.

COMPARISON OF THE QUOTES ITALGAS, FTSE MIB AND EURO STOXX 600 UTILITIES  
(1 JANUARY 2017 - 31 DECEMBER 2017, FIGURES ADJUSTED FOR DIVIDENDS)



## SHAREHOLDERS

The share capital of the Company as at 31 December 2017 consisted of 809,135,502 shares without par value, giving a share capital value of €1,001,231,518.44.

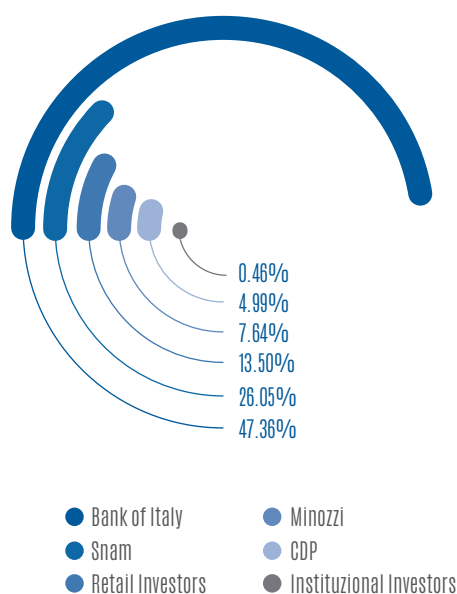
As at 31 December 2017, based on the shareholders' list, the information available and the notices received pursuant to Article 120 of the Consolidated Finance Act, the owners of significant shareholdings (shares exceeding 3%) are represented below.

Consolidating Company	Registrants	% Ownership
Italgas S.p.A.	CDP Reti S.p.A. <sup>(*) (**)</sup>	26.05
	Snam S.p.A.	13.50
	Lazard Asset Management Llc	7.57
	Romano Minozzi	4.99
	Other shareholders	47.89

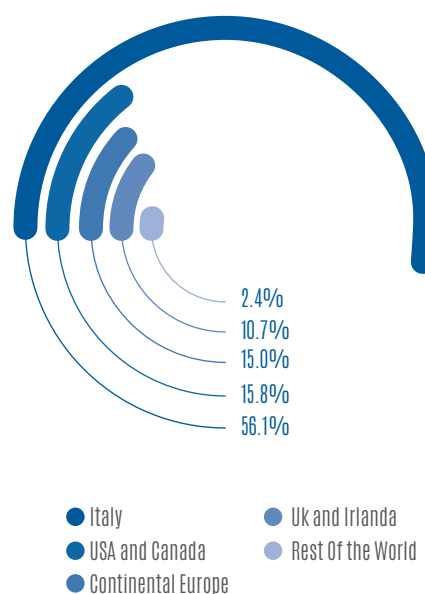
(\*) On 20 October 2016, a shareholders' agreement was concluded between Snam, CDP Reti and CDP Gas, with effect from the date of the demerger, in relation to Italgas S.p.A. Effective as of 1 May 2017, CDP Gas was merged by incorporation into CDP. Subsequently, on 19 May 2017, CDP sold to CDP Reti, *inter alia*, the equity investment held in Italgas S.p.A., equal to 0.969% of the share capital of Italgas S.p.A.

(\*\*) CDP Reti is owned 59.1% by CDP, 35% by State Grid Europe Limited – SGEL, a subsidiary of State Grid Corporation of China, and 5.9% by some Italian institutional investors.

Italgas Shareholders by type investor



Italgas Shareholders by geographical area







## The Italgas Group

### OVERVIEW OF ITALGAS

Italgas is the leader in Italy in the industry of natural gas distribution and is the third largest operator in Europe.

The distribution service consists of transporting gas through local pipeline networks, from points of delivery at the reduction and measurement stations interconnected with the transport networks ("city-gates") up to the final delivery points to customers (households, enterprises, etc.).



Furthermore, Italgas is engaged in metering activities, which consist of determining, gathering, making available and archiving metering data on natural gas withdrawn over the distribution networks.

Italgas is subject to regulation by the Italian Regulatory Authority for Energy, Networks and Environment (also referred to as the Authority or ARERA), formerly the Authority for Electricity, Gas and Water systems (AEEGSI), which defines both how to conduct the service and the rates for distribution and metering.

Gas distribution is traditionally carried out under concession by awarding the service on a municipal basis. In 2011, four ministerial decrees were adopted to reform the regulations regulating the sector. Specifically, a special decree established 177 minimum geographical areas ("ATEM") based on which the new concessions should be awarded.

The gas distribution service is performed by transporting the gas on behalf of authorised sales companies for marketing to end customers.

The relationship between the distribution companies and sales companies is governed by a special document prepared by the AEEGSI called the "Network Code," which specifies services performed by the distributor. These are broken down into main services (gas distribution service; technical management of the distributed plant) and ancillary services (start-up of new plants; activation, deactivation, suspension and reactivation of supply to end customers; group verification of metering at the request of end customers, etc.).

## 180 YEARS OF ITALGAS HISTORY



### 1837 - THE FOUNDING



The history of Italgas is identified with that of the gas industry in Italy that began in Turin in 1837 with the establishment of the Public Gas Lighting Company in the city of Turin. In 1851, when the Turin Stock Exchange opened, the Company's stock was one of the 7 "Private funds" allowed to be listed. In 1863, immediately after the unification of Italy, the company changed its name and took the name of Società Italiana per il Gaz.

### 1900 - THE EXPANSION

1900 marked its entrance into the Milan Stock Exchange. The spread of electricity instead of gas for public lighting impelled the company to seek new business opportunities in homecare applications, beginning with cooking and then heating and hot water. In the 1920s, a large acquisition programme was launched for majority packets of gas companies operating in some Italian cities, including Venice (1924), Rome (1929) and Florence (1929), with the goal of creating a large industrial group.

### 1967 - ENTRANCE INTO ENI

The stock packet that ensured the control of Italgas was acquired by Eni, even then one of the largest energy groups in the world. With the progressive confirmation of natural gas and the development, starting from the 1970s, of import pipeline networks, the company has focussed on delivering new city networks and the modernization

of existing ones, taking a leading role in developing the country's natural gas supply. In 2003, as part of a reorganization process, Eni delisted the Italgas stock from the stock market.

### 2009 - ITALGAS WAS ACQUIRED BY SNAM

Snam collected Eni's entire stake in Italgas as part of an operation aimed at creating an integrated group to safeguard all the regulated activities of the natural gas sector, from transport to storage, from urban distribution to regasification.

### 2016 - SEPARATION FROM SNAM AND RETURN TO THE STOCK EXCHANGE

On 7 November 2016, with the completion of the operation of the Snam Group's industrial reorganisation, the Italgas stock went back to being listed on the FTSE MIB index of the Italian Stock Exchange.

### 2017 - 180 YEARS OF HISTORY CELEBRATED

On 12 September 2017 Italgas celebrated 180 years of business: a milestone not only for the company, but for an entire industrial segment and for the whole country, for which the company has developed a fundamental service, i.e. gas distribution, changing Italians' habits forever. The 180 years of history are celebrated in a book written by the historian Valerio Castronovo, edited by Laterza for the "Grandi Opere" series, and with events held in four cities: Turin, Milan, Rome, Naples.

### 2017 - LAUNCH OF ITALGAS GROWTH THROUGH NEW ACQUISITIONS

In November 2017, Italgas launched its process of acquiring new companies with a view to accelerating its growth and increasing its market share in Italy from 30% to 40%.



## Summary figures and information

### MAIN EVENTS

#### THE CONSOLIDATION PROCESS

In 2017 and the first part of 2018, Italgas carried out transactions consistent with the growth strategy illustrated in the 2017-2023 Business Plan, which offers further enhancement of its role in areas of interest in Italy. In particular, in 2017 it acquired 100% of Enerco Distribuzione and its subsidiary S.G.S., in January 2018 the business units of Amalfitana Gas and AEnergia Reti for a total of 40 natural gas distribution concessions and over 70 thousand active delivery points, then in February 2018 Ichnusa Gas.



On 1 October 2017, Napoletanagas was merged into the parent company Italgas Reti after acquisition of the entire share capital of the merged company.

On 30 November 2017, Italgas signed a binding agreement with CPL Concordia for the acquisition of a **portfolio of 7 gas concessions in Southern Italy**, covering a total of 16 municipalities. The total value of the portfolio involved in the agreement was established at €13 million. Finalisation is expected by the end of April 2018, subject to a number of pre-closing formalities. In particular, the agreement envisages that Italgas acquires:

- 3 concessions for natural gas supply in Barano, Lacco Ameno and Casamicciola on the island of Ischia;
- the concession for natural gas supply on the island of Procida;
- the concession for natural gas supply in the Bacino 12 area of Calabria, formed from 10 municipalities in the province of Reggio Calabria;
- 2 concessions for natural gas supply in the municipalities of Favara and Siculiana in the province of Agrigento.

Of the 7 concessions, some are to be built, others to be implemented. One of them - for the island of Procida - is operative. The total investment to create the networks is expected to be around €95 million, part-financed by public grants. Once they are completed, the infrastructures will span over 400 kilometres and serve an area with potential for around 32,000 new customers.

Italgas finalised acquisition of 100% of **Enerco Distribuzione** on 6 December 2017. The closing value of the investment was €35.9 million, corresponding to an enterprise value of €50.3 million. Enerco Distribuzione, which holds 27 concessions in the provinces of Padua and Vicenza, manages a network of over 800 km of pipelines and serves about 30 thousand users.

This transaction will allow Italgas to increase its presence in an area of North-East Italy considered to be of enormous importance to the Group's development and to implement potential synergies with concessions already managed in that region.

On 21 December 2017, Italgas and Hera signed a binding agreement for the transfer to Italgas of 100% of the share capital of **Medea**, holder of the concession for gas distribution and sales in the city of Sassari. The total value of Medea was established at €24.1 million. The company serves around 13,000 customers, all resident in Sassari, to which it distributes more than 5 million cubic metres of LPG per year. The company's potential catchment area is around 30,000 customers. The network, ready for future conversion to natural gas, covers

over 190 kilometres and is currently powered by LPG through a storage and production plant located on the outskirts of the city.

On 26 January 2018, the acquisition of the **Amalfitana Gas business unit** was finalised for natural gas distribution activities in three ATEMs in Campania and Basilicata. The total Amalfitana Gas assets acquired include 12 concessions in the municipalities of Somma Vesuviana, Viggiano, Baronissi, Calvanico, Pellezzano, Fisciano, Siano, Oliveto Citra, Contursi Terme, Montesano sulla Marcellana, Monte San Giacomo and Atena Lucana, with an operations network spanning around 330 kilometres and serving over 22,000 users. The value of the transaction was €21 million.

Subsequently, on 31 January 2018, Italgas finalised the acquisition of the AEnergia Reti business unit relating to the distribution network serving the municipality of Portopalo di Capo Passero (Syracuse). The AEnergia Reti business unit acquisition involves a network, completed but not yet operative, that spans around 35 kilometres and serves a potential customer base of 1,400. The amount paid was €2.2 million.

Implementing the binding agreement signed on 8 November 2017, on 28 February 2018 Italgas acquired 100% of the share capital of **Ichnusa Gas**, a holding company with control of 12 companies granted concessions for the installation and operation of gas distribution networks in 81 municipalities in Sardinia, from CPL Concordia and Impresa Costruzioni Ing. Raffello Pellegrini S.r.l. The enterprise value of Ichnusa Gas was established at €26.2 million. As at the acquisition date, 2 of the 12 concessions are provisionally operative with the first customers served with LPG, whilst the remaining 10 refer to networks under construction and to be implemented for a total investment forecast at over €170 million, part-financed from regional public grants.

The aforementioned Ichnusa and Medea transactions mark the Group's entry into Sardinia, the only region in Italy that still does not benefit from an interconnected natural gas distribution infrastructure.

Lastly, note that on 21 December 2017 the administrative bodies of Enerco Distribuzione, S.G.S. and Italgas Reti approved the plan to merge Enerco Distribuzione and its subsidiary S.G.S. into Italgas Reti, effective from 1 January 2018 for accounting purposes.

#### **DIGITISATION OF THE CORPORATE NETWORKS AND PROCESSES**



In the current growth context, digital technology plays a key role in enabling corporate strategies, providing tools to optimise processes and improve the service to customers and end users.

As a first step towards digital transformation, Italgas decided to profit from the advantages offered by the Public Cloud and to adopt Infrastructure as a Service (IaaS) as the infrastructural solution for its application map.

This technological leap will not only allow Italgas to improve the management and reliability of its IT systems, but will also lay the foundations for the future digitisation of the company.

The project is currently in progress and the launch is expected in summer 2018.

In parallel, Italgas has begun to simplify its application map. This will allow Italgas immediate access to all the new technologies offered by the world's major IT vendors now and in the future, creating the technology base necessary for the digitisation of corporate processes through the use of innovative technologies.

#### OPTIMISATION OF THE DEBT STRUCTURE AND EMTN PROGRAMME

In order to have a financial structure featuring low borrowing costs, a high average duration of debt and a fixed rate debt percentage that is also high with the aim of seizing upon the favourable financial market terms, in 2017 Italgas issued bond loans for a total of €2,650 million with the following characteristics: (i) €1,500 million, issued on 19 January 2017 and divided into two tranches, the first with a term of 5 years and the second of 10 years, both at a fixed rate, amounting to €750 million each and an annual coupon of 0.50% and 1.625%, respectively; (ii) €650 million issued on 14 March 2017, maturing on 14 March 2024 with a fixed rate annual coupon of 1.125%; (iii) €500 million issued on 18 September 2017, maturing on 18 January 2029 with a fixed rate annual coupon of 1.625%.

#### ARRANGED BOND ISSUES FOR A TOTAL NOMINAL VALUE OF

# €2,650mn

These bond loans were issued as part of the Euro Medium Term Notes Programme of the company, renewed on 9 November 2017 and increased up to a total of €3.5 billion, in implementation of the action approved on 23 October 2017 by the Italgas Board of Directors.

The programme, valid until 31 October 2018, provides for the issue of one or more unconvertible bond issues, to be placed with institutional investors operating in Europe. This allowed full repayment of the €2.3 billion floating rate Bridge to Bond loan already in April 2017. The Bridge to Bond was provided by a pool of 11 banks as part of the financing package signed by Italgas in October 2016 with leading banks that also included two floating rate revolving credit lines, for committed amounts of €600 million and €500 million with durations of 3 years and 5 years, respectively, and a 3-year floating rate term loan for a total of €200 million maturing in October 2019.

The reopening, achieved by Italgas on 30 January 2018, for €250 million of the bond issue originally released on 18 September 2017 (€500 million, maturing 18 January 2029 with a coupon of 1.625%) allowed partial early repayment in February 2018 of the term loan for €200 million and continuation of the process to optimise the debt structure, increasing the average duration and the fixed rate percentage.

Added to these loans are those made available by the European Investment Bank (EIB),

which totalled €784 million as at 31 December 2017. In fact, on 19 December 2017, Italgas finalised a new 20-year EIB loan for €360 million to finance a Network Upgrade project consisting in the extension and enhancement of the gas distribution network, the installation of smart meters and the modernisation and replacement of existing assets to improve the network's safety and operating efficiency. At the same time as disbursement of the loan, a previous EIB loan for €300 million was repaid.

January 2018 saw the finalisation of an Interest Rate Swap transaction maturing in 2024, used to transform the entire EIB loan for the Gas Network Upgrade amounting to €360 million from floating rate to fixed rate.

**FINALISED AN EIB LOAN FOR**

# €360mn

## KEY FIGURES

In order to allow for a better assessment of economic and financial performance, the Directors' Report includes the reclassified financial statements and certain alternative performance indicators, including EBITDA, EBIT and net financial debt, in addition to the financial statements and conventional indicators laid out in IAS/IFRS. These figures are presented in the tables below, the relative notes and the reclassified financial statements. For the definition of the terms used, when not directly specified, please refer to the chapter "Financial results, NON-GAAP Measures".

## KEY SHARE FIGURES

(€ million)	2016	2017
Number of shares of share capital (million)	809	<b>809</b>
Number of shares outstanding as at 31 December (million)	809	<b>809</b>
Average number of shares outstanding during the year (million)	809	<b>809</b>
Year-end official share price (€)	3.73	<b>5.11</b>
Official average price per share for the year (€)	3.47	<b>4.51</b>
Market capitalisation <sup>(a)</sup> (million)	3,019	<b>4,135</b>

(a) The product of the number of shares outstanding (exact number) multiplied by the year-end official share price.

## KEY FINANCIAL FIGURES

(€ million)	2016	2017
Total revenues <sup>(*)</sup>	1,077.9	<b>1,124.2</b>
EBITDA <sup>(**)</sup>	661.6	<b>776.2</b>
Adjusted EBITDA <sup>(**)</sup>	684.4	<b>781.2</b>
EBIT <sup>(**)</sup>	336.0	<b>417.9</b>
Adjusted EBIT <sup>(**)</sup>	358.8	<b>422.9</b>
Net profit	119.2	<b>292.8</b>
Adjusted net profit <sup>(**)</sup>	221.1	<b>296.4</b>

(\*) Revenue from the construction and upgrading of distribution infrastructure entered in accordance with IFRIC 12 and recognised in an amount equal to the costs incurred (€315.5 million and €479.7 million respectively in 2016 and 2017) is shown as a direct reduction of the respective cost items.

(\*\*) The reported and adjusted versions of EBITDA and EBIT, and the adjusted net profit, are not measures allowed by IFRS. For their calculation, reference should be made to the chapter "NON-GAAP Measures" in this report.

(€ million)	31.12.2016	31.12.2017
Net invested capital as at 31 December	4,681.7	<b>4,905.9</b>
Shareholders' equity	1,064.3	<b>1,185.6</b>
Net financial debt	3,617.4	<b>3,720.3</b>

## OPERATING PERFORMANCE

The main operating figures of the Italgas Group in 2017 are shown below. To allow comparison with 2016 figures, the consolidated operating data is also provided for the conglomerate comprising Italgas S.p.A. since its incorporation (1 June 2016) and for Italgas Reti S.p.A., Napoletanagas S.p.A. and ACAM Gas S.p.A. from 1 January 2016.

### INVESTMENTS

In 2017 technical investments were made for €521.9 million, an increase of €143.9 million compared to 2016 (+38.1%).

(€ million)	2016	2017	Abs. change	Change %
<b>Distribution</b>	<b>210.0</b>	<b>253.2</b>	<b>43.2</b>	<b>20.6</b>
Network maintenance and development	172.0	<b>201.0</b>	29.0	16.9
Replacement of cast-iron pipes	38.0	<b>52.2</b>	14.2	37.4
<b>Metering</b>	<b>112.0</b>	<b>229.5</b>	<b>117.5</b>	
<b>Other investments</b>	<b>56.0</b>	<b>39.2</b>	<b>(16.8)</b>	<b>(30.0)</b>
	<b>378.0</b>	<b>521.9</b>	<b>143.9</b>	<b>38.1</b>

**Investments in distribution** (€253.2 million) mainly related to development projects (extensions and new networks) and the renovation of old sections of pipe, including the replacement of cast-iron pipes.

**Investments in metering** (€229.5 million) relate essentially to the remote metering plan which provided for the replacement of traditional meters with electronic ones, resulting in the installation of roughly 1.66 million new meters during 2017.

**Other investments** (€39.2 million) mainly concern IT, property and vehicle investments.

### KEY OPERATING FIGURES

(€ million)	31.12.2016	31.12.2017	Abs. change	Change %
Active meters (million)	6,536	<b>6,586</b>	0.1	0.8
Gas distribution concessions (number)	1,472	<b>1,500</b>	28.0	1.9
Distribution network (kilometres) <sup>(a)</sup>	56,798	<b>57,773</b>	975	1.7

(a) The data refers to kilometres of Italgas operating networks.

### MUNICIPALITIES IN CONCESSION AND LOCAL AREA TENDERS<sup>3</sup>

As at 31 December 2017, Italgas was the gas distribution service concession holder in 1,500 municipalities (1,472 as at 31 December 2016), of which 1,484 operative (1,422 as at 31 December 2016). The higher number of concessions is essentially due to the acquisition on 6 December 2017 of Enerco Distribuzione S.p.A. Also taking associates into account, the number of concessions totals 1,609.



In January 2018 Italgas finalised acquisitions of the gas distribution business units of two companies operating in Southern Italy: Amalfitana Gas and AEnergia Reti. From the Amalfitana Gas business unit acquisition, concluded on 26 January 2018, Italgas Reti gained the concessions for 12 municipalities in Campania and Basilicata. The acquisition of the AEnergia Reti business unit, concluded on 31 January 2018, gave Italgas the concession for the municipality of Portopalo di Capo Passero.

The following map shows the presence of the Italgas Group in Italy as at 31 December 2017.



<sup>3</sup> For more information on the regulation concerning the assignments of gas distribution service and the related call for tenders, please see the specific paragraph in the chapter "Legislative and regulatory framework".

In 2017, Italgas, present in 113 ATEMs, continued its activities of preparing and transmitting to the Local Authorities and/or Contractors the information and documentation provided by law, preparatory to offering tenders (Articles 4 and 5 of Ministerial Decree No. 226/11). In this context, activities were continued to achieve the approval for the repayment amounts owed to Group companies.

As a result of the business unit acquisitions from Amalfitana Gas and AEnergia Reti in January 2018, Italgas is present in 114 ATEMs.

Within the regulatory framework that provides for assigning gas distribution service by tenders for territory (and not individual municipality) as at 31 December 2017, 20 local tender notices were published (of which 5 suspended, 1 cancelled, 1 past the deadline for bids but suspended, another 2 past the deadline for bids and pending award, 6 extended beyond the initial deadlines and 2 revoked).

On 28 June, Italgas submitted the bid for the Turin 2 ATEM (geographical area) gas distribution services tender (roughly 190 thousand delivery points in 48 municipalities in the area surrounding the capital of Piedmont). No other operators submitted bids. The bid was admitted as it met the requirements laid out in the call for tenders.

On 1 September, Italgas also submitted a bid for the Belluno ATEM gas distribution services tender (roughly 45 thousand delivery points in 74 municipalities). The following operators also submitted bids in addition to Italgas: 2i Rete Gas, Ascopiave and Erogasmet, which filed an appeal with the Veneto Regional Administrative Court for cancellation of the tender. The appeal was rejected by the Veneto Regional Administrative Court with decision no. 78/2018, published on 24 January 2018. As a result of the pending appeal, the assessment of bids by the contracting authority had been frozen and following the decision can now begin again.

#### **GAS DISTRIBUTED**

As at 31 December 2017 Italgas had distributed 7,767 million cubic metres of gas (7,470 million cubic metres in 2016) through 284 marketing companies (282 in 2016). Also taking into account the associates, the gas distributed in 2017 totalled 8,979 million cubic metres.

#### **DISTRIBUTION NETWORK**

The gas distribution network as at 31 December 2017, covered 57,773 km (56,798 km as at 31 December 2016), an increase of 975 km compared with 31 December 2016. Also taking associates into account, the distribution network spans 66,154 kilometres.

**PRESENT, IN JANUARY 2018, IN**

**114** minimum geographical areas



## METERS

As at 31 December 2017, the number of active meters at delivery points amounted to 6.586 million (6.536 as at 31 December 2016). Also considering associates, the total number of active meters is 7.438 million.



The legislation on remote meter reading (Resolution No. 631/2013/R/gas as amended) defines the objectives, differentiated by calibre, of electronic meters put into service. These objectives were changed multiple times during the period (from Resolution ARG/gas 155/08 to Resolution 554/2015/R/gas). To comply with this requirement, the Italgas Group foresees replacement of approximately 3.7 million meters by the end of 2018, of which 2.8 million are already replaced. Also considering associates, Italgas expects to replace 3.95 million meters by the end of 2018, of which 3.07 million already replaced.

### NUMBER OF ACTIVE METERS AT DELIVERY POINTS AS AT 31 DECEMBER 2017

# 6.6 mn

## ENERGY EFFICIENCY - WHITE CERTIFICATES

The energy efficiency improvement goal for end use in Italy was mainly implemented through the Energy Efficiency Certificates mechanism (TEEs or White Certificates). This procedure was launched on 1 January 2005 in accordance with provisions of the Decree dated 20 July 2004.



By Decree dated 11 January 2017, the Ministry of Economic Development reiterated that all electricity and natural gas distributors with at least 50,000 end customers linked to their distribution network are mandatorily required to achieve energy savings goals for the years 2017-2020. To comply with these obligations, distributors can: directly implement projects, through subsidiaries or companies operating in energy services sectors, to encourage end consumers to improve the energy efficiency of installed technologies or related user habits, or purchase TEE from third parties confirming that the energy savings goals have been reached.

The Decree of 11 January 2017 also established energy saving goals for the three-year period 2017-2020 and introduced a further interim cancellation session in November, in addition to that envisaged for 31 May. In order to avoid penalties, the obliged entities must comply with at least 60% of the obligation envisaged and complete the remainder in the following year.

Based on criteria introduced by the Ministerial Decree, by Resolution no. 435/2017/R/efr of 15 June 2017 the Authority defined the calculation method for the tariff contribution towards costs incurred by the distribution companies subject to Energy Efficiency Certificate obligations for 2017 onwards. The tariff contribution is calculated on the weighted average price of trading carried out on the GME market during the reference year (1 June in year  $n$  to 31 May in year  $n+1$ ), applying certain adjusting ratios.

By the Resolution of 14 July 2017, the ARERA established the final tariff contribution as 191.40 €/TEE for 2016 (1 June 2016-31 May 2017).

Italgas's obligation for 2016 was 1,186,417 TEE. In May 2017, the Group notified the GSE that it had reached 60% of the 2016 obligation and completed the remainder from 2014. Note that the subsidiary Italgas Reti arranged the cancellation of 453,030 TEE from the 2016 obligation (41.0%), below the obligation threshold of 60% required by the Decree of 11 January 2017. In this respect, note that on 7 February 2018 the ARERA notified the company of the start of a penalties procedure<sup>4</sup>.

From 1 June 2017, Italgas began to acquire TEE on the market sufficient to comply with the 2017 obligation (822,123 TEE) and the residual obligations accrued in 2015 and 2016. The purchasing strategy aims as far as possible to reproduce the value of the 2017 contribution, the result of the calculation envisaged in the Resolution of 15 June 2017.

In the interim cancellation session of 30 November 2017, Italgas arranged the cancellation of 724,248 TEE obtained as an advance from the Energy and Environmental Services Fund (CSEA) at 191.4 €/TEE. The balance for the final contribution for 2017 will be paid at the same time as cancellation of the remainder at the cancellation session of 31 May 2018.

It is also important to mention a number of changes to the TEE mechanism introduced in 2017 that will have an impact from 2018 onwards. In particular, Resolution no. 435/2017/R/efr and the later Resolution no. 634/2017/R/efr gradually introduced the accrual criterion for recognition of the tariff contribution, in place of the cash criterion valid at the time. An appeal filed against these Resolutions by the ANIGAS trade association before the Regional Administrative Court is still pending. In addition, by Decree dated 11 January 2017 the cumulative period for residual obligations was reduced from 2 years to 1 year. Consequently, in 2018 (1 June 2018-31 May 2019) the distribution companies will need to cancel all residual obligations for 2016 and 2017.

<sup>4</sup> Further information is provided in note 25, "Disputes and other measures" in the Notes to the consolidated financial statements.

In 2017 as a whole, the Italgas Group purchased 1,197,441 TEE for an outlay of €319.2 million. On 31 May 2017 it cancelled 662,410 certificates and collected €126.8 million, then collected a further €138.6 million at the interim cancellation session of 30 November 2017 with a net financial commitment for the year of €53.8 million.

In 2017, economic management of the TEE led to expense for the Italgas Group of €0.1 million (€14.8 million in 2016).







## Regulation

The distribution of natural gas is regulated by the Regulatory Authority for Energy, Networks and Environment (ARERA), formerly the Electricity, Gas and Water System Authority (AEEGSI). Among its functions are the calculation and updating of the tariffs, and the provision of rules for access to infrastructure and for the delivery of the relative services.



The rate system establishes in particular that the reference revenue for the formulation of rates is determined so as to cover the costs incurred by the operator and allow for a fair return on invested capital. Three cost categories are recognised:

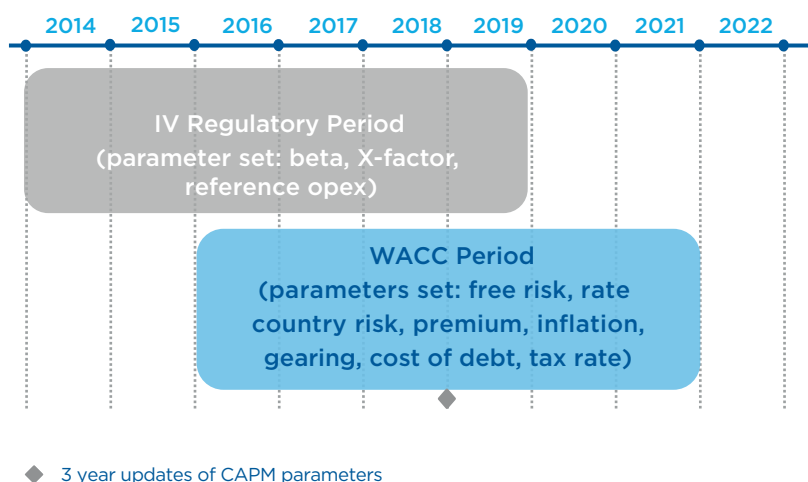
- the cost of net invested capital for RAB (Regulatory Asset Base) purposes through the application of a rate of return;
- economic and technical amortisation, covering investment costs;
- operating costs.

The main rate elements are reported below on the basis of the regulatory framework (Resolution no. 573/2013/R/gas as amended).

### Highlights from the fourth regulation period (from 01/01/2014 to 31/12/2019)

End of regulatory period (TARIFFS)	31 December 2019
Calculation of net invested capital recognised for regulatory purposes (RAB) (*)	Revalued historical cost Parametric method for centralised assets
Return on net invested capital recognised for regulatory purposes (pre-tax WACC)	Distribution: 6.1% for years 2016-2018 Metering: 6.6% for years 2016-2018
Incentives on new investments	Return on investments t-1 to offset the regulatory time lag (from 2013)
Efficiency factor (x factor)	1.7% - on distribution operating costs 0.0% - on metering operating costs

(\*) The estimated RAB for 2017 of the companies currently included in the scope of consolidation, calculated by applying the criteria adopted by the Authority in the definition of the reference rates, is equal to over €5.8 billion.



With **Resolution no. 573/2013/R/gas** the Authority defined the rate criteria for the distribution service and the metering service for the fourth regulatory period, from 1 January 2014 to 31 December 2019.

The invested capital of the distribution companies (RAB) is broken down into two categories: local invested capital and centralised invested capital. For the first three years of the regulatory period 2014-2016 (for the second three-year period, 2017-2019, please see Resolution no. 775/15 below):

- the approach for the valuation of local invested capital is based on the revalued historical cost method, while for investments relating to electronic meters, the standard cost method applies;
- for the valuation of centralised invested capital relating to the real estate and industrial buildings and other tangible and intangible assets, the parametric method applies;
- for centralised assets relating to remote management systems, there is a tariff recognition of remote metering/remote management costs and costs relating to concentrators incurred by companies for the first two years of the fourth regulatory period.

The revenue components correlated with the return and amortisation are determined on the basis of the annual update of net invested capital (RAB), with the inclusion of assets realised in year t-1.

The methodology for updating “price-cap” tariffs is applied only to the revenue component relating to operating costs, which are updated for inflation and reduced by a coefficient for the recovery of annual productivity which is established at 1.7% for operating costs relating to the distribution service and 0% for operating costs relating to the metering and marketing service.

With **Resolution no. 583/2015/R/com** the Authority defined the methods for determining and updating the rate of return on invested capital (WACC) for regulated infrastructural services of the electricity and gas sectors, unifying all parameters with the exception of the specific parameters for the individual services, including the beta parameter which expresses the specific level of non-diversifiable risk of the individual service and the weight of equity and debt capital used for the weighting (D/E ratio).

The duration of the regulatory period of the rate of return on invested capital for infrastructural regulations in the electricity and gas sectors is established as six years (2016-2021) and there is a mechanism for updating the rate in mid-period on the basis of economic trends.

For the distribution service, the WACC value for the 2016-18 three-year period was set by the Authority at 6.1% (down compared with 6.9% used in 2014-2015) in real terms before taxes, whereas for the metering service this value, for the same period of 2016-18, was set by the Authority at 6.6% (down compared with 7.2% used in 2014-2015) in real terms before taxes.

**Resolution no. 645/2015/R/gas** approved the mandatory tariffs and the bimonthly equalisation prepayment amounts for the natural gas distribution and metering services for the year 2016.

**Resolution no. 704/2016/R/gas** adopted provisions on the recognition of costs relating to investments in natural gas distribution networks. In particular, the Authority confirmed the introduction of standard costs in the mechanism for the recognition of costs relating to investments in natural gas distribution networks starting with investments in 2018, with impacts on tariffs starting in 2019.

**Resolution no. 774/2016/R/gas** approved the mandatory tariffs and the bimonthly equalisation prepayment amounts for the natural gas distribution and metering services for the year 2017.

**Resolution no. 775/2016/R/gas** defined criteria for the infra-period updating, applicable for 2017-2019, of the gas distribution and metering services tariff regulation. The update, applicable as of 1 January 2017, regarded the rates of annual reduction of unit costs recognised to cover the operating costs of distribution, metering and marketing services (X-factor), the component covering costs deriving from mandatory periodic checking of converters (DCVER), the components covering centralised costs for the remote metering/remote management system and the costs of concentrators (t(tel) and t(con), respectively) and the standard costs to be applied to electronic metering units for capital cost recognition. In particular:

- with respect to the operating costs of the distribution and metering service, the Authority confirmed the productivity recovery targets, set at 1.7% and 0%, respectively;
- in relation to the operating costs of the marketing service, the Authority increased the unit cost recognised for the year 2017, setting it at €2.0/delivery point and confirmed the X-factor of 0%;
- in relation to the component covering costs relating to meter checks (DCVER), pending detailed investigations, the Authority established a provisional reduction for the year 2017 of the component's unit value, setting it at €50 per delivery point;
- in relation to the component covering centralised costs for the remote metering/remote management system t(tel) and the component covering the costs of concentrators t(con), the Authority established, also for the year 2017, the recognition of actual costs (with a ceiling on the tariff recognitions for costs incurred equal to €5.74 per delivery point at which a smart meter is operating);
- in relation to the recognition of investments in metering units of a class equal to or lower than G6 relating to the year 2016, the Authority confirmed the current system, recognising the actual costs incurred by the companies within the limits of 150% of the standard cost;
- in relation to standard costs for investments in metering units of a class equal to or lower than G6 for the year 2017, the Authority set a level of €135/metering unit for calibre G4 metering units and €170/metering unit for G6 calibre metering units.

Resolution no. **145/2017/R/gas** determined the final reference tariffs for gas distribution and metering services for 2016, calculated on the basis of the actual balance sheet figures for 2015.

Resolution no. **146/2017/R/gas** redetermined the reference tariffs for gas distribution and metering services for 2009-2015, on the basis of several requests for adjustment submitted by the distribution companies and received by 15 February 2017.

Resolution no. **220/2017/R/gas** determined the provisional reference tariffs for gas distribution and metering services for 2017 on the basis of the preliminary balance sheet figures for 2016, pursuant to Article 3, paragraph 2, letter a) of the Gas Distribution and Metering Service Tariff Regulation (RTDG).

Resolution no. **389/2017/R/gas** recognised operating costs for the natural gas metering service, relating to remote metering/remote management systems and concentrators for



the years 2011-2013, incurred by distribution companies that opted for the provision of services by third parties (buy type solution), in the case of installing their own systems and concentrators (make type solution).

Resolution no. **858/2017/R/gas** redetermined the reference tariffs for gas distribution and metering services for 2009-2016, on the basis of several requests for adjustment submitted by the distribution companies and received by 15 September 2017.

Resolution no. **859/2017/R/gas** approved the mandatory tariffs and the bimonthly equalisation prepayment amounts for the natural gas distribution and metering services, as well as the values of components to cover operating expense for the distribution service, metering service, marketing of distribution and metering services and the component to cover centralised capital costs for the year 2018.

Resolution no. **904/2017/R/gas** adopted provisions for the recognition of costs relating to metering activities on natural gas distribution networks and for the effective date for the application of investment measurement criteria based on standard costs. In particular:

in relation to the recognition methods for costs relating to remote reading/management systems and concentrator costs, the adoption of benchmark logics is deferred to the fifth regulatory period, envisaging that the recognition of costs for 2018 and 2019 essentially continues to apply the criteria currently envisaged, based on final figures that are capped. The cap, for 2017 set at €5.74 per delivery point fitted with smart meters, is reduced to €5.24 per delivery point fitted with smart meters for 2018 and to €4.74 for 2019, with the aim of gradual closure over six years of the existing gap with cost levels considered to be efficient, established at €2.74 per delivery point fitted with smart meters;

- as regards criteria for the definition of standard costs for gas metering units for 2018 and 2019, for classes G4 and G6 the standard cost values defined for 2017 are confirmed, whilst with reference to the sharing of higher/lower investment costs associated with smart meters, the weighted average standard cost and actual cost are adopted, with a 40% weighting for the standard cost and a 60% weighting for the actual cost;
- as regards the cost recognition methods for meter checks, for 2017 the value of €50 per delivery point for the  $\Delta CVER_{unit,t}$  component is confirmed as final. For 2018 and 2019 the recognition of a balancing amount is envisaged, deferring any recognition of costs on a standard basis to a subsequent phase, when accurate figures will be available on the costs incurred by companies for the checks to be performed in application of the provisions of Ministerial Decree no. 93/17;
- as regards deadlines for the minimum schedule of installation obligations envisaged in the Directives on the service start-up of gas metering units, the Authority has postponed the setting of specific targets until 2020 as a result of the measure to be adopted by the end of February 2018;
- as regards adjustment of the tariff recognition criteria that also takes into account the residual depreciation of traditional G4 and G6 metering units replaced with smart meters in accordance with the Directives on the service start-up of gas metering units, in the event of early disposal of meters that have not reached the end of their useful lives or which have changed as a result of successive regulatory amendments, the Authority intends to conduct further studies as necessary;



- as regards definition of the price list and the mechanism for recognising investments in natural gas distribution networks as standard costs, the Authority confirmed application starting from investments in 2019, with impacts on tariffs starting in 2020 as a result of a measure to be adopted by the end of November 2018.





## Comment on the economic and financial results

On 7 November 2016, 100% of the Italgas Reti equity investment was separated and transferred from Snam S.p.A. to Italgas S.p.A., a company established on 1 June 2016.



As of that date, Italgas therefore obtained direct control over Italgas Reti and indirect control over Napoletanagas (merged into Italgas Reti with effect from 1 October 2017) and ACAM Gas.

The reported 2017 Income Statement values are compared below with those for 2016, which includes Italgas balances from 1 June 2016 to 31 December 2016 and those of the operating companies from 7 November 2016 to 31 December 2016:

### RECLASSIFIED INCOME STATEMENT

(€ million)	1.6 - 31.12.2016	2017
Gas Distribution regulated revenue	184.1	<b>1,096.8</b>
Other revenues	12.0	<b>27.4</b>
<b>Total revenues (*)</b>	<b>196.1</b>	<b>1,124.2</b>
Operating costs (*)	(90.1)	<b>(348.0)</b>
<b>EBITDA</b>	<b>106.0</b>	<b>776.2</b>
Amortisation, depreciation and impairment	(76.8)	<b>(358.3)</b>
<b>EBIT</b>	<b>29.2</b>	<b>417.9</b>
Net financial expense	(122.8)	<b>(36.2)</b>
Net income from equity investments	3.1	<b>23.0</b>
<b>Pre-tax profit (loss)</b>	<b>(90.5)</b>	<b>404.7</b>
Income taxes	18.3	<b>(111.9)</b>
<b>Net profit (net loss) (**)</b>	<b>(72.2)</b>	<b>292.8</b>

(\*) Net of the effects of IFRIC 12 "Service concession arrangements" (€479.7 and €61.7 million in 2017 and in the period 1 June-31 December 2016, respectively) and of other items reported in the paragraph "Reconciliation between reclassified consolidated financial statements and the legally required financial statements" in this report.

(\*\*) Net profit (net loss) applies to Italgas.

To allow comparison between Italgas Group figures for 2017 and the corresponding values in 2016, the values and data from the previous year in reference to the conglomerate comprising Italgas S.p.A. since its incorporation (1 June 2016) and for Italgas Reti S.p.A., Napoletanagas S.p.A. and ACAM Gas S.p.A. from 1 January 2016, are illustrated and commented below.



(€ million)	2016	2017	Abs. change	Change %
Gas Distribution regulated revenue	1,051.3	<b>1,096.8</b>	45.5	4.3
Other revenues	26.6	<b>27.4</b>	0.8	3.0
<b>Total revenues (*)</b>	<b>1,077.9</b>	<b>1,124.2</b>	<b>46.3</b>	<b>4.3</b>
Adjusted operating costs (*)	(393.5)	<b>(343.0)</b>	50.5	(12.8)
<b>Adjusted EBITDA</b>	<b>684.4</b>	<b>781.2</b>	<b>96.8</b>	<b>14.1</b>
Amortisation, depreciation and impairment	(325.6)	<b>(358.3)</b>	(32.7)	10.0
<b>Adjusted EBIT</b>	<b>358.8</b>	<b>422.9</b>	<b>64.1</b>	<b>17.9</b>
Adjusted net financial expense	(48.4)	<b>(36.2)</b>	12.2	(25.2)
Net income from equity investments	20.2	<b>23.0</b>	2.8	13.9
<b>Adjusted pre-tax profit</b>	<b>330.6</b>	<b>409.7</b>	<b>79.1</b>	<b>23.9</b>
Adjusted income taxes	(109.5)	<b>(113.3)</b>	(3.8)	3.5
<b>Adjusted net profit (**)</b>	<b>221.1</b>	<b>296.4</b>	<b>75.3</b>	<b>34.0</b>

(\*) Net of the effects of IFRIC 12 "Service concession arrangements" (€479.6 and €315.5 million in 2017 and 2016, respectively) and of other items reported in the paragraph "Reconciliation between reclassified consolidated financial statements and the legally required financial statements" in this report.

(\*\*) Adjusted net profit applies to Italgas.

The **adjusted EBIT** achieved in 2017 was €422.9 million, up €64.1 million (+17.9%) on 2016. The increase is mainly due to: (i) higher revenue (+€46.3 million; +4.3%), (ii) lower adjusted operating costs (-€50.5 million; 12.8%) and (iii) higher amortisation, depreciation and impairment (+€32.7 million; +10%). The change in adjusted operating expense mainly derives from lower costs for services following the substantial decline in services received from Snam after the demerger (-€18 million), the higher labour costs (+€8.8 million), lower net provisions for risks and future expenses (-€18.3 million) and lower net costs relating to Energy Efficiency Certificates (-€14.7 million). Greater amortisation and depreciation is recorded, mainly as a result of the reduction in the useful life of traditional meters<sup>5</sup>, subject to the plan to replace them with smart meters as required by ARERA resolutions under the terms of the remote metering reading plan.

The **adjusted net profit** for 2017, amounting to €296.4 million, recorded an increase of €75.3 million compared to 2016, +34% as a result not only of the aforementioned increase in adjusted EBIT for €64.1 million, but also to: (i) lower adjusted net financial expense for €12.2 million mainly due to a decrease in expense associated with the financial debt and lower financial expense for the discounting of environmental provisions, and (ii) the higher

5 In line with the scheduled meter replacement plan, starting in the second half of 2016 the useful life of the meters included in the replacement project pursuant to AEEGSI Resolutions 631/13 and 554/15 was adjusted in order to complete the depreciation process in 2018. As regards 2017, the useful life of the meters to be replaced during the year was conventionally considered as at the end of the first half.

net income from equity investments (+€2.8 million)<sup>6</sup>. These factors were in part offset by higher income taxes (+€3.8 million), due primarily to the increase in the tax base for the year and partly offset by the decrease in the IRES rate from 27.5% to 24%.

## **RECONCILIATION OF EBIT AND THE REPORTED NET PROFIT WITH ADJUSTED EBIT AND ADJUSTED NET PROFIT**

Italgas' management assesses Group performance on the basis of alternative performance indicators<sup>7</sup> not envisaged by IFRS, obtained by excluding special items from EBIT and net profit.

The income components are classified as special items, if significant, when: (i) they result from non-recurring events or transactions or from transactions or events which do not occur frequently in the ordinary course of business; or (ii) they result from events or transactions which are not representative of the normal course of business.

The tax rate applied to the items excluded from the calculation of adjusted net profit is determined on the basis of the nature of each revenue item subject to exclusion. Adjusted EBIT and adjusted net profit are not provided for by either IFRS or other standard setters. These performance metrics allow for analysis of the business trends, making it easier to compare results. The NON-GAAP financial report must be considered complementary to and not replacing the reports prepared according to IFRS.

The items excluded from the calculation of the adjusted results are described below.

The income components classified as special items in 2017 referred to non-recurring staff leaving incentives (€5.0 million; €3.6 million net of tax).

With reference to 2016, the income components classified as special items referred to: (i) non-recurring staff leaving incentives (€14.8 million; €10.1 million net of tax); (ii) non-recurring costs related to the demerger and listing transaction (€8.0 million; €5.5 million net of tax); (iii) financial expenses resulting from the early repayment of loan contracts in effect with the former parent company Snam (€119.0 million euro; €86.2 million net of tax).

<sup>6</sup> In particular, the change essentially concerns the restatement of deferred taxes relating to extraordinary transactions carried out in previous years (€2.7 million).

<sup>7</sup> For the definition of alternative performance indicators, reference should be made to the chapter "NON-GAAP Measures" in this report.

(€ million)	2016	2017
<b>Reported EBIT</b>	<b>336.0</b>	<b>417.9</b>
Excluding special items	22.8	5.0
<b>Adjusted EBIT</b>	<b>358.8</b>	<b>422.9</b>
Net financial expense	(167.4)	<b>(36.2)</b>
- of which special items	119.0	
Net income from equity investments	20.2	<b>23.0</b>
Income taxes	(69.6)	<b>(111.9)</b>
- of which special items	(39.9)	<b>(1.4)</b>
<b>Reported net profit (loss)</b>	<b>119.2</b>	<b>292.8</b>
Excluding special items		
- financial expense from early settlement of loans (*)	86.3	
- expense for staff leaving incentives (*)	10.2	<b>3.6</b>
- demerger and listing costs (*)	5.5	
<b>Adjusted net profit</b>	<b>221.2</b>	<b>296.4</b>

(\*) Net of the related tax effect.



## ANALYSIS OF THE RECLASSIFIED INCOME STATEMENT ITEMS

### TOTAL REVENUE

(€ million)	2016	2017	Abs. change	Change %
Distribution revenue	974.8	<b>996.9</b>	22.1	2.3
Other gas distribution regulated revenue	76.5	<b>99.9</b>	23.4	30.6
<b>Total gas distribution regulated revenue</b>	<b>1,051.3</b>	<b>1,096.8</b>	<b>45.5</b>	<b>4.3</b>
<b>Other revenues</b>	<b>26.6</b>	<b>27.4</b>	<b>0.8</b>	<b>3.1</b>
	<b>1,077.9</b>	<b>1,124.2</b>	<b>46.3</b>	<b>4.3</b>

**Total revenue** for 2017 stood at €1,124.2 million, an increase of €46.3 million compared with 2016. It refers to the gas distribution regulated revenue (€1,096.8 million) and other revenues (€27.4 million).



The gas distribution regulated revenue increased by €45.5 million and was the result of: (i) increased distribution revenue (+€22.1 million; +2.3%) due to the tariff components (+€10.6 million) and tariff adjustments relating to previous years (+€11.5 million), (ii) higher gas distribution regulated revenue (+€23.4 million; +30.7%), mainly due to the increase in the contribution pursuant to Article 57 of ARERA Resolution 367/14 (+€18.9 million), in relation to the investment plan to replace traditional meters with electronic smart meters, as set out in the remote metering project pursuant to ARERA Resolutions 631/13 and 554/15, as well as higher revenue for accessory network services and other regulated revenue (+€4.6 million; +9.7% on 2016).

Other revenue of €27.4 million refers essentially to water services, third-party services and rental income.

#### OPERATING COSTS

(€ million)	2016	2017	Abs. change	Change %
<b>Fixed gas distribution costs</b>	<b>283.3</b>	<b>267.2</b>	<b>(16.1)</b>	<b>(5.7)</b>
of which:				
- <i>personnel costs</i>	130.3	139.1	8.8	(6.8)
- <i>net external costs</i>	153.0	128.1	(24.9)	(16.3)
- <i>of which special items</i>	8.0		8.0	
<b>Adjusted fixed gas distribution costs</b>	<b>275.3</b>	<b>267.2</b>	<b>(8.1)</b>	<b>(2.9)</b>
<b>Variable gas distribution costs</b>	<b>4.7</b>	<b>3.4</b>	<b>(1.3)</b>	<b>(27.7)</b>
<b>Other gas distribution costs</b>	<b>104.4</b>	<b>67.2</b>	<b>(37.2)</b>	<b>(35.6)</b>
- <i>of which special items</i>	14.8	5.0	(9.8)	(66.2)
<b>Adjusted other gas distribution costs</b>	<b>89.6</b>	<b>62.2</b>	<b>(27.4)</b>	<b>(30.6)</b>
<b>Total gas distribution costs</b>	<b>369.6</b>	<b>332.8</b>	<b>(36.8)</b>	<b>(10.0)</b>
Other business costs	23.9	10.2	(13.7)	(57.3)
<b>Operating costs</b>	<b>416.3</b>	<b>348.0</b>	<b>(68.3)</b>	<b>(16.4)</b>
<b>Adjusted operating costs</b>	<b>393.5</b>	<b>343.0</b>	<b>(50.5)</b>	<b>(12.8)</b>

**Adjusted fixed costs for gas distribution**, consisting of the sum of personnel costs and external costs, amounted to €267.2 million as at 31 December 2017, down €8.1 million compared with 2016 (€275.3 million) as a result mainly of a reduction in costs for services linked to the Snam service contract (-€18 million), offset in part by higher net personnel costs (+€8.8 million) mainly associated with the insourcing of technical and staffing activities, and to higher costs for maintenance (+€7.2 million).

Compared to the adjusted figures, the fixed gas distribution costs (€267.2 million, down €16.1 million on 2016) do not include non-recurring costs incurred in 2016 in association with the demerger and with listing of the company (-€8 million).

**Adjusted other gas distribution costs** totalled €62.2 million, including €53.2 million relating to concession fees. The €27.4 million decrease compared with the previous year was due to lower net costs relating to Energy Efficiency Certificates (-€14.7 million) and reduced net provisions for risks and future expenses (-€10.2 million). The provisions for risks and charges include, amongst other things, a provision allocated in 2017 of €16 million for probably future charges relating to the return to full function of a number of smart meters installed from 2014 onwards.

Compared to the adjusted figures, the other costs (€67.2 million, down €37.2 million on 2016) do not include non-recurring staff leaving incentives (€5.0 million in 2017 and €14.8 million in 2016).

The **other business costs** amounted to €10.2 million, of which €8.6 million relating to external costs and €1.6 million to personnel costs. These costs decreased by €13.7 million, mainly due to lower provisions for environmental liabilities (-€8.1 million).

#### AMORTISATION, DEPRECIATION AND IMPAIRMENT

(€ million)	2016	2017	Abs. change	Change %
<b>Total amortisation and depreciation</b>	<b>325.6</b>	<b>352.0</b>	<b>26.4</b>	<b>8.1</b>
Intangible assets IFRIC12	280.2	<b>295.2</b>	15.0	5.4
- of which, metering	97.3	<b>118.2</b>	20.9	21.5
Intangible assets	28.1	<b>40.5</b>	12.4	44.1
Property, plant and equipment	17.3	<b>16.3</b>	(1.0)	(5.8)
<b>Impairment</b>		<b>6.3</b>	<b>6.3</b>	
	<b>325.6</b>	<b>358.3</b>	<b>32.7</b>	<b>10.0</b>



**Amortisation, depreciation and impairment** (€358.3 million) increased by €32.7 million, or 10.0%, compared with 2016. This growth was due primarily to greater depreciation as a result of the reduced useful life of traditional meters<sup>8</sup>, subject to the plan to replace them with electronic meters (smart meters), required by ARERA Resolutions under the scope of the implementation of the remote metering plan. Impairment totalled €6.3 million and relates essentially to metering.

#### NET FINANCIAL EXPENSE

(€ million)	2016	2017	Abs. change	Change %
<b>Expense (income) on short-term and long-term financial debt</b>	<b>159.1</b>	<b>28.8</b>	<b>(130.3)</b>	<b>(81.9)</b>
of which:				
- <i>special items</i>	119.0		(119.0)	
<b>Expenses (income) on adjusted financial debt</b>	<b>40.1</b>	<b>28.8</b>	<b>(11.3)</b>	<b>(28.2)</b>
<b>Other net financial expense (income)</b>	<b>8.9</b>	<b>7.5</b>	<b>(1.4)</b>	<b>(15.6)</b>
Upfront fees and other commissions	2.3	7.2	(15.6)	215.2
- Expenses (income) related to the discounting of environmental provisions and provisions for employee benefits	6.7	1.8	(4.9)	(73.1)
- Other expense (income)	(0.1)	(1.5)	(1.4)	
<b>Financial expense capitalised</b>	<b>(0.6)</b>	<b>(0.1)</b>	<b>0.5</b>	<b>(83.3)</b>
<b>Net financial expense</b>	<b>167.4</b>	<b>36.2</b>	<b>(131.2)</b>	<b>(78.4)</b>
<b>Adjusted net financial expense</b>	<b>48.4</b>	<b>36.2</b>	<b>(12.2)</b>	<b>(25.2)</b>

<sup>8</sup> In line with the scheduled meter replacement plan, starting in the second half of 2016 the useful life of the meters included in the replacement project pursuant to AEEGSI Resolutions 631/13 and 554/15 was adjusted in order to complete the depreciation process in 2018. As regards 2017, the useful life of the meters to be replaced during the year was conventionally considered in the first half-year.

The **adjusted net financial expense** (€36.2 million) reduced by €12.2 million compared to 2016 mainly due to: (i) lower expense associated with debt (€11.3 million) following the decrease in the average borrowing costs, partly offset by the higher average debt; (ii) increased upfront fees (€5.0 million) due mainly to bank fees and commissions paid in 2016 for the Bridge to Bond loan repaid in full in 2017 and to the 2017 portion of expense relating to bond placements during the year; (iii) lower financial expense associated with the discounting of environmental provisions and employee benefits (€4.9 million).

In the adjusted figures, the net financial expense for 2016 does not include expense incurred during the year from the early extinguishment of loan agreements payable to the former parent company Snam (€119.0 million).

**Net income from equity investments**, equal to €23.0 million in 2017 (€20.2 million in 2016), mainly regards the portions attributable to the group of the net income for the period of companies measured with the equity method and refers in particular to Toscana Energia<sup>9</sup>.

#### INCOME TAXES

(€ million)	2016	2017	Abs. change	Change %
<b>Current taxes</b>	<b>119.3</b>	<b>131.5</b>	<b>12.2</b>	<b>10.2</b>
Deferred taxes	(33.6)	<b>(34.3)</b>	(0.7)	2.1
Prepaid taxes	(16.1)	14.7	30.8	
<b>(Prepaid) Deferred taxes</b>	<b>(49.7)</b>	<b>(19.6)</b>	<b>30.1</b>	<b>(60.6)</b>
<b>Income taxes</b>	<b>69.6</b>	<b>111.9</b>	<b>42.3</b>	<b>60.8</b>
<b>- Adjustments for special items</b>	<b>40</b>	<b>1.4</b>	<b>(38.6)</b>	
<b>Adjusted income taxes</b>	<b>109.5</b>	<b>113.3</b>	<b>3.8</b>	<b>3.5</b>
<b>Tax rate (%)</b>	<b>36.9%</b>	<b>27.7%</b>		
<b>Adjusted tax rate (%)</b>	<b>33.1%</b>	<b>27.7%</b>		

The **adjusted income taxes for 2017** (€13.3 million) rose by €3.8 million compared to the corresponding value for the previous year, mainly as a result of the increase in gross profit and changes in current taxes accrued in previous years, mitigated by the decrease in the IRES tax rate from 27.5% (applied in 2016) to 24% (in 2017) and the adjustments to deferred taxes carried out in 2016 and 2017.

<sup>9</sup> Specifically, the change essentially concerns the restatement of deferred taxes relating to extraordinary transactions carried out in previous years (€2.7 million).

The adjusted tax rate was 27.7% (33.1% in 2016). The reconciliation of the theoretical tax rate with the effective tax rate is described in the note "Income taxes" in the Notes to the consolidated financial statements.

## RECLASSIFIED STATEMENT OF FINANCIAL POSITION

The Reclassified Statement of Financial Position combines the assets and liabilities of the mandatory format included in the Annual Report based on the criterion of how the business operates, conventionally split into the three basic functions of investment, operations and financing.

The statement provided represents useful information for the investor because it makes it possible to identify the sources of financial resources (own and third-party funds) and uses of financial resources in fixed and working capital.

The Italgas Reclassified Statement of Financial Position as at 31 December 2017, compared with that as at 31 December 2016, is summarised below:

(€ million)	31.12.2016	31.12.2017	Abs. change
<b>Fixed capital</b>	<b>4,792.8</b>	<b>4,950.9</b>	<b>158.1</b>
Property, plant and equipment	227.5	<b>224.6</b>	(2.9)
Intangible assets	4,486.5	<b>4,676.6</b>	190.1
Equity investments	175.8	<b>184.9</b>	9.1
Financial receivables and securities instrumental to operations	0.1	<b>0.1</b>	0.0
Net payables for investments	(97.1)	<b>(135.3)</b>	(38.2)
Net working capital	(9.5)	<b>71.1</b>	80.6
<b>Provisions for employee benefits</b>	<b>(120.6)</b>	<b>(116.1)</b>	<b>4.5</b>
<b>Assets held for sale and directly related liabilities</b>	<b>19.0</b>		<b>(19.0)</b>
<b>NET INVESTED CAPITAL</b>	<b>4,681.7</b>	<b>4,905.9</b>	<b>224.2</b>
<b>Shareholders' equity (including minority interests)</b>			
- attributable to the Group	1,063.4	<b>1,185.6</b>	122.2
- attributable to minority interests	0.9		(0.9)
	<b>1,064.3</b>	<b>1,185.6</b>	<b>121.3</b>
<b>Net financial debt</b>	<b>3,617.4</b>	<b>3,720.3</b>	<b>102.9</b>
<b>COVERAGE</b>	<b>4,681.7</b>	<b>4,905.9</b>	<b>224.2</b>

The **net invested capital** as at 31 December 2017 amounts to €4,905.9 million and consists of the items discussed below.

**Fixed capital** (€4,950.9 million) rose by €158.1 million compared with 31 December 2016 essentially due to the increase in intangible assets (+€190.1 million), in part offset by the increase in net financial payables relating to investment activities (-€38.2 million) and the reduction in property, plant and equipment (-€2.9 million).

**Property, plant and equipment and intangible assets** amount to €4,901.2 million. Intangible assets include service concessions accounted for pursuant to IFRIC 12 under the item intangible assets (€4,563.6 million). Property, plant and equipment regards primarily buildings (€174.2 million) and industrial and commercial equipment (€32.1 million).

An analysis of the changes in **Property, plant and equipment** and **Intangible assets** is provided below:

(€ million)

	Property, plant and equipment	IFRIC 12 assets	Intangible assets	Total
<b>Balance as at 31 December 2016</b>	<b>227.5</b>	<b>4,364.2</b>	<b>122.3</b>	<b>4,714.0</b>
Investments	10.9	479.5	31.5	<b>521.9</b>
Amortisation, depreciation and impairment	(16.3)	(295.2)	(46.8)	<b>(358.3)</b>
Change in the scope of consolidation		60.0		<b>60.0</b>
Transfers, eliminations and divestments		(8)		<b>(7.8)</b>
Grants		(28.5)		<b>(28.5)</b>
Other changes	2.5	0.9	(3.5)	<b>(0.1)</b>
<b>Balance as at 31 December 2017</b>	<b>224.6</b>	<b>4,568.9</b>	<b>107.7</b>	<b>4,901.2</b>

Investments in 2017, equal to €521.9 million, mainly refer to the replacement of meters and the placement/replacement of gas networks.

The item **Equity investments** (€184.9 million) includes the measurement of equity investments with the equity method and refers to Toscana Energia (€182.4 million), Umbria Distribuzione Gas (€1.4 million) and Metano Sant'Angelo Lodigiano (€1.1 million).

Consolidated **net working capital** as at 31 December 2017 amounts to €71.1 million and is broken down as follows:

(€ million)	31.12.2016	31.12.2017	Abs. change
Trade receivables	417.6	<b>406.5</b>	(11.1)
Inventories	32.6	<b>22.4</b>	(10.2)
Tax receivables	53.5	<b>45.2</b>	(8.3)
Accruals and deferrals from regulated activities	33.3	<b>78.5</b>	45.2
Other assets	149.1	<b>197.3</b>	48.2
Trade payables	(174.5)	<b>(184.1)</b>	(9.6)
Provisions for risks and charges	(230.5)	<b>(208.3)</b>	22.2
Deferred tax liabilities	(106.3)	<b>(94.8)</b>	11.5
Net tax payables	(13.5)	<b>(15.9)</b>	(2.4)
Other liabilities	(170.8)	<b>(175.7)</b>	(4.9)
	<b>(9.5)</b>	<b>71.1</b>	<b>80.6</b>

Compared to 31 December 2016, the change of +€80.6 million in working capital mainly derives from the algebraic sum of the following: (i) the increase in accruals and deferrals from regulated activities (+€45.2 million) associated with the tariff recognition estimated in accordance with current regulations regarding the plan to replace traditional meters with smart meters; (ii) the increase in other current assets (+€48.2 million) deriving mainly from the higher receivables from the CSEA connected to Energy Efficiency Certificates (€53.8 million) and the decrease in accruals and deferrals (-€4.1 million); (iii) the increase in trade payables (+€9.6 million) particularly for payables to suppliers and to the CSEA, (iv) the decrease in trade receivables (-€11.1 million) particularly in relation to lower receivables from gas sales companies (-€23.1 million), partly offset by the higher receivables due from the CSEA (+€9.5 million); (v) lower inventories (-€10.2 million) in relation to higher withdrawals connected to the gas meter replacement plan; (vi) the reduced balance of tax items (-€0.8 million) due in particular to the decrease in net deferred taxes; (vii) lower provisions for risks and charges (-€22.2 million).



Note that the Company has finalised factoring agreements with financial counterparties on the basis of which the Company's receivables can be factored without recourse. Specifically, during the year a number of factoring transactions were completed of receivables associated with 2017 revenue: (i) trade receivables for a total of €115.5 million and (ii) relating to White Certificates for €138.6 million.

Tax receivables for a total of €24.6 million were also factored without recourse.

**Assets held for sale and directly related liabilities** reduced as a result of the sale of a property complex with a book value of €19 million (net of environmental provisions for charges relating to reclamation work on the property)<sup>10</sup>.

#### STATEMENT OF COMPREHENSIVE INCOME

(€ million)	2017
<b>Net profit</b>	<b>292.8</b>
<b>Other components of comprehensive income</b>	
<i>Components not reclassifiable to the income statement:</i>	
Actuarial gains (losses) from remeasurement of defined benefit plans for employees	(1.5)
Tax effect	0.4
	(1.0)
<b>Total other components of comprehensive income, net of tax effect</b>	
<b>Total comprehensive income for the year</b>	<b>291.7</b>
<b>Attributable to:</b>	
- Italgas	291.7
- Minority interests	

<sup>10</sup> At the time of the Snam demerger, Italgas Reti retained rights and obligations relating to the property complex located in Via Ostiense in Rome property complex deriving from specific contractual agreements within the context of the disposal of the entire share capital of Italgas Reti S.p.A. from Eni to Snam in 2009. The rights and obligations regarding the price adjustment, on the other hand, were transferred from Snam to Italgas.

## SHAREHOLDERS' EQUITY

(€ million)

<b>Shareholders' equity as at 31 December 2016</b>	<b>1,064.3</b>
<i>Increase for:</i>	
- 2017 comprehensive income	291.7
	1,356
<i>Decrease for:</i>	
- 2016 dividend distribution	(161.8)
- Other changes	(8.5)
	<b>1,185.6</b>
<b>Shareholders' equity as at 31 December 2017</b>	<b>1,185.6</b>
<i>attributable to:</i>	
- Italgas	<b>1,185.6</b>

## NET FINANCIAL DEBT

(€ million)	31.12.2016	31.12.2017	Abs. change
<b>Financial and bond debt</b>	<b>3,619.0</b>	<b>3,723.2</b>	<b>104.2</b>
Short-term financial debt <sup>(*)</sup>	2,696.0	106.1	(2,589.9)
Long-term financial debt	923.0	3,617.1	2,694.1
<b>Financial receivables and cash and cash equivalents</b>	<b>(1.6)</b>	<b>(2.9)</b>	<b>(1.3)</b>
Cash and cash equivalents	(1.5)	(2.8)	(1.3)
Securities not instrumental to operations	(0.1)	(0.1)	
	<b>3,617.4</b>	<b>3,720.3</b>	<b>102.9</b>

(\*) Includes the short-term portion of long-term financial debt.

**Net financial debt** was €3,720.3 million as at 31 December 2017, up €102.9 million (€3,617.4 million as at 31 December 2016).

Financial payables and bonds as at 31 December 2017, totalling €3,723.2 million (€3,619.0 million as at 31 December 2016) were denominated entirely in euros and referred to bonds (€2,651.9 million), payables to banks (€287.8 million) and loan agreements concerning European Investment Bank (EIB) funding (€783.5 million).



The increase in financial payables and bonds of €104.2 million derives from the increase in long-term financial payables (€2,694.1 million) resulting from: (i) the issue of bond loans for a total value of €2,650 million with the following characteristics: nominal €1,500 million issued on 19 January 2017 and divided into two tranches, one 5-year and one 10-year, both fixed rate, for a total of €750 million each and annual coupons of 0.50% and 1.625%, respectively; nominal €650 million issued on 14 March 2017, maturing 14 March 2024 and with a fixed rate annual coupon of 1.125%; nominal €500 million on 18 September 2017, maturing 18 January 2029, with a fixed rate annual coupon of 1.625%; (ii) a new loan agreed with the EIB, disbursed on 28 December 2017 for €360 million, with same-time settlement of an EIB loan for €300 million; (iii) the inclusion of Enerco Distribuzione in the scope of consolidation from 6 December 2017, which increased the gross financial debt by a total of €12.0 million. This increase was partly offset by the reduction in short-term financial debt (-€2,589.9 million) mainly attributable to the settlement of a bridge to bond syndicate loan for an original amount of €2,300 million, associated with the aforementioned bond loan issues and to less use of the bank credit facilities (-€321.2 million).

The breakdown of debt by type of interest rate as at 31 December 2017 is as follows

(€ million)	31.12.2016	%	31.12.2017	%
Fixed rate			<b>2,651.9</b>	<b>71.2</b>
Floating rate	3,619.0	100.0	<b>1,071.3</b>	28.8
	<b>3,619.0</b>	<b>100.0</b>	<b>3,723.2</b>	<b>100.0</b>

Fixed rate financial liabilities stood at €2,651.9 million and refer to the issue of bond loans.

Floating rate financial liabilities totalled €1,071.3 million and fell by €2,547.7 million compared with 31 December 2016 mainly as a result of the above-mentioned issue of bond loans which replaced short-term bank loans.





Italgas, as at 31 December 2017, had unused committed long-term credit lines amounting to €1.1 billion.

As at 31 December 2017, there were no financial covenants and collateralised bilateral and syndicated loan agreements in place with banks and other financial institutions. Some of these contracts provide, *inter alia*, for the following: (i) negative pledge commitments pursuant to which Italgas and its subsidiaries are subject to limitations on pledging real property rights or other restrictions on all or part of the respective assets, shares or merchandise; (ii) *pari passu* and change-of-control clauses; and (iii) limitations on certain extraordinary transactions that the Company and its subsidiaries may carry out. These commitments were satisfied as at 31 December 2017.

## RECLASSIFIED STATEMENT OF CASH FLOWS

The reclassified statement of cash flows provided below is the summary of the legally required cash flow statement. The reclassified statement of cash flows makes it possible to reconcile the change in cash and cash equivalents at the start and end of the period with the change in net financial debt at the start and end of the period. The measure which allows for the reconciliation between the two statements is the free cash flow<sup>11</sup>, i.e. the cash surplus or deficit remaining after the financing of investments.

11 The free cash flow alternatively represents: (i) the change in cash for the period, after the addition/subtraction of cash flows relating to financial payables/receivables (usage/repayment of financial receivables/payables) and equity (payment of dividends/capital contributions); (ii) the change in net financial debt for the period, after the addition/subtraction of flows of debt relating to equity (payment of dividends/capital contributions).

(€ million)	2016	2017
<b>Net profit</b>	<b>119.2</b>	<b>292.8</b>
Adjusted:		
- Amortisation, depreciation and other non-monetary components	305.4	<b>335.3</b>
- Net capital losses (capital gains) on asset sales and eliminations	10.9	<b>4.1</b>
- Interest and income taxes	228.4	<b>141.5</b>
Change in working capital due to operating activities	(5.2)	<b>(105.7)</b>
Dividends, interest and income taxes collected (paid)	(287.3)	<b>(118.6)</b>
<b>Net cash flow from operating activities</b>	<b>371.4</b>	<b>549.4</b>
Technical investments	(349.5)	<b>(493.3)</b>
Disinvestments		<b>22.4</b>
Other changes relating to investment activities	(13.5)	<b>30.7</b>
<b>Free cash flow before M&amp;A transactions</b>	<b>8.4</b>	<b>109.2</b>
Change in scope of consolidation	(1,503.0)	<b>(38.7)</b>
of which:		
<i>price paid for equity</i>		<b>(35.9)</b>
<i>takeover of payables of acquired companies</i>		<b>(2.8)</b>
<b>Free cash flow</b>	<b>(1,494.6)</b>	<b>70.5</b>
Change in short- and long-term financial debt (*)	1,770.0	<b>92.6</b>
Equity cash flow	(275.0)	<b>(161.8)</b>
<b>Net cash flow for the year</b>	<b>0.4</b>	<b>1.3</b>

\* Includes the net financial debt of the companies acquired.



## CHANGE IN NET FINANCIAL DEBT

(€ million)	2016	2017
<b>Free cash flow before M&amp;A transactions</b>	<b>8.4</b>	<b>109.2</b>
Change due to acquisitions of equity investments (*)	(1,847.8)	<b>(50.3)</b>
<i>Equity cash flow</i>	<b>(275.0)</b>	<b>(161.8)</b>
<i>Change in net financial debt</i>	<b>(2,114.4)</b>	<b>(102.9)</b>

(\*) Includes the net financial debt of the companies acquired.

The net cash flow from operations in 2017 amounted to €549.4 million which completely covered the funding of net investments, equal to €440.1 million, generating a free cash flow before Merger and Acquisition transactions of €109.2 million, which partly covered the cash flow of equity of -€161.8 million (dividend paid). The increase in net financial debt was €102.9 million, including the effect deriving from the change in the scope of consolidation (€50.3 million) following the inclusion from 6 December 2017 of the subsidiary Enerco Distribuzione S.p.A.



## Comment on the economic and financial results of Italgas S.p.A.

Italgas S.p.A. was incorporated on 1 June 2016 and listed on the Milan Stock Exchange from 7 November 2016. Italgas S.p.A. is responsible for the strategic planning, management, coordination and control of its 100% subsidiaries Italgas Reti S.p.A., ACAM Gas S.p.A., Enerco Distribuzione S.p.A. and S.G.S. S.r.l.



### RECLASSIFIED INCOME STATEMENT

In view of Italgas S.p.A.'s nature as an industrial investment holding, the following reclassified Income Statement has been prepared, which inverts the order of the income statement items under Leg. Decree 127/91, presenting first those which relate to the financial operations, as this is the most significant income component for those companies<sup>12</sup>.

(€ million)	1.6.2016-31.12.2016	2017	Abs. change	Var. %
<b>Financial income and expense</b>				
Income from equity investments	190.0	<b>197.4</b>	7.4	3.9
Interest income	2.0	<b>21.8</b>	19.8	
Interest expense and other financial expense	(4.5)	<b>(36.1)</b>	(31.6)	
<b>Total financial income and expense</b>	<b>187.5</b>	<b>183.1</b>	<b>(4.4)</b>	<b>(2.3)</b>
Revenue from services	7.7	<b>64.5</b>	56.8	
Other income		<b>0.4</b>	0.4	
<b>Other operating income</b>	<b>7.7</b>	<b>64.9</b>	<b>57.2</b>	
<b>Other operating expenses</b>				
For personnel	(6.1)	<b>(41.8)</b>	(35.7)	
For non-financial services and other costs	(12.6)	<b>(36.3)</b>	(23.7)	
<b>Total other operating expenses</b>	<b>(18.7)</b>	<b>(78.1)</b>	<b>(59.4)</b>	
<b>Pre-tax profit</b>	<b>176.5</b>	<b>169.9</b>	<b>(6.6)</b>	<b>(3.7)</b>
<b>Income taxes</b>	<b>0.6</b>	<b>4.3</b>	<b>3.7</b>	
<b>Net profit</b>	<b>177.1</b>	<b>174.2</b>	<b>(2.9)</b>	<b>(1.6)</b>

The **net profit** for 2017 amounted to €174.2 million, down by €2.9 million compared to the period between the company's date of incorporation (1 June 2016) and 31 December 2016.

<sup>12</sup> See Consob Communication 94001437 of 23 February 1994.



## ANALYSIS OF THE RECLASSIFIED INCOME STATEMENT ITEMS

### Financial income and expense

(€ million)	1.6.2016-31.12.2016	2017	Abs. change	Var. %
Income from equity investments	190.0	<b>197.4</b>	7.4	3.9
Interest income	2.0	<b>21.8</b>	19.8	
Interest expense and other financial expense	(4.5)	<b>(36.1)</b>	(31.6)	
	187.5	<b>183.1</b>	(4.4)	(2.3)

Income from equity investments (€197.4 million) consists of the dividends paid by the subsidiary Italgas Reti.

Interest income (€21.8 million) essentially relates to interest income from the intragroup loans granted by Italgas to its subsidiaries.

Interest expense and other financial expense (€36.1 million) mainly refers to the costs relating to financial debt, and concerns bond loan expense<sup>13</sup> (€26.0 million) and loans from banks (€9.8 million).

### Other operating income

Other operating income (€64.9 million) refers to chargebacks to subsidiaries of costs incurred for the provision of services centrally managed by Italgas S.p.A. These services are governed by contracts stipulated between Italgas S.p.A. and its subsidiaries and concern the following areas: ICT, personnel and organisation, planning, administration, finance and control, general services, property and security services, legal and corporate affairs and compliance, health, safety and environment, regulation, external relations and communication, internal audit and Enterprise Risk Management (ERM).

### Other operating expenses

(€ million)	1.6.2016-31.12.2016	2017	Abs. change
For personnel	<b>(6.1)</b>	<b>(41.8)</b>	(35.7)
For non-financial services and other costs	<b>(12.6)</b>	<b>(36.3)</b>	(23.7)
<b>Total other operating expenses</b>	<b>(18.7)</b>	<b>(78.1)</b>	<b>(59.4)</b>

<sup>13</sup> The details of bond issues during the year and related terms are provided in the note "Short-term financial liabilities, long-term financial liabilities and short-term portions of long-term financial liabilities" in the Notes to the financial statements.

Other operating expenses (€78.1 million) refer to personnel costs (€41.8 million) and costs for non-financial services and other costs (€36.3 million). The latter include costs for services provided by Snam S.p.A. (€13.1 million) and costs for consultancy and professional services (€10.1 million).

## RECLASSIFIED STATEMENT OF FINANCIAL POSITION<sup>14</sup>

(€ million)	31.12.2016	31.12.2017	Abs. change
<b>Fixed capital</b>	<b>3,690.4</b>	<b>5,209.1</b>	<b>1,518.7</b>
Property, plant and equipment	0.4	1.9	1.5
Equity investments	2,966.7	2,974.2	7.5
Financial receivables instrumental to operations	723.3	2,240.8	1,517.5
Net receivables (payables) relating to investment activities		(7.8)	(7.8)
<b>Net working capital</b>	<b>13.0</b>	<b>4.0</b>	<b>(9.0)</b>
<b>Provisions for employee benefits</b>	<b>(4.9)</b>	<b>(6.5)</b>	<b>(1.6)</b>
<b>NET INVESTED CAPITAL</b>	<b>3,698.5</b>	<b>5,206.6</b>	<b>1,508.1</b>
<b>Shareholders' equity</b>	<b>1,640.7</b>	<b>1,653.2</b>	<b>12.5</b>
<b>Net financial debt</b>	<b>2,057.8</b>	<b>3,553.4</b>	<b>1,495.6</b>
<b>COVERAGE</b>	<b>3,698.5</b>	<b>5,206.6</b>	<b>1,508.1</b>

The **Fixed capital** amounted to €5,209.1 million, up by €1,518.7 million compared to 31 December 2016 principally as a result of higher financial receivables instrumental to operations from subsidiaries (€1,517.5 million).

<sup>14</sup> Please see the "NON-GAAP Measures" section of this report for an illustration of methods adopted for the reclassified financial statements.



The €2,974.2 million in **Equity investments** relate to the equity held in Italgas Reti. The €7.5 million increase compared to 31 December 2016 is the result of the balance of payments recognised to Eni from the sale of the property complex in Via Ostiense in Rome following the application of contractual commitments made by Snam and Eni at the time of Snam's purchase of Italgas Reti (then Italgas S.p.A.) in 2009. These commitments were transferred to Italgas with the demerger in 2016.

#### NET WORKING CAPITAL

(€ million)	31.12.2016	31.12.2017	Abs. change <sup>a</sup>
Tax receivables	28.8	<b>6.1</b>	(22.7)
Trade receivables	8.7	<b>21.6</b>	12.9
Other assets	12.8	<b>5.2</b>	(7.6)
Trade payables	(15.6)	<b>(16.1)</b>	(0.5)
Tax payables	(17.1)	<b>(4.5)</b>	12.6
Deferred tax assets		<b>2.3</b>	2.3
Provisions for risks and charges	(1.2)	<b>(2.2)</b>	(1.0)
Other liabilities	(3.4)	<b>(8.4)</b>	(5.0)
	<b>13.0</b>	<b>4.0</b>	<b>(9.0)</b>

The **Net working capital** (€4.0 million) reduced by €9.0 million compared to 31 December 2016 mainly as a result of: (i) the decrease in tax receivables (-€22.7 million) due to lower receivables from subsidiaries for the National Tax Consolidation (-€16.4 million); (ii) the decline in other assets (-€7.6 million) due mainly to reversal to the income statement of prepayments relating to upfront fees on the revolving credit lines (-€4.2 million). These effects were partly offset by the lower tax payables (-€12.6 million) resulting from changes in the tax payments on account and the increase in trade receivables (+€12.9 million) due to the increase in services provided to the subsidiaries.

## NET FINANCIAL DEBT

(€ million)	31.12.2016	31.12.2017	Abs. change
<b>Financial and bond debt</b>	<b>3,619.0</b>	<b>3,711.8</b>	<b>92.8</b>
Short-term financial debt <sup>(*)</sup>	2,696.0	<b>99.9</b>	(2,596.1)
Long-term financial debt	923.0	<b>3,611.9</b>	2,688.9
<b>Financial receivables non-instrumental to operations and cash and cash equivalents</b>	<b>(1,561.2)</b>	<b>(158.3)</b>	<b>1,402.9</b>
Financial receivables non-instrumental to operations	(1,561.2)	<b>(158.2)</b>	1,403.0
Cash and cash equivalents		<b>(0.1)</b>	(0.1)
	<b>2,057.8</b>	<b>3,553.5</b>	<b>1,495.7</b>

(\*) Includes the short-term portion of long-term financial debt.

**Net financial debt** was €3,553.5 million as at 31 December 2017, up €1,495.7 million compared to 31 December 2016 (€2,057.8 million).

Financial payables and bonds as at 31 December 2017, totalling €3,711.8 million (€3,619.0 million as at 31 December 2016) were denominated entirely in euros and referred to bonds (€2,651.9 million), payables to banks (€276.4 million) and loan agreements concerning European Investment Bank (EIB) funding (€783.5 million).

The increase of €1,495.7 million is mainly due to the increase in long-term financial payables and bonds (€2,688.9 million) resulting from: (i) the issue of bond loans for a total value of €2,650 million with the following characteristics: nominal €1,500 million issued on 19 January 2017 and divided into two tranches, one 5-year and one 10-year, both fixed rate, for a total of €750 million each and annual coupons of 0.50% and 1.625%, respectively; nominal €650 million issued on 14 March 2017, maturing 14 March 2024 and with a fixed rate annual coupon of 1.125%; nominal €500 million on 18 September 2017, maturing 18 January 2029, with a fixed rate annual coupon of 1.625%; (ii) a new loan agreed with the EIB, disbursed on 28 December 2017 for €360 million, with same-time early settlement of an EIB loan for €300 million. This increase was partly offset by the reduction in short-term financial debt (-€2,595.1 million) mainly attributable to the settlement of a bridge to bond syndicated loan for an original amount of €2,300.0 million and less net usage of short-term bank credit facilities for €319.5 million.

The financial receivables non-instrumental to operations (€158.2 million) refer to financial receivables due from subsidiaries paid through the intercompany current account. The decrease of €1,403.0 million compared to 31 December 2016 is due to the presence in 2016 of receivables arising essentially following the repayment by Italgas, on behalf of its subsidiaries, of existing loan agreements as at 7 November 2016 to Snam for a total of €1,708 million. The separation of Italgas Reti from Snam in effect brought about the early settlement of the above-mentioned loan agreements.

The breakdown of debt by type of interest rate as at 31 December 2017 is as follows:

(€ million)	31.12.2016	%	31.12.2017	%
Fixed rate			<b>2,651.9</b>	71.4
Floating rate	3,619.0	100.0	<b>1,059.9</b>	28.8
	<b>3,619.0</b>	<b>100.0</b>	<b>3,711.8</b>	<b>100.0</b>

Fixed rate financial liabilities stood at €2,651.9 million and refer to the issue of bond loans.

Floating rate financial liabilities totalled €1,059.9 million and fell by €2,559.1 compared with 31 December 2016 mainly as a result of the above-mentioned issue of bond loans which replaced short-term bank loans.

As at 31 December 2017, Italgas had unused committed long-term credit lines worth €1.1 billion.

As at 31 December 2017, there were no financial covenants and collateralised bilateral and syndicated loan agreements in place with banks and other financial institutions. Some of these contracts provide, *inter alia*, for the following: (i) negative pledge commitments pursuant to which Italgas and its subsidiaries are subject to limitations on pledging real property rights or other restrictions on all or part of the respective assets, shares or merchandise; (ii) pari passu and change-of-control clauses; and (iii) limitations on certain extraordinary transactions that the Company and its subsidiaries may carry out. These commitments were satisfied as at 31 December 2017.

## RECLASSIFIED STATEMENT OF CASH FLOWS

(€ million)	1.6.2016-31.12.2016	2017
<b>Net profit</b>	<b>177.1</b>	<b>174.2</b>
<i>Adjusted:</i>		
- Amortisation, depreciation and other non-monetary components	0.8	<b>1.1</b>
- Dividends, interest and income taxes	(189.8)	<b>(193.3)</b>
Change in working capital due to operating activities	3.6	<b>3.8</b>
Dividends, interest and income taxes collected (paid)	177.4	<b>199.2</b>
<b>Net cash flow from operating activities</b>	<b>169.1</b>	<b>185.0</b>
Investments	(2,227.0)	<b>(1,526.6)</b>
Other changes relating to investment activities		<b>7.7</b>
<b>Free cash flow</b>	<b>(2,057.9)</b>	<b>(1,333.8)</b>
Change in current and non-current financial payables	3,619.0	<b>92.7</b>
Current financial receivables instrumental to operations	(1,561.2)	1,403.0
Net contributions of equity	0.1	
Equity cash flow		<b>(161.8)</b>
Net cash flow for the year	(1,561.2)	0.1
<b>Flusso di cassa netto dell'esercizio</b>	<b>-</b>	<b>0,1</b>

## Change in net financial debt

(€ million)	1.6.2016-31.12.2016	2017
<i>Free cash flow</i>	(2,057.9)	<b>(1,333.8)</b>
Net contributions of equity	0.1	
<b>Equity cash flow</b>		<b>(161.8)</b>
<b>Change in net financial debt</b>	<b>(2,057.8)</b>	<b>(1,495.6)</b>

## NON-GAAP Measures

### ALTERNATIVE PERFORMANCE INDICATORS

On 5 October 2015, the ESMA (European Security and Markets Authority) published its guidance (ESMA/2015/1415) on the presentation criteria for alternative performance indicators (API), which replaces the CESR/05-178b recommendations from 3 July 2016. The NON-GAAP financial report must be considered complementary to and not replacing the reports prepared according to IAS/IFRS.

The alternative performance indicator adopted in this report are illustrated below.

### MAIN ALTERNATIVE PERFORMANCE INDICATORS

Alternative capital performance indicators	Description
Gas Distribution regulated revenue	Operating performance indicator representing revenue from regulated gas distribution activities, calculated by subtracting the revenue for construction and enhancement of infrastructures recognised pursuant to IFRIC 12, penalties payable to the Authority and other components of the statement of reconciliation of the reclassified income statement with the reported income statement from core business revenue and other revenue and income.
EBITDA	Operating performance indicator, calculated by subtracting operating costs from revenue.
Adjusted EBITDA	Operating performance indicator, calculated by subtracting income components classified as special items (as defined in the chapter "Comment on the economic and financial results" of this report) from EBITDA.
EBIT	Operating performance indicator, calculated by subtracting operating costs, amortisation, depreciation and impairment from revenue.
Adjusted EBITDA	Operating performance indicator, calculated by subtracting income components classified as special items (as defined in the chapter "Comment on the economic and financial results" of this report) from EBIT.

Alternative capital performance indicators	Description
Net working capital	A capital indicator that expresses the capital employed in non-financial current assets and liabilities and indicates the company's short-term balance. This is defined as the sum of the values relating to trade receivables and payables, inventories, tax receivables and payables, provisions for risks and charges, deferred tax assets, deferred tax liabilities and other current assets and liabilities.
Fixed capital	A capital indicator that expresses the total fixed assets. Fixed capital is defined as the sum of the values relating to items of property, plant and equipment, intangible assets, equity investments and payables net of investment.v
Net invested capital	A capital indicator that expresses net investments of an operating nature, represented by the sum of the values related to fixed assets, net working capital, provisions for employee benefits and assets held for sale and the directly associated liabilities.

Alternative capital performance indicators	Description
Free cash flow before Merger and Acquisition transactions	The free cash flow representing the difference between the net cash flow from operating activities and the net cash flow from investment activities resulting from mergers and acquisitions.
Free cash flow	The free cash flow representing the difference between the net cash flow from operating activities and the net cash flow from investment activities.
Net financial debt	Determined as the sum of the values relating to short and long-term financial payables, net of cash and cash equivalents.

## RECONCILIATION OF THE RECLASSIFIED INCOME STATEMENT, STATEMENT OF FINANCIAL POSITION AND STATEMENT OF CASH FLOWS

In line with ESM/2015/1415 guidance, the reconciliation of the Income Statements, Statements of Financial Position and Statements of Cash Flows of the Italgas Group and Italgas S.p.A., commented in the Directors' Report, is provided below with the related legally required statements.



## RECONCILIATION BETWEEN RECLASSIFIED CONSOLIDATED FINANCIAL STATEMENTS AND THE LEGALLY REQUIRED FINANCIAL STATEMENTS

### RECLASSIFIED INCOME STATEMENT

(€ million)		1.6.2016 31.12.2016		
Reclassified Income Statement items	Reference to the notes to the consolidated financial statements	Figures from mandatory statements	Partial figures from mandatory statements	Figures from reclassified statements
<b>Revenue</b>		<b>273.7</b>		
Revenues for construction and upgrading distribution infrastructures IFRIC 12	(note 26)		(61.7)	
Net income from Energy Efficiency Certificates	(note 26)			
Gas distribution service safety improvement penalties	(note 27)		(15.9)	
Management refunds	(note 26)			
<b>Total gas distribution regulated revenue</b>				<b>196.1</b>
<b>Operating costs</b>		<b>(167.7)</b>		
Costs for construction and upgrading distribution infrastructures IFRIC 12	(note 27)		61.7	
Net income from Energy Efficiency Certificates	(note 26)			
Gas distribution service safety improvement penalties	(note 27)		15.9	
Management refunds	(note 26)			
<b>Total operating costs</b>				<b>(90.1)</b>
<b>EBITDA</b>				<b>106.0</b>
Amortisation, depreciation and impairment		(76.8)		(76.8)
<b>EBIT</b>		<b>29.2</b>		<b>29.2</b>
Net financial expense		(122.8)		(122.8)
Net income from equity investments		3.1		3.1
<b>Pre-tax profit</b>		<b>(90.5)</b>		<b>(90.5)</b>
Income taxes		18.3		18.0
<b>Net profit (loss)</b>		<b>(72.2)</b>		<b>(72.2)</b>

2017

Figures from mandatory statements	Partial figures from mandatory statements	Figures from reclassified statements
1,621.0		
	(479.7)	
	(8.1)	
	(7.9)	
	(1.1)	
		1,124.2
(844.8)		
	479.7	
	8.1	
	7.9	
	1.1	
		(348.0)
		776.2
(358.3)		(358.3)
417.9		417.9
(36.2)		(36.2)
23.0		23.0
404.7		404.7
(111.9)		(111.9)
292.8		292.8

## RECLASSIFIED STATEMENT OF FINANCIAL POSITION

(€ million)	31.12.2016		31.12.2017		
Reclassified Statement of Financial Position items					
(Where not expressly indicated, the item is obtained directly from the legally-required statement)	Reference to the notes to the consolidated financial statements	Partial figures from mandatory statements	Figures from reclassified statements	Partial figures from mandatory statements	Figures from reclassified statements
<b>Fixed capital</b>					
Property, plant and equipment			227.5		224.6
Intangible assets			4,486.5		4,676.6
Investments valued using the equity method			175.7		184.8
Other investments			0.1		0.1
<i>Net payables relating to investment activities, composed of:</i>			(97.1)		(135.3)
- Payables for investment activities	(note 19)	(102.9)		(140.6)	
- Receivables for investment/divestment activities	(note 10)	5.8		5.3	
Other financial assets			0.1		0.1
<b>Total fixed capital</b>			<b>4,792.8</b>		<b>4,950.9</b>
<b>Net working capital</b>					
Trade receivables	(note 10)		417.6		406.5
Inventories			32.6		22.4
<i>Tax receivables, composed of:</i>			53.5		45.2
- Current income tax assets and other current tax assets	(note 12)	37.9		29.7	
- IRES receivables for National Tax Consolidation Scheme	(note 10)	15.6		15.5	
Trade payables	(note 19)		(174.5)		(184.1)
<i>Tax payables, composed of:</i>			(13.5)		(15.9)
- Current income tax liabilities and other current tax liabilities	(note 12)	(13.5)		(15.9)	
<i>Other assets, composed of:</i>					
Provisions for risks and charges			(230.5)		(208.3)
- Other receivables	(note 10)	140.1		192.0	
- Other current and non-current assets	(note 13)	9.0		5.3	

(€ million)

31.12.2016

31.12.2017

**Reclassified Statement  
of Financial Position items**

(Where not expressly indicated, the item is obtained directly from the legally-required statement)	Reference to the notes to the consoli- dated financial statements	Partial figures from mandatory statements	Figures from reclassified statements	Partial figures from mandatory statements	Figures from reclassified statements
<i>Assets and liabilities from regulated activities, composed of:</i>			33.3		78.5
- Regulated activities	(note 13)	33.3		78.5	
- Liabilities from regulated activities	(note 20)				
<i>Other liabilities, composed of:</i>			(171.1)		(175.7)
- Other payables	(note 19)	(166.0)		(173.5)	
- Other current and non-current liabilities	(note 20)	(5.1)		(2.2)	
<b>Total net working capital</b>			<b>(9.5)</b>		<b>71.1</b>
Provisions for employee benefits			(120.6)		(116.1)
<b>Assets held for sale and directly associated liabilities, composed of:</b>			<b>19.0</b>		<b>0.0</b>
- Assets held for sale		25.0			
- Liabilities directly associated with assets held for sale		(6.0)			
<b>NET INVESTED CAPITAL</b>			<b>4,681.7</b>		<b>4,905.9</b>
Shareholders' equity including minority interests			1,064.3		(1,185.6)
Net financial debt					
<i>Financial liabilities, composed of:</i>			3,619.0		3,723.2
- Long-term financial liabilities		923.0		3,617.0	
- Current portions of long-term financial liabilities		0.4		25.1	
- Short-term financial liabilities		2,695.6		81.1	
<i>Financial receivables and cash and cash equivalents, composed of:</i>			(1.6)		(2.9)
- Financial receivables non-instrumental to operations					
- Cash and cash equivalents	(note 8)	(1.6)		(2.8)	
- Other financial assets held for trading or available for sale				(0.1)	
<b>Total net financial debt</b>			<b>3,617.4</b>		<b>3,720.3</b>
<b>COVERAGE</b>			<b>4,681.7</b>		<b>4,905.9</b>

## RECLASSIFIED STATEMENT OF CASH FLOWS

(€ million)	1.6.2016 - 31.12.2016		2017	
Reclassified Statement of Cash Flows items and intersection of legally-required statement items	Partial figures from mandatory statements	Figures from reclassified statements	Partial figures from mandatory statements	Figures from reclassified statements
<b>Net profit</b>		<b>(72.2)</b>		<b>292.8</b>
Adjusted:				
<i>Amortisation, depreciation and other non-monetary components:</i>		<i>73.7</i>		<i>330.4</i>
- Amortisation and depreciation	76.8		<b>352.0</b>	
Change in provisions for employee benefits	(4.5)		<b>(4.9)</b>	
- Net impairment of property, plant and equipment and intangible assets			<b>6.3</b>	
- Effect of valuation using equity method	(3.1)		<b>(23.0)</b>	
Net capital losses (capital gains) on sales and asset radiation		0.7		<b>4.1</b>
<i>Interest, income taxes and other changes:</i>		<i>103.2</i>		<i>141.5</i>
- Interest income	(0.4)		<b>(0.8)</b>	
- Interest expense	121.9		<b>30.4</b>	
- Income taxes	(18.3)		<b>111.9</b>	
<i>Change in operating capital relating to operations:</i>		<i>39.5</i>		<i>(100.8)</i>
- Inventories	(7.6)		<b>10.3</b>	
- Trade receivables	(33.6)		<b>12.4</b>	
- Trade payables	51.9		<b>8.4</b>	
- Change to provision for risks and charges	20.8		<b>(22.5)</b>	
- Other assets and liabilities	8.0		<b>(112.2)</b>	
- Takeover of payables of acquired companies			<b>2.8</b>	
<i>Dividends, interest and income taxes collected (paid):</i>		<i>(185.9)</i>		<i>(118.6)</i>
- Dividends collected			<b>13.8</b>	
- Interest income	(0.4)		<b>0.8</b>	
- Interest paid	(121.9)		<b>(30.4)</b>	
- Income taxes (paid) refunded	(64.4)		<b>(102.8)</b>	
<b>Net cash flow from operating activities</b>		<b>(45.5)</b>		<b>549.4</b>



(€ million)	1.6.2016 - 31.12.2016		2017	
Reclassified Statement of Cash Flows items and intersection of legally-required statement items	Partial figures from mandatory statements	Figures from reclassified statements	Partial figures from mandatory statements	Figures from reclassified statements
<i>Technical investments:</i>		(79.5)		(493.3)
- Property, plant and equipment	(5.7)		(10.9)	
- Intangible assets	(73.8)		(482.4)	
<i>Disinvestments:</i>				22.4
- Intangible assets			0.4	
- Equity investments			22.0	
<i>Other changes relating to investment activities:</i>		14.9		30.7
- Changes in payables and receivables relating to investment activities	14.9		30.7	
<b>Free cash flow before M&amp;A transactions</b>		(110.1)		109.2
Change in scope of consolidation		(1,503.0)		(38.7)
of which:				
<i>price paid for equity</i>			(35.9)	
<i>takeover of net payables of acquired companies</i>			(2.8)	
<b>Free cash flow</b>		(1,613.1)		70.5
<i>Change in financial payables:</i>		1,614.6		92.6
- Assumptions of long-term financial payables	927.5		3,012.0	
- Repayments of long-term financial payables	(1,441.4)		(300.4)	
- Increase (decrease) in net short-term financial payables	2,128.5		(2,619.0)	
Equity cash flow				(161.8)
<b>Net cash flow for the year</b>		1.5		1.3

## RECONCILIATION BETWEEN RECLASSIFIED ITALGAS S.P.A. FINANCIAL STATEMENTS AND THE LEGALLY REQUIRED FINANCIAL STATEMENTS

### RECLASSIFIED STATEMENT OF FINANCIAL POSITION

(€ million)		31.12.2016	31.12.2017
(Where not expressly indicated, the item is obtained directly from the legally-required statement)	Reference to the notes to the consolidated financial statements	Partial figures from mandatory statements	Figures from reclassified statements
<b>Fixed capital</b>			
Property, plant and equipment		0.4	1.9
Investments valued using the equity method		2,966.7	2,974.2
Financial receivables instrumental to operations	(note 6)	723.3	2,240.8
<i>Net payables relating to investment activities, composed of:</i>			(7.8)
- Payables for investment activities			(7.8)
<b>Total fixed capital</b>		<b>3,690.4</b>	<b>5,209.1</b>
<b>Net working capital</b>			
<i>Trade receivables</i>	(note 8)	<b>8.7</b>	<b>21.6</b>
Tax receivables, composed of:		28.3	6.1
- IRES receivables for National Tax Consolidation Scheme	(note 7)		6.1
- Current income tax assets and other current tax assets	(note 8)	28.3	
Deferred tax assets			2.3
Trade payables	(note 11)	(15.6)	(16.1)
<i>Tax payables, composed of:</i>		<b>(17.2)</b>	<b>(4.5)</b>
- Current income tax liabilities and other current tax liabilities	(note 7)	(0.8)	(4.5)
- IRES payables for National Tax Consolidation Scheme	(note 11)	(16.4)	

(€ million)

31.12.2016

31.12.2017

(Where not expressly indicated, the item is obtained directly from the legally-required statement)	Reference to the notes to the consolidated financial statements	Partial figures from mandatory statements	Figures from reclassified statements	Partial figures from mandatory statements	Figures from reclassified statements
Provisions for risks and charges			(1.2)		(2.2)
<i>Derivatives</i>	<i>(notes 11 and 18)</i>				
<i>Other assets, composed of:</i>			<b>13.4</b>		<b>5.2</b>
- Other receivables	(note 6)	7.8		<b>3.2</b>	
- Other current and non-current assets	(note 8)	5.6		<b>2.0</b>	
<i>Other liabilities, composed of:</i>			<b>(3.4)</b>		<b>(8.4)</b>
- Other payables	(note 11)	(3.4)		<b>(8.4)</b>	
- Other current and non-current liabilities					
<b>Total net working capital</b>			<b>13.0</b>		<b>4.0</b>
Provisions for employee benefits			(4.9)		(6.5)
<b>Assets held for sale and directly associated liabilities, composed of:</b>			<b>0</b>		<b>0</b>
- Assets held for sale					
- Liabilities directly associated with assets held for sale					
<b>NET INVESTED CAPITAL</b>			<b>3,698.5</b>		<b>5,206.6</b>
Shareholders' equity including minority interests			1,640.7		<b>1,653.2</b>
<b>Net financial debt</b>					
<i>Financial liabilities, composed of:</i>			<b>3,619.0</b>		<b>3,711.6</b>
- Long-term financial liabilities		923.0		<b>3,611.9</b>	
- Current portions of long-term financial liabilities		0.4		<b>23.3</b>	
- Short-term financial liabilities		2,695.6		<b>76.4</b>	
<i>Financial receivables and cash and cash equivalents, composed of:</i>			(1,561)		(158)
- Financial receivables non-instrumental to operations	(note 8)	(1,561.2)		<b>(158.2)</b>	
<b>Net financial debt</b>			<b>2,057.8</b>		<b>3,553.4</b>
<b>COVERAGE</b>			<b>3,698.5</b>		<b>5,206.6</b>

## RECLASSIFIED STATEMENT OF CASH FLOWS

(€ million)	01.06.2016 - 31.12.2016		2017	
Reclassified Statement of Cash Flows items and intersection of legally-required statement items	Partial figures from mandatory statements	Figures from reclassified statements	Partial figures from mandatory statements	Figures from reclassified statements
<b>Net profit</b>		<b>177.1</b>		<b>174.2</b>
<i>Adjusted:</i>				
<i>Amortisation, depreciation and other non-monetary components:</i>		<b>0.8</b>		<b>1.1</b>
Change in provisions for employee benefits	0.8		1.1	
<i>Interest, income taxes and other changes:</i>		<b>(189.8)</b>		<b>(193.3)</b>
- Dividends and other income from investments	(190.0)		<b>(197.4)</b>	
- Interest income	(2.0)		<b>(21.5)</b>	
- Interest expense	2.8		<b>29.9</b>	
- Income taxes	(0.6)		<b>(4.3)</b>	
<i>Change in working capital due to operating activities:</i>		<b>3.6</b>		<b>3.8</b>
- Trade receivables	(8.7)		<b>(12.9)</b>	
- Trade payables	15.6		<b>0.5</b>	
- Change to provision for risks and charges	0.7		<b>1.0</b>	
- Other assets and liabilities	(4.0)		<b>15.2</b>	
<i>Dividends, interest and income taxes collected (paid):</i>		<b>177.4</b>		<b>199.2</b>
- Dividends and other income collected from investments	190.0		<b>197.4</b>	
- Interest income	2.0		<b>21.5</b>	
- Interest paid	(2.8)		<b>(29.9)</b>	
- Income taxes (paid) refunded	(11.8)		<b>10.2</b>	
<b>Net cash flow from operating activities</b>		<b>169.1</b>		<b>185.0</b>
<i>Investments:</i>		<b>(2,226.8)</b>		<b>(1,526.5)</b>
- Property, plant and equipment	(0.5)		<b>(1.6)</b>	
Equity investments	(1,503.2)		<b>(7.5)</b>	
Non-current financial receivables instrumental to operations	(723.3)		<b>(1,517.4)</b>	

(€ million)	01.06.2016 - 31.12.2016		2017	
Reclassified Statement of Cash Flows items and intersection of legally-required statement items	Partial figures from mandatory statements	Figures from reclassified statements	Partial figures from mandatory statements	Figures from reclassified statements
<i>Disinvestments:</i>				<b>7.7</b>
- Change in receivables relating to disinvestment activities			7.7	
<b>Free cash flow</b>		<b>(2,057.9)</b>		<b>(1,333.8)</b>
<i>Change in financial payables:</i>		<b>3,619.0</b>		<b>92.7</b>
- Assumptions of long-term financial payables	923.4		3,011.8	
- Repayment of long-term financial payables			(300.0)	
- Increase (decrease) in short-term financial payables	2,695.6		(2,619.1)	
- Current financial receivables instrumental to operations		(1,561.2)		1,403.0
- Net contributions to equity		0.1		
Equity cash flow				(161.8)
<b>Net cash flow for the year</b>		<b>0</b>		<b>0.1</b>





## Other information

### TREASURY SHARES

The company did not own any treasury shares as at 31 December 2017.

Compensation paid to directors and statutory auditors, general managers and managers with strategic responsibilities, and investments held by each of these

Information on the compensation paid to directors and statutory auditors, general managers and managers with strategic responsibilities, and the equity investments held by each of these, can be found in the Remuneration Report, which is prepared in accordance with Article 123-ter of Legislative Decree 58/1998 (TUF). The Remuneration Report is available on the Italgas website ([www.italgas.it](http://www.italgas.it)) under Governance, to which reference should be made.

### RELATED-PARTY TRANSACTIONS

Based on Italgas' current ownership structure, the parties related to Italgas include, in addition to the directors, statutory auditors, key managers and companies associated with the Group or under its joint control, also the subsidiaries directly or indirectly controlled by CDP, therefore including the shareholder Snam, and the Ministry of Economy and Finance (MEF). Transactions with these entities relate to the exchange of assets, the provision of services and, in the case of CDP, the provision of financial resources.

These transactions are part of ordinary business operations and are generally settled at arm's length, i.e. the conditions which would be applied between two independent parties. All the transactions carried out were in the interest of the companies of the Italgas Group.

Pursuant to the provisions of the applicable legislation, the Company has adopted internal procedures to ensure that transactions carried out by the Company or its subsidiaries with related parties are transparent and correct in their substance and procedure.

Directors and statutory auditors declare potential interests that they have in relation to the Company and the Group periodically, and/or when changes in said interests occur; they also inform the Chief Executive Officer (or the Chairman, in the case of the Chief Executive Officer's interests), who in turns informs the other directors and the Board of Statutory Auditors, of individual transactions that the Company intends to carry out and in which they have an interest.

Italgas is not managed or coordinated by any other entity, although CDP and CDP Reti consolidate it pursuant to IFRS 10. As at 31 December 2017, Italgas manages and coordinates its subsidiaries, pursuant to Article 2497 et seq. of the Italian Civil Code.

The amounts involved in commercial, miscellaneous and financial relations with related parties, descriptions of the key transactions and the impact of these on the balance sheet, income statement and cash flows, are provided in the paragraph "Related-party transactions" of the Notes to the consolidated financial statements.

Relations with Key Managers are shown in the paragraph “Operating costs” of the Notes to the consolidated financial statements.

## **PERFORMANCE OF SUBSIDIARIES**

For information on the outlook of the areas where Italgas operates in whole or in part through subsidiaries, please refer to “Operating performance” and “Comment on the Economic and Financial Results” of this Report.

## **BRANCH OFFICES**

In compliance with Art. 2428, fourth paragraph of the Italian Civil Code, it is noted that the company does not have secondary offices.

## **RESEARCH AND DEVELOPMENT**

Italgas’ research and development activities are described by sector under “Sustainable Development Commitment”.

## **SIGNIFICANT EVENTS AFTER YEAR END**

The significant transactions carried out after 31 December 2017 are summarised below.

Italgas Acqua was established on 1 January 2018 following the proportional partial demerger of Italgas Reti to a newco through assignment to the latter of the “former Napoletanagas water business unit”.

On 15 January 2018, Italgas signed an Interest Rate Swap (IRS) contract to hedge a floating rate EIB loan (6M Euribor) totalling €360 million, disbursed on 28 December 2017 and maturing on 15 December 2037. The aforementioned floating rate will therefore be recalculated at a fixed rate through the IRS with a seven-year duration, calculated on the same amount and with the same repayment schedule as the underlying loan.

On 24 January and 31 January 2018 the administrative bodies of ACAM Gas and Italgas Reti approved the plan to merge ACAM Gas into Italgas Reti, effective from 1 January 2018 for accounting purposes.

On 26 January 2018, the acquisition of the Amalfitana Gas business unit was finalised for natural gas distribution activities in three ATEMs in Campania and Basilicata.

On 30 January 2018 Italgas successfully arranged the reopening of €250 million of the previous bond issue of 18 September 2017 (€500 million, maturing 18 January 2029 and with a coupon of 1.625%). The secondary market performance of the original issue allowed an improvement of the reopening terms compared to that issue, with a 58 bps spread on

the mid-swap rate compared to the original 72 bps. The transaction led to an increase in the issue total from €100 million to €250 million following strong demand that was more than 7 times higher than the amount offered.

Subsequently, on 31 January 2018, Italgas finalised the acquisition of the AEnergia Reti business unit relating to the distribution network serving the municipality of Portopalo di Capo Passero (Syracuse).

With regard to the regulatory framework, note that through Resolution 1/2018-DMRT of 29 January 2018, the Authority defined the national energy efficiency annual quantitative obligations of natural gas end users to be achieved in 2018 by distributors with more than 50,000 end users connected to its distribution network as at 31 December 2016.

For subsidiaries and associates of Italgas S.p.A., the quantitative obligation for 2018, rounded off to the nearest whole number on a commercial basis and expressed as a number of White Certificates, is €825,722 for Italgas Reti, €121,790 for Toscana Energia, €10,595 for ACAM Gas and €5,853 thousand for Umbria Distribuzione Gas.

On 15 February 2018, the Energy Markets Manager (GME) published the updated version of the Operating Rules for the Energy Efficiency Certificates Market, which enters into force immediately on publication. The update follows a specific communication from the Ministry of Economic Development received on 14 February 2018 concerning the application to adopt urgent corrective measures in relation to the trading methods envisaged on the TEE Market.

In particular, the Ministry of Economic Development, in concert with the Ministry for the Environment in order to protect the correct operation of the incentives mechanism and limit the effects of strong price volatility on the tariff contribution calculation, considered it appropriate at present to reduce the market session frequency to just one session per month.

The dates and times of the next market trading sessions will be published on the GME website.

Implementing the binding agreement signed on 8 November 2017, on 28 February 2018 Italgas acquired 100% of **Ichnusa Gas**, a holding company with control of 12 companies granted concessions for the installation and operation of gas distribution networks in 81 municipalities in Sardinia, from CPL Concordia and Impresa Costruzioni Ing. Raffello Pellegrini S.r.l. The enterprise value of Ichnusa Gas was established at €26.2 million. As at the acquisition date, 2 of the 12 concessions are provisionally operative with the first customers served with LPG, whilst the remaining 10 refer to networks under construction and to be implemented for a total investment forecast at over €170 million, part-financed from regional public grants.







## Information on corporate governance and ownership structure

### INTRODUCTION

The complete picture of the Italgas corporate governance system is analytically described in the “2017 Report on Corporate Governance and the Ownership Structure” (hereinafter the “2017 Governance Report”) prepared pursuant to Art. 123-bis of Legislative Decree No. 58/1998 (hereinafter the “Consolidated Finance Act” or “TUF”), approved by the Board of Directors on 12 March 2018.

The “2017 Report on Corporate Governance and Ownership” is published on the website [www.italgas.it](http://www.italgas.it) along with the Annual Report.

### CORPORATE GOVERNANCE SYSTEM

Italgas is an issuer with shares listed on the Electronic Stock Market managed by Borsa Italian S.p.A., and therefore fulfils the legal and regulatory obligations for the listing.

The Italgas corporate governance system is the set of planning, management and control rules and methods necessary for the operation of the Company and has been outlined by the Board of Directors:

- in compliance with applicable law, also taking into account its qualification as a listed Issuer and its characteristic activity (such as the laws on so-called unbundling),
- in accordance with the Code of Corporate Governance,
- having as reference the national and international best practices.

This system is founded on certain basic principles, such as fair and transparent management of business choice also ensured by identifying the information flows between corporate bodies and the efficient definition of the internal control and risk management system. A system of Enterprise Risk Management was implemented, composed of rules, procedures and organisational structures aimed at identifying, measuring, managing and monitoring the main risks that might affect the achievement of the strategic objectives.

The Bylaws define the Company’s governance model and the main rules for the functioning of corporate bodies. Italgas adopted a traditional administration and control system, characterised by the presence of the following bodies:

- Shareholders’ Meeting;
- Board of Directors;
- Board of Statutory Auditors.

### SHAREHOLDERS’ MEETING

The Shareholders’ Meeting is a decision-making body of the shareholders and appoints the Board of Directors and the Board of Statutory Auditors.

The validity of the Meeting’s quorum and its deliberations is established in accordance with the law.

According to the Bylaws, the Meeting deliberates on the matters covered by law. However, as permitted by law, the Bylaws assign the Board jurisdiction to decide on the following matters:

- merger in the cases set forth by Art. 2505 and 2505-bis of the Italian Civil Code, also referred to for a demerger;
- establishment, modification and elimination of secondary offices;
- share capital decrease when a shareholder withdraws;
- compliance of the Bylaws with regulatory provisions;
- transfer of the registered office within Italy.

In accordance with the provisions of the Code of Corporate Governance, the Shareholders' Meeting approved its own dedicated meeting regulations that regulate the order and functions of the General Meeting and guarantee that each shareholder is entitled to express his/her opinion about the issues being discussed.

The corporate Bylaws provide for a combined notice of meeting for both the Ordinary and Extraordinary Shareholders' Meetings. The right to attend Shareholders' Meetings is governed by law, the Bylaws and the provisions contained in the notice of meeting. Those with voting rights may be represented by written proxy within the legal limits and notice of this proxy must be delivered to the Company by certified email. Shareholders may ask questions about agenda items even prior to a meeting. Questions arriving before the Shareholders' Meeting will be answered during the Meeting, at the latest. The information is provided in observance of the rules for price sensitive information.

#### BOARD OF DIRECTORS

The Board of Directors is vested with full powers of ordinary and extraordinary administration and can perform all acts

deemed appropriate to achieve the corporate purpose, in line with the Corporate Governance Code and the applicable rules and regulations, with the exception of those actions which the law and the Bylaws reserve to the Shareholders' Meeting. The Board of Directors appoints the Chairman, if the Shareholders' Meeting has not already done so, delegates its powers to one or more of its members and may set up Committees. Specifically, the Board of Directors has created the following Committees, in compliance with the Code of Corporate Governance and the Bylaws: The Appointments and Remuneration Committee, Committee for Control, Risk and Related Party Transactions and the Sustainability Committee.

On 4 August 2016 the Meeting set nine as the number of members of the Board of Directors of Italgas S.p.A. and the term of Office as three years, expiring on the date of the General Meeting to be convened in 2019 to approve the financial statements as at 31 December 2018, and appointed as Directors Lorenzo Bini Smaghi (Chairman), Paolo Gallo, Nicola Bedin, Barbara Borra, Maurizio Dainelli, Cinzia Farisè, Yunpeng He, Paolo Mosa and Paola Annamaria Petrone. The Italgas S.p.A. Board of Directors meeting of 27 July 2017 co-opted Federica Lolli to replace Barbara Borra, who had resigned. The Board of directors of Italgas S.p.A. determined that for the 9 Directors, of which 4 are independent, there are no grounds for ineligibility or incompatibility, that each one meets the integrity requirements established by law and that Directors Nicola Bedin, Cinzia Farisè, Federica Lolli and Paola Annamaria Petrone satisfy the requisites of independence established by law and the Corporate Governance Code. The feminine gender is represented on the Board of Directors with three of nine members, in compliance with current regulations regarding gender balance (one third of the members).

**Consigliere****Carica e qualifica**

Lorenzo Bini Smaghi	Non-executive director and Chairman
Paolo Gallo	Chief Executive Officer
Nicola Bedin	Non-executive director (1)
Federica Lolli	Non-executive director (1)
Maurizio Dainelli	Non-executive director
Yunpeng He	Non-executive director
Cinzia Farisè	Non-executive director (1)
Paolo Mosa	Non-executive director
Paola Annamaria Petrone	Non-executive director (1)

(1) Independent director pursuant to the Consolidated Finance Act (TUF) and the Corporate Governance Code.

The meeting of the Board of Directors of 4 August 2016 appointed Paolo Gallo as Chief Executive Officer, granting him all the powers and authority, excluding those otherwise provided for by law and the Bylaws and which are not reserved to the Board of Directors or the Chairman.

On 28 November 2016, the Board of Directors appointed Alessio Minutoli, the Head of Legal and Corporate Affairs and Compliance, as Secretary to the Board of Directors.

The Board, at the time of its appointment and periodically thereafter, evaluates the independence and integrity of the directors, as well as the lack of grounds for ineligibility or incompatibility.

With effect starting upon completion of the separation of Italgas Gas from the Snam Group, Paolo Gallo also assumed the position of General Manager of Italgas, while on the same date Antonio Paccioretti took over as General Director of Finance and Services.

**Committees established by the Board of Directors**

The Board of Directors of Italgas established three internal committees, appointing the members:

- Appointments and Remuneration Committee, established on 23 October 2017 to replace the former Nominations Committee and Compensation Committee;
- Control, Risk and Related-Party Transactions Committee;
- Sustainability Committee.

The composition, duties, and operation of the committees are being governed by the Board with appropriate regulations. The Board appoints the members.

The committees are composed of three non-executive directors in the majority independent except for the Committee for Control and Risks and Transactions with Related Parties which is composed of only independent directors, and the Sustainability Committee which is composed of non-executive directors. The term of Office of each member corresponds to the tenure of the Director's office.

In the performance of their functions, the Committees may access information and company departments. They have sufficient financial resources and may use external consultants within the terms set from time to time by the Board of Directors. Committee meetings may be attended, upon invitation, also by parties that are not members.

The Control, Risk and Related-Party Transactions Committee is composed as follows:

Member	Position
Paola Annamaria Petrone	Independent, non-executive (*) - Chairman
Nicola Bedin	Independent, non-executive (*)
Federica Lolli	Independent, non-executive (*)
(*) Independent pursuant to the independence requirements set out by the TUF and the Code of Corporate Governance.	

The Board of Directors has determined that at least one Member of the Committee of Control, Risk and Related Party Transactions has specific expertise in accounting, financial or risk management matters as required by the Corporate Governance Code.

The Appointments and Remuneration Committee is composed as follows:

Member	Position
Cinzia Farisè	Independent, non-executive (*), Chairman
Maurizio Dainelli	Non-executive
Federica Lolli	Independent, non-executive (*)
(*) Independent pursuant to the independence requirements set out by the TUF and the Code of Corporate Governance.	

The Board of Directors has verified that at least one member has sufficient knowledge and experience of financial matters or remuneration policies required by the Corporate Governance Code.

The Sustainability Committee is composed as follows:

Member	Position
Nicola Bedin	Independent, non-executive (*) - Chairman
Yunpeng He	Non-executive
Paolo Mosa	Non-executive

(\*) Independent pursuant to the independence requirements set out by the TUF and the Code of Corporate Governance.

#### BOARD OF STATUTORY AUDITORS

The Board of Statutory Auditors supervises compliance with the law and the Articles of Association, respect for the principles of correct administration in carrying out corporate activities, the adequacy of the organisational structure for aspects of responsibility, of the system of internal control and accounting system as well as the reliability of the latter in correctly representing transactions, and how to implement the corporate governance rules provided under the Corporate Governance Code. Pursuant to Legislative Decree No. 39 of 27 January 2010, the Board of Statutory Auditors also performs supervisory functions in its capacity as “Committee for internal control and account auditing”.

Italgas’s Board of Statutory Auditors is made up of three standing auditors and two alternates appointed by the Shareholders’ Meeting for three financial years and can be re-elected for the term of office. Statutory auditors are chosen from among those who meet the professionalism and integrity requirements indicated in Decree No. 162 of the Ministry of Justice of 30 March 2000. For the purposes of the decree and as provided by the Bylaws, the matters strictly pertaining to the company activities are: business law, economics and corporate finance. Likewise, the sector pertaining strictly to the Company’s business is the engineering and geology sector.

Upon prior notice to the Chairman of the Board of Directors, the Board of Statutory Auditors may call Shareholders’ Meetings and Board of Directors’ meetings. The power to call Board of Directors’ meetings may be exercised individually by each member of the Board of Statutory Auditors; the power to call Shareholders’ Meetings must be exercised by at least two members of the Board. The Board of Statutory Auditors is asked to attend the meetings of the Committee of Control and Risk and Related Party Transactions.

Pursuant to the procedure “Transactions in which directors and statutory auditors have an interest and related-party transactions”, members of the Board of Statutory Auditors must declare any interest on their own behalf or that of third parties in specific transactions submitted to the Board of Directors.

The current Board of Statutory Auditors was appointed by the Shareholders’ Meeting of 4 August 2016 for a term of three financial years and in any event until the date of the Shareholders’ Meeting called in 2019 to approve the financial statements for 2018.

**Member****Position**

Gian Piero Balducci	Standing auditor and Chairman
Giandomenico Genta	Standing auditor
Laura Zanetti	Standing auditor
Barbara Cavalieri (1)	Alternate auditor
Walter Visco	Alternate auditor

(1) Appointed by the Shareholders' Meeting on 28 April 2017 to replace Marilena Cederna, who had resigned.

The Board has reviewed and confirmed that its members have the requirements of professionalism and integrity set forth in Ministerial Decree 162 of 30 March 2000 as specified by Art. 20.1 of the Bylaws and the independence requirements set forth by law and the Corporate Governance Code, sending the Board the results of this analysis in accordance with Application Criterion 8.C.1. of the Corporate Governance Code approved by the Committee for Corporate Governance (July 2015 edition).

**INDEPENDENT AUDITORS**

As required by law, auditing activities are assigned to an independent auditing firm included in the relevant register and appointed by the Shareholders' Meeting based on a reasoned proposal from the Board of Statutory Auditors.

On 28 April 2017 the Shareholders' Meeting assigned the statutory audit of Italgas S.p.A. to PricewaterhouseCoopers S.p.A. for the years 2017-2025.

**INFORMATION ON OWNERSHIP STRUCTURE****SHARE CAPITAL AND KEY SHAREHOLDERS**

The share capital of Italgas is composed of registered ordinary shares, which are indivisible and confer the right to one vote. As at 31 December 2017 (unchanged as at 12 March 2018) the share capital of Italgas amounts to €1,001,231,518.44 and is divided into 809,135,502 ordinary shares, with no par value indicated.

The Italgas stock is quoted in the FTSE MIB index of the Milan Stock Exchange.



Based on the information available and communications received pursuant to Article 120 of the Consolidated Finance Act and Consob Resolution No. 11971/1999 (Consob Issuer Regulations), as of 31 December 2017 shareholders holding shares worth more than 3% of the Italgas share capital are:

#### Significant shareholdings

Registrant	Direct Shareholder	% share of ordinary capital	% share of voting capital
CDP S.p.A.	CDP Reti S.p.A.(2)	26.05	26.05
	<b>Total</b>	<b>26.05</b>	<b>26.05</b>
Snam S.p.A.	Snam S.p.A.	13.50	13.50
Lazard Asset Management LLC	Lazard Asset Management	7.57	7.57
Romano Minozzi	Granitifiandre S.p.A.	0.38	0.38
	Finanziaria Ceramica Castellarano S.p.A.	0.23	0.23
	Iris Ceramica Group S.p.A.	1.88	1.88
	Romano Minozzi	2.50	2.50
	<b>Total</b>	<b>4.99</b>	<b>4.99</b>

(1) CDP Reti is owned 59.1% by CDP, 35% by State Grid Europe Limited – SGEL, a subsidiary of State Grid Corporation of China, and 5.9% by some Italian institutional investors.

Further information, as required pursuant to Article 123- bis, paragraph 1 of the TUF, can be found in the 2017 Report on corporate governance and the ownership structure.

#### SHAREHOLDER AGREEMENTS BETWEEN SHAREHOLDERS

The agreements between shareholders pursuant to Art. 122 of the TUF of which Italgas is aware are as follows.

On 20 October 2016 Snam S.p.A. (“Snam”), CDP Reti S.p.A. (“CDP Reti”) and CDP Gas S.p.A. (“CDP”) signed a shareholders’ agreement (the “Italgas Shareholders Agreement”) covering all the shares that the respective parties held in Italgas of consequence and with effect starting on the effective date of the partial and proportional demerger from Snam in favour of Italgas and the simultaneous listing of the Italgas shares,

namely 7 November 2016. Amongst other things, the Italgas Shareholders’ Agreement governs: (i) the exercise of voting rights attached to the syndicated shares; (ii) the establishment of a consultation committee; (iii) the obligations and procedures for submitting a joint list for the appointment of members of the company’s Board of Directors; and (iv) certain restrictions on the sale and purchase of Italgas shares. The Italgas Shareholders’ Agreement was filed in copy at the Milan Business Registry on 11 November 2016 and can be retrieved in extract from the company’s website at: <https://www.italgas.it/en/investors/shares-and-ownership-structure/shareholders-agreements/>.

On 1 May 2017, CDP Gas was merged into CDP, to which the Italgas shares held by CDP Gas were transferred. On 19 May 2017

these same shares were transferred to CDP Reti, already party to the Italgas Shareholders' Agreement.

On 27 November 2014, CDP S.p.A. ("CDP"), on the one hand, and State Grid Europe Limited ("SGEL") and State Grid International Development Limited ("SGID"), on the other, entered into a shareholders' agreement (the "SGEL Shareholders' Agreement") in the context of the sales contract concluded between the same parties on 31 July 2014 in accordance with which on 27 November 2014 SGEL acquired from CDP a stake equal to 35% of the share capital of CDP Reti. In conjunction with the effectiveness of the partial and proportional demerger from Snam in favour of Italgas and the simultaneous listing of the Italgas shares on 7 November 2016, SGEL, SGID and CDP have amended and supplemented the SGEL Shareholders' Agreement, effective on the same date, extending its application to the stake held by CDP Reti in Italgas. The SGEL Shareholders' Agreement was filed in copy at the Milan Business Registry on 11 November 2016 and can be retrieved in extract from the company's website at: <https://www.italgas.it/en/investors/shares-and-ownership-structure/shareholders-agreements/>.

## ITALGAS REGULATORY SYSTEM

In accordance with the evolving process aimed at continually improving the effectiveness and efficiency of its internal control and risk management system, Italgas has adopted its own regulatory system comprising the following regulatory levels: (i) Italgas Enterprise System (regulatory level 1), (ii) Process Standards and Compliance Standards (regulatory level 2) and (iii) Operating Instructions (regulatory level 3). The regulatory system also includes as an integral part thereof, the documents belonging to the certified management systems for health, safety, environment and quality in accordance with international ISO standard (Policies, Manuals, Procedures and Operating Instructions). Lastly, there are regulatory circulars to govern specific issues (sometimes with temporary validity). The Bylaws, the Ethics Code, the Corporate Governance Code, Model 231 and the Internal Control System on Corporate Information are placed in the general framework of the Regulatory System, as, although specific tools, the principles that inspire them are recognised as the founding principles of the conduct of the Italgas Group and, therefore, part of the general framework of the entire regulatory system.

These regulatory tools are part of the efficient handling of the Management and Coordination activities performed by Italgas concerning Subsidiaries, and they are subject to regular delivery to, and/or formal adoption by, the Boards of Directors of the Subsidiaries.

### PRINCIPLES OF THE SYSTEM OF RISK MANAGEMENT AND INTERNAL CONTROL IN RELATION TO THE FINANCIAL REPORTING PROCESS

The control and risk management system and the corporate reporting process of the Italgas Group are elements of the same "System" (the Corporate Reporting Control System), which aims to ensure the reliability<sup>15</sup>, accuracy<sup>16</sup>, dependability and timeliness of corporate disclosure with regard to financial reporting and the ability of the relevant business processes

<sup>15</sup> Reporting reliability: reporting that is correct, complies with generally accepted accounting standards and fulfils the requirements of the applicable laws and regulations.

<sup>16</sup> Disclosure accuracy: information free of errors.

to produce this information in keeping with generally accepted accounting standards. The reporting in question consists of all the data and information contained in the periodic accounting documents required by law – the separate and consolidated Annual Financial Report, half-year financial report and interim report on operations – as well as in any other accounting document or external communication – such as press releases and prospectuses prepared for specific transactions – covered by the statements provided for by Article 154-bis of the TUF. This reporting includes both financial and non-financial information, where the latter aims to describe significant aspects of the business, comment on the financial results for the year and/or describe future prospects.

The control and risk management model adopted by Italgas and its subsidiaries with regard to corporate reporting was defined in accordance with the provisions of the above-mentioned Article 154-bis of the TUF that Italgas is required to ensure compliance with, and is based in methodological terms on the “COSO Framework” (“Internal Control - Integrated Framework”, issued by the Committee of Sponsoring Organisations of the Treadway Commission), the international reference model for the establishment, updating, analysis and assessment of the control system.

The planning, institution and maintenance of the Corporate Reporting Control System are achieved through the activities of scoping, identifying and assessing the risks and controls (at the business level and process level through the activities of risk assessment and monitoring) and the related information flows (reporting).

The structure of the control system features company entity-level controls which operate transversely across the entity in question (group/individual company) and process-

level controls.

The controls, both at the entity level and process level, are subject to regular evaluation (monitoring) to verify the adequacy of the design and actual operability over time. For that purpose, there is provision for ongoing monitoring activities, assigned to the management responsible for the relevant procedures/activities, as well as independent monitoring assigned to Internal Audit, which operates according to an annual plan agreed with the Director responsible for preparing the company's financial reports (DP), which aims to define the scope and objectives of its actions through concerted audit procedures.

## MODEL 231 AND THE SUPERVISORY BODY

The Board of Directors of Italgas S.p.A. on 18 October 2016 approved its “Model 231”, of which the Ethics Code is an integral part, indicating the principles of organisation, management and control to prevent crimes from being committed in the interest or to the advantage of the Company as per the regulations on the administrative liability of companies (Legislative Decree 231 dated 8 June 2001).

On 20 December 2016 Italgas S.p.A.'s Board of Directors appointed the Supervisory Body, composed of Prof. Carlo Piergallini as Chairman and Professors Eliana La Ferrara and Francesco Profumo.

The Supervisory Body is guarantor of the Ethics Code and is equipped with autonomous powers of initiative and control in accordance with the regulation of law. The Body may be submitted requests for clarifications and interpretations on the principles and contents of the Ethics Code, suggestions regarding its application and notices of code violations, also anonymously.

In 2017, the Company completed a project to prepare the “Special Section” of Model 231, which supplements the model with indication of the risks/offences affecting each Sensitive Activity and reference to the codes of conduct, control mechanisms and specific control standards. This document was approved by the Board of Directors on 14 December 2017.

## **ETHICS CODE**

The Ethics Code defines a shared value system, expresses Italgas’s business ethics culture and forms the basis for the Company’s strategic thinking and the conduct of its corporate activities.

The Ethics Code is a compulsory general principle of the “Model 231”, containing the fundamental principles that must guide Italgas, such as respect for the law, fair competition, honesty, integrity, fairness and good faith towards all parties with which it has relationships. It also contains the general principles of sustainability and corporate responsibility, in addition to recalling the principles that must be respected in matters of the workplace, relations with stakeholders and suppliers and for the protection of personal data.











## Elements of risk and uncertainty

Below are the main risks analysed and monitored by the Italgas Group.

### FINANCIAL RISKS

#### INTEREST RATE RISK

Fluctuations in interest rates affect the market value of Italgas' financial assets and liabilities and its net financial expense. The Italgas Group has adopted a centralised organisational model. In accordance with this model, Italgas' various departments access the financial markets and use funds to cover financial requirements, in compliance with approved objectives, ensuring that the risk profile stays within the defined limits.

As at 31 December 2017 the financial debt at floating rate was 28.8% and at fixed rate was 71.2%.

As at the same date the Italgas Group used external financial resources in the following forms: Bonds subscribed by institutional investors, bilateral and syndicated loans with banks and other financial institutions, in the form of medium/long-term loans and bank credit lines at interest rates indexed to market benchmark rates, in particular the Europe Interbank Offered Rate (Euribor).

Therefore, an increase in interest rates, not implemented - in full or in part - in the regulatory WACC, could have negative effects on the assets and on the economic and financial situation of the Italgas Group.

At full performance, Italgas aims to maintain a debt ratio between a fixed rate and variable rate to minimise the risk of rising interest rates, with a goal being a fixed-rate and variable-rate debt composition of approximately 2/3 for fixed-rate and 1/3 for variable-rate. In this respect, in 2017 the Company issued bond loans for a total of €2,650 million with the following characteristics: (i) €1,500 million, issued

on 19 January 2017 and divided into two tranches, the first with a term of 5 years and the second of 10 years, both at a fixed rate, amounting to €750 million each and an annual coupon of 0.50% and 1.625%, respectively; (ii) €650 million issued on 14 March 2017, maturing on 14 March 2024 with a fixed rate annual coupon of 1.125%; (iii) €500 million issued on 18 September 2017, maturing on 18 January 2029 with a fixed rate annual coupon of 1.625%.

#### CREDIT RISK

Credit risk is the exposure to potential losses arising from counterparties failing to fulfil their obligations. Default or delayed payment of amounts owed may have a negative impact on the financial results and financial situation of Italgas.

The rules for customer access to the gas distribution service are established by the ARERA and set out in the Network Codes, namely, in documents that establish, for each type of service, the rules regulating the rights and obligations of the parties involved in the process of providing said services and contain contractual conditions that reduce the risk of non-compliance by customers, such as the provision of bank or insurance guarantees on first request.

As at 31 December 2017 there were no significant credit risks. However, note that on average 94% of trade receivables are settled by the due date and over 99% within the next 4 days, confirming the strong reliability of the business customers.

It cannot be ruled out, however, that Italgas could incur liabilities and/or losses due to its customers' failure to fulfil their payment obligations.

#### LIQUIDITY RISK

Liquidity risk is the risk that new financial resources may not be available (funding liquidity risk) or that the company may be

unable to convert assets into cash on the market (asset liquidity risk), meaning that it cannot meet its payment commitments. This may affect profit or loss should the company incur extra costs to meet its commitments or, in extreme cases, lead to insolvency and threaten the company's future as a going concern.

In order to mitigate this risk and to maintain a level of liquidity consistent with maintaining the requirements of its rating, Italgas signed finance agreements unused as at 31 December 2017. These credit lines (€1.1 billion) may be used to address possible liquidity needs, where necessary, if the actual borrowing requirement is higher than estimated. Also note that at the same date, in addition to the funding from the banking system, the Euro Medium Term Notes (EMTN) programme, approved by the Italgas Board of Directors on 23 October 2017, has allowed issue of the remaining bonds worth €850 million to be placed with institutional investors.

Italgas aims, in financial terms, at establishing a financial structure that, in line with its business objectives, ensures a level adequate for the group in terms of the duration and composition of the debt. The achievement of this financial structure will take place through the monitoring of certain key parameters, such as the ratio between debt and the RAB, the ratio between short-term and medium-/long-term debt, the ratio between fixed rate and floating rate debt and the ratio between bank credit granted and bank credit used.

#### **RATING RISK**

With reference to the long-term debt of Italgas, on 4 August and 12 October 2017, respectively, Fitch and Moody's confirmed the ratings assigned to Italgas S.p.A. (BBB+ with stable outlook and Baa1 with negative outlook).

Based on the methodologies adopted by the rating agencies, a downgrade of one notch in the Italian Republic's current rating could trigger a downward adjustment in Italgas' current rating.

#### **DEBT COVENANT AND DEFAULT RISK**

As at 31 December 2017, there were no financial covenants and collateralised bilateral and syndicated loan agreements in place with banks and other financial institutions. Some of these contracts provide, *inter alia*, for the following: (i) negative pledge commitments pursuant to which Italgas and its subsidiaries are subject to limitations on pledging real property rights or other restrictions on all or part of the respective assets, shares or merchandise; (ii) *pari passu* and change-of-control clauses; and (iii) limitations on certain extraordinary transactions that the Company and its subsidiaries may carry out.

The bonds issued by Italgas as at 31 December 2017 as part of the Euro Medium Term Notes programme provide for compliance with covenants that reflect international market practices regarding, *inter alia*, negative pledge and *pari passu* clauses.

Failure to comply with the commitments established for these loans - in some cases only when this non-compliance is not remedied within a set time period - and the occurrence of other events, such as cross-default events, some of which are subject to specific threshold values, may result in Italgas' failure to comply and could trigger the early repayment of the relative loan.

With reference to the EIB, the relative contracts contain a clause whereby, in the event of a significant reduction in EBITDA resulting from the loss of concessions, there is a disclosure obligation to the EIB and a subsequent consultation period, after which the early repayment of the loan may be required.

## OPERATING RISKS

The Italgas Group uses specific, certified management systems with the objective of overseeing the processes and business activities in accordance with the health and safety of workers, environmental protection and the quality and the energy effectiveness of services offered.

### RISKS ASSOCIATED WITH FAILURES AND UNFORESEEN INTERRUPTION OF DISTRIBUTION SERVICE

Managing regulated gas activities involves a number of risks of malfunctioning and unforeseeable distribution service disruptions from unintended events, such as accidents, breakdowns or malfunctioning of equipment or control systems, the under performance of plants, and extraordinary events such as explosions, fires, earthquakes, landslides or other similar events beyond Italgas' control. These related events could cause a decrease in revenue and involve substantial damage to persons, property or the environment. Although Italgas has taken out specific insurance policies in line with best practices to cover some of these risks, the related insurance coverage could be insufficient to meet all the losses incurred, the compensation obligations or cost increases.

### RISKS ASSOCIATED WITH ENVIRONMENTAL PROTECTION, HEALTH AND SAFETY

The activity of Italgas is subject to the Italian and European Union law on environmental protection.

Italgas conducts its business in compliance with the laws and regulations concerning the environment and safety. Given this, the possibility of the Group incurring significant costs or liability cannot be entirely ruled out. It is, in fact, difficult to foresee the economic and financial repercussions of any previous environmental damage, also in view of the possible effect of new laws or regulations that may be introduced for environmental protection, the impact of any new technologies for environmental clean-ups, possible litigation that arises and the difficulty in determining the possible consequences, also with respect to other parties' liability.

Italgas is engaged in the remediation of sites contaminated essentially due to manufactured gas production performed in the past, removal and disposal of waste (mainly for demolition of obsolete plant facilities) and disposal of materials containing asbestos.

To cover the liabilities estimated in relation to the formalities required by the law in effect, a special fund has been set up, amounting to €130 million.

### RISK ASSOCIATED WITH SMART METER INSTALLATION

At the end of 2010, Italgas initiated a plan to replace traditional meters with smart meters, until mid-2014 affecting classes higher than G6 and later also the mass market class.

In the first replacement phase, the new remote-read meters represent a technology that is still under development. For producers, the construction characteristics established by the Authority led to the need to plan and build a product, according to timing consistent with the obligations set by ARERA, targeting the Italian market only. Also note the complete availability only from 2015 of the reference technical regulations prepared by the CIG (Italian Gas Committee, regulator affiliated with the UNI).

Italgas began the installation of these devices in compliance with the calendar defined by ARERA. There is therefore the risk that the level of malfunctions is higher than past performances recorded for traditional meters and that this generates higher maintenance costs for the company.

#### **RISKS RELATED TO ENERGY EFFICIENCY CERTIFICATES**

Legislative Decree No. 164/00 concerning the liberalisation of the gas market, provides under Article 16.4 that distributors of natural gas for civil use are to pursue energy savings for the end users and the development of renewable energy; to this end, distributors are assigned the so-called Energy Efficiency Certificates, the annulment of which triggers a refund from the Energy and Environmental Services Fund on the basis of funds constituted through the RE (Energy Saving) components in the distribution fees.

To set the national savings amount per year to be pursued through the mechanism of the “white certificates”, the Authority determines its specific energy saving targets for electricity and natural gas distributors.

There is a potential risk of economic loss due to any negative difference between the mean purchase value of the certificates and the recognised tariff-based fee and the failure to achieve the targets set.

#### **RISKS ASSOCIATED WITH THE EXPIRATION AND RENEWAL OF GAS DISTRIBUTION CONCESSIONS**

The gas distribution activity that the Group Italgas performs operates by virtue of concessions issued by individual municipalities. As at 31 December 2017, Italgas managed 1,500 natural gas distribution concessions throughout Italy.

Inter ministerial Decree No. 226/11 ruled that the gas distribution service can only be performed on the basis of tendering procedures exclusively by ATEM, mainly provincial in dimension.

Under the tender processes launched, Italgas may not be awarded concessions in the planned areas, or may be awarded said concessions under conditions that are less favourable than the current conditions, with a possible negative impact on its operating results, financial position and cash flows. However, it must be noted that, in the event of failure to be awarded the concessions with regard to municipalities previously managed, Italgas would be entitled to the reimbursement amount provided to the outgoing operator (see next section).

It should also be noted that, in the context of procedures for the tenders initiated, Italgas may be awarded concessions in ATEM previously managed entirely or partially by other operators; therefore, it cannot be ruled out that such awards could lead, at least initially, to higher operating expenses for the Group than their standard operations.

Given the complexity of the regulations governing the expiration of the concessions held by Italgas, this could give rise to judicial and/or arbitral disputes between concession holders, with possible negative effects on the assets and on the economic and financial position of the Italgas Group.

#### **RISKS ASSOCIATED WITH THE REIMBURSEMENT AMOUNT PAID BY THE NEW OPERATOR**

With reference to the gas distribution concessions for which Italgas also owns the networks and facilities, Legislative Decree No. 164/00, as subsequently supplemented and amended, provides that the reimbursement amount paid to the outgoing service operators and owners of existing assignments and concessions is calculated in accordance with the provisions in the agreements or contracts, provided that they were concluded before the date of the regulation entering into force pursuant to Ministerial Decree No. 226 dated 12 November 2011 (i.e., before 11 February 2012). Further, and, to the extent not attributable to the will of the parties, as well as for aspects not governed by those agreements or contracts, based on the Guidelines on the criteria and procedures for assessing the reimbursement value, subsequently prepared by the Ministry of Economic Development with the document dated 7 April 2014 and approved by Ministerial Decree dated 22 May 2014<sup>17</sup>.

Where there is a disagreement between the local authority and the outgoing operator with regard to the reimbursement amount, the public notice contains a reference amount to be used for the purpose of the tender. This reference amount is the estimate of the contracting local authority or the RAB, whichever is greater.

Ministerial Decree No. 226/11 on the tender process criteria and bid evaluation, states that the incoming operator acquires ownership of the plant with the payment of the reimbursement to the outgoing operator, with the exception of any portions of the plant that are municipally owned.

Eventually, i.e., in subsequent periods, the reimbursement to the outgoing operator shall be the value of local net fixed assets, net of government grants for capital expenditure and private contributions relating to local assets, calculated on the basis of criteria used by the Authority to determine distribution tariffs (RAB).

In light of the new legal framework introduced, it cannot be ruled out that the reimbursement value of the concessions, which are assigned a third-party beneficiary upon conclusion of the tenders, would be less than the value of the RAB. This could lead to negative effects on the assets and the balance sheet, and the economic and financial situation of Italgas.

#### **CONCESSION-RELATED RISK**

The concessions envisage commitments for the concession holder, including investments. It cannot be excluded that, also due to delays in obtaining the authorisations and permits, these investments are made beyond the specified deadlines, with the risk that the company incurs charges.

<sup>17</sup> In other words, the specific methods provided for in the individual concession agreements entered into and effective prior to 11 February 2012 take precedence over the guidelines, albeit subject to the limitations set forth in the guidelines and in the tender criteria regulation mentioned in Ministerial Decree No. 226/11.

### REGULATORY RISK

Italgas carries out its activities in a gas sector subject to regulation. The relevant directives and legal provisions issued by the European Union and the Italian government and the resolutions of the ARERA and, more generally, changes to the regulatory framework, may have a significant impact on the operating activities, the economic results and the financial equilibrium of the Group.

Considering the specific nature of its business and the context in which Italgas operates, developments in the regulatory context with regard to criteria for determining the reference tariffs are particularly significant.

Future changes to European Union policies or at the national level, which may have unforeseeable effects on the relevant legislative framework and, therefore, on Italgas' operating activities and results, cannot be ruled out.

### LEGAL AND NON-COMPLIANCE RISK

Legal and non-compliance risk concerns the failure to comply, in full or in part, with rules and regulations at the European, national, regional and local levels with which Italgas must comply in relation to the activities it performs. The violation of such rules and regulations may result in criminal, civil and/or administrative penalties, as well as damage to the balance sheet, financial position and/or reputation. As regards specific cases, among other things, the infringement of regulations regarding the protection of workers' health and safety and of the environment, and the infringement of anti-corruption rules, may also result in (possibly significant) penalties for the Company, based on the administrative liability of entities (Legislative Decree No. 231/01).



## Business Outlook

Italgas will continue to pursue its strategic objectives focusing on the realisation of investments, the streamlining of processes and operating costs and the optimisation of the financial structure, whilst paying constant attention to development opportunities.



With specific reference to **technical investments** in property, plant and equipment and intangible assets, in 2018 and on a like-for-like basis, Italgas envisions expenses largely in line with the previous year, mainly for maintenance and development of the networks managed, implementation of the major smart meter installation programme and the completion of new networks under construction.

In accordance with the strategic priorities of the 2017-2023 Plan, Italgas will take part in **tenders of interest** for award of the natural gas distribution service, pursuing its business development goals and those to consolidate a sector that is still very fragmented.

In addition, in line with Strategic Plan objectives, after the acquisition in December 2017 of 100% of Enerco Distribuzione S.p.A., 2018 envisages the finalisation of further **development initiatives for external lines**, which will enhance territorial presence and the competitiveness of Italgas in future tenders, anticipating the effects in terms of growth of the scope of business.

Italgas intends to continue increasing its **operational efficiency**, pursuing the implementation of a cost reduction programme and improving the quality of processes and services launched in 2017. This project also aims to revise the organisational structure of Italgas Reti, characterised by a new territorial model and the simplification of operating processes, introducing a cultural change for the sustainability of the new model over time.

During 2018 Italgas will also continue actions aimed at **financial structure optimisation** of the Italgas Group by extending the average maturity of the debt and increasing the fixed-rate debt component, in line with its target financial structure.



## Legislative and regulatory framework

### ASSIGNMENT OF THE GAS DISTRIBUTION SERVICE AND RELATED LOCAL TENDER NOTICES

Italgas operates in a regulatory environment characterised by subsequent legislative acts aimed at implementing the provisions of Article 46-bis of Decree-Law No. 159/07. With this Decree, the legislature entrusted the Minister for Economic Development the task of defining the new criteria to define the criteria for calls for tenders referring to the distribution service, no longer for individual municipalities, but for minimum territorial areas, according to the identification of optimal user pools, based on the criteria of efficiency and cost savings.



In 2011, the Ministry of Economic Development adopted four reorganisation measures regarding the matter, described below.

The Areas Decree of 19 January 2011 established multi-municipality minimum geographical areas (ATEM) for which new gas distribution concessions must be assigned. The subsequent Decree of 18 October 2011 identified the municipalities that are part of the 177 ATEM.

Then on 12 November 2011, the Ministerial Decree was adopted, outlining the criteria for the tender and evaluation of the bids for the award of natural gas distribution services. The measure was subsequently amended by Decree of the Minister of Economic Development No. 106, in consultation with the Minister for Regional Affairs and Autonomy, on 20 May 2015, published in the Official Gazette No. 161 on 14 July 2015.

The measure contains instructions on preliminary aspects of the tender (including the participation requirements, the criteria for assessing bids, the value of the compensation to be paid to the outgoing operator, etc.), as well as the “standard” calls for tenders and the tender regulations. The reimbursement value for holders of expired contracts and concessions upon expiry is calculated in accordance with the provisions in the agreements or contracts, provided that they were concluded before the date the regulation became effective under Ministerial Decree No. 226 12 November 2011 (i.e., before 11 February 2012) and, for aspects which are not inferable from the specific intentions of the parties, as well as for aspects not governed by those conventions or contracts, the reimbursement value will be based on the Guidelines on criteria and procedures, subsequently stipulated by the Ministry of Economic Development and approved by Ministerial Decree dated 22 May 2014. In any case, private contributions relating to local assets, as valued according to the current tariff regulation methodology, shall be subtracted from the amount to be reimbursed. Where there is a disagreement between the local authority and the outgoing operator with regard to the reimbursement amount, the public notice contains a reference amount to be used for the purpose of the tender. This reference amount is the estimate of the contracting local authority or the RAB, whichever is greater. Once the dispute has been resolved, any difference will be settled between the incoming operator and the outgoing operator. Eventually, i.e., in subsequent periods, the reimbursement to the outgoing operator shall be the value of local net fixed assets, net of government grants for capital expenditure and private contributions relating to local assets, calculated on the basis of criteria used by the Authority to determine distribution tariffs (RAB).

The tenders will be awarded on the basis of the most economically advantageous bid, in accordance with criteria of safety, quality of service and development plans for the systems.

On 5 February 2013, the Ministerial Decree was finally adopted, approving the format for the service type contract to perform distribution activities.

#### MAIN PROVISIONS OF 2017 CONCERNING TENDERS

Article 128, paragraph 27-*quiquies*, Italian Legislative Decree 56/2017 amends Article 216 of Legislative Decree 50/2016 (the Tenders Code), establishing that: a) tender procedures for the award of gas distribution services continue to apply the provisions of Legislative Decree no. 164 of 23 May 2000, to the extent they are compatible with Part III of the Tenders Code, Article 46-*bis* of Legislative Decree 159/2007, on geographical areas and tender criteria, later defined by decrees adopted by the Ministry of Economic Development, and Article 4, Law Decree no. 69 of 21 June 2013, converted with amendments to Law no. 98 of 9 August 2013; b) the service concession period is determined pursuant to Article 168 of the Tenders Code, in any event without prejudice to the maximum duration of 12 years.

By **Resolution no. 344/2017/R/gas of 18 May 2017**, the Authority introduced a number of simplifications to the procedure for analysing RIV-RAB deviations, governed by Resolution no. 310/2014/R/gas, for the purpose of verifications prior to publication of the invitation to tender.

In particular, simplification applies:

- if the local authority (or contracting party, if delegated) can demonstrate for RIV assessment purposes the exclusive application of the Guidelines of 7 April 2014, approved by the Ministerial Decree of 22 May 2014;
  - if the municipalities in the area, other than that with the highest number of delivery points, with a population of up to 100,000 as recorded in the latest census, have gas distribution networks serving up to 10,000 delivery points.
- In such situations:
  - the local authority submits only the documentation referred to in Article 9.1, paragraph c) of Resolution no. 310/2014/R/gas to the Authority, specifying that it has applied only the Guidelines of 7 April 2014 to assess the installations;
  - the local authority must not submit (via the contracting party) all the detailed documentation necessary for verifying RIV-RAB deviations, but only make available such documentation if asked to do so by the Authority;
  - in relation to the declarations of exclusive application of the Guidelines, within 30 days of the contracting party's completion of the submissions of RIV-RAB deviations for the municipalities in the same geographical area, the Authority randomly requests detailed documentation as envisaged in Article 9.1, paragraphs a), b), d), e) and f) of Resolution no. 310/2014/R/gas for the purpose of systematic verifications referred to therein, without prejudice to the Authority's powers of control, also at a later date, to verify that the declarations are true.

The simplifications do not apply, however:

- in cases where some provisions of the Guidelines have been applied in combination with assessments based on arrangements stated in the concessions or agreements between the parties;
- for the reimbursement values relating to distribution networks located in the area's municipality with the highest number of delivery points and in other municipalities in the area with over 100,000 residents and over 10,000 delivery points.

These provisions apply with effect from the entry into force of the Resolution, published on 19 May 2017, and therefore do not apply to municipalities already acquired on the

RIV-RAB IT platform prior to said date of publication, for which the assessment procedure for RIV-RAB deviations by the Authority's departments is in progress.

Official Gazette no. 189 of 14 August 2017 published the **Annual Antitrust Law no. 124 of 4 August 2017**, in force from 29 August 2017.

The single Article, paragraphs 93, 94 and 95 of the law establishes rules to accelerate or simplify the tender procedures for the award of gas distribution services. In particular:

in relation to assessment of the RIV-RAB deviations exceeding 10%, the provision according to which the local authority submits detailed assessments of the reimbursement value to the Authority, for verification prior to publication of the tender, will not apply if the local authority self-certifies, also through a suitable third party, that:

- the reimbursement value was determined by applying the Guidelines contained in the Ministerial Decree of 22 May 2014;
- the aggregate RIV-RAB deviation for the area is not greater than 8%, provided that the deviation of a single municipality does not exceed 20%.

If the RAB value deviates from the sector averages, the value used in the deviation calculation is determined by applying the benchmark assessment criteria defined by the Authority;

- the Authority defines simplified procedures for assessing tender documents, applying in cases where the documents are prepared in compliance with the typical formats for the tender, regulations and service contract.

In any event, with reference to the maximum scores envisaged in Ministerial Decree no. 226/2011 for tender criteria and sub-criteria, the tender documents cannot deviate from certain sub-criteria except within the limits imposed by Articles 13, 14 and 15 of that Decree.

- for the purpose of participation in tenders as temporary business associations and ordinary consortia, the technical capacity requirements only need to be satisfied by one of the participants, as regards registration with the Chamber of Commerce for the capacity to operate as a gas distribution service provider, possession of UNI ISO 9001 certification and experience in operating in compliance with safety regulations, whilst the requirements relating to operating experience must be satisfied cumulatively by all participants.

By **Resolution no. 905/2017/R/gas of 27 December 2017**, following the consultation developed through the paper 734/2017/R/gas, the Authority implemented the provisions of the Antitrust Law no. 124/2017 on simplifying the regulations for the award of gas distribution services via tender.

To this end, the Resolution:

- approved the integrated texts of the Authority's provisions on determining and verifying the reimbursement value of networks and the tender assessment procedure;
- repealed the previous Resolutions 113/2013/R/gas, 155/2014/R/gas and 310/2014/R/gas, as the new integrated texts fully include the related provisions without significant new aspects.

With reference to calculation of the reimbursement value, the related integrated text specifies that verification of any deviation between RIV and RAB is performed by the Authority under three arrangements.

- standard municipality-specific arrangement;
- simplified municipality-specific arrangement;
- simplified arrangement per Italian Law 124/17.

The integrated text also specifies that, in the event of disagreement between the local authority and the outgoing operator, for the purpose of determining the deviation for the area, the reimbursement value is the higher of the two values.

For admission to the simplified individual municipality procedure, the local authority or contracting party, if delegated, makes a declaration available to the Authority confirming the application only of the Guidelines of 7 April 2014.

With reference to the tender assessment procedure, the related integrated text specifies that the verification is carried out by the Authority under standard or simplified arrangements.

Lastly, the Resolution envisages that:

- within 60 days of publication, for cases where the documentation relating to RIV-RAB deviations has already been submitted, the contracting parties formally advise the Authority of their intention to exercise the option envisaged in Law no. 124/17;
- specific in-depth studies were carried out on cost-benefit analyses in order to make a contribution at suitable institutional events, in coordination with the Ministry of Economic Development, to identifying criteria that encourage efficient infrastructural development;
- specific in-depth studies were carried out in relation to cases where the value

of fixed assets was clearly misaligned compared to the sector average, also through technical work groups of the distribution companies involving trade associations.

## ENERGY EFFICIENCY

In 2017, the main provisions on the issue of energy efficiency were as follows:

The **Decree of 11 January 2017** adopted by the Ministry of Economic Development in conjunction with the Ministry of the Environment was published in Official Gazette No. 78 of 3 April 2017. It determines the national quantitative energy saving targets for 2017 to 2020 and approves the new Guidelines for the preparation, execution and evaluation of energy efficiency project and for the definition of the criteria and methods for issuing White Certificates.

The main innovations compared with the previous ministerial decree of 28 December 2012 and the Guidelines attached to the resolution 9/11 of the EEN Authority include the new provision:

- relating to the verification of the achievement of the objectives, without prejudice to the expiry of the year of obligation, established as at 31 May of the subsequent year, introduces the possibility that obligated parties send the GSE the White Certificates they hold, for the purpose of fulfilling their obligations, twice a year, by 31 May and 30 November each year, rather than only once, as stipulated in the existing legislation;
- requires that, if the obligated party does not reach 100% of the obligated quota, but rather at least 60%, it can make up for the residual quota in the following year, rather than in the next two-year period, as previously, without incurring penalties;



- requires that there are 4 types of White Certificates confirming that energy savings have been achieved rather than 5 as there were previously;

The other provisions of the decree include annual national quantitative energy saving targets to be reached in the period 2017-2020 through the White Certificates mechanism, of:

- 7.14 million toe of primary energy in 2017;
- 8.32 million toe of primary energy in 2018;
- 9.71 million toe of primary energy in 2019;
- 11.19 million toe of primary energy in 2020.

The measures and interventions that allow gas distribution companies with more than 50,000 end users to comply with the annual national energy saving quantitative obligations for natural gas end users in the period 2017-2020, should produce a reduction in primary energy consumption, expressed in the number of White Certificates, in accordance with the following annual quantities and frequencies:

- 2.95 million White Certificates, to be obtained in 2017;
- 3.08 million White Certificates, to be obtained in 2018;
- 3.43 million White Certificates, to be obtained in 2019;
- 3.92 million White Certificates, to be obtained in 2020.

The share of obligations to be fulfilled by each individual gas distribution company is determined by the ratio between the self-certified quantity of natural gas distributed by said business to the end users connected to its network and the quantity of gas distributed nationally by all obligated parties, calculated annually by the Authority, counted in the year prior to the previous one. Said Authority notifies the Ministry of Economic Development and the GSE of these figures by 31 January of each year.

Any White Certificates issued in relation to projects carried out under the scope of Ministerial Decree 106 of 20 May 2015, based on tender criteria for gas distribution annulled by the GSE in the reference year, reduce the overall savings obligations for the next year in equal measure.

Except for the portion covered by other resources, the portion of the obligations compliance costs incurred by distributors is covered through electricity and natural gas transportation and distribution tariff elements.

Costs are covered, for each of the two transmission sessions for the Certificates held, in accordance with the criteria and methods defined by the Authority, to an extent that reflects the performance of the price of the White Certificates on the market, taking into account prices observed pursuant to free negotiations between the parties and with the definition of a maximum recognition value.

The decree, regarding which the opinions of the competent Parliamentary Committees and the Authority and the agreement of the Joint Conference were acquired, has been in force, with the relevant annexes that constitute an integral part thereof, since the day after publication in the Official Gazette and applies, with certain exceptions, to all projects submitted from that date.

The Authority defined the national energy efficiency annual quantitative obligations of natural gas end users to be achieved in 2017 by distributors with more than 50,000 end users connected to its distribution network as at 31 December 2015 through **resolution 6/2017 - DMRT of 12 April 2017**.

For subsidiaries and associates of Italgas S.p.A., the quantitative obligation for 2017, rounded off to the nearest whole number on a commercial basis and expressed as a number of White Certificates, is: 753,109 for Italgas Reti; 110,067 for Toscana Energia; 62,198 for Napoletanagas; 6,816 for ACAM Gas and 5,763 for Umbria Distribuzione Gas.

Through **Resolution 435/2017/R/efr of 15 June 2017**, in response to consultation paper 312/2017/R/efr of 5 May 2017, the Authority approved the revision of the rules for calculating the tariff contribution paid to electricity and gas distributors subject to the obligations under the scope of the Energy Efficiency Certificates (TEE) mechanism for the period 2017-2020.

The provision takes into account the amendments made to the mechanism by the Ministerial Decree of 11 January 2017 and the results of the preliminary investigation launched by the Authority through Resolution 710/2016/E/efr and approved through Resolution 292/2017/E/efr, with reference to the performance of the prices of TEE transactions on the market organised by the GME, from November 2016 onwards.

Specifically, the adjustments made to the rules for calculating the contribution already provided for by Resolution 13/2014/R/efr pursuant to the obligation years 2013-2016, include:

- for the establishment of the value of the contribution to be paid, the introduction of a “relevant session reference price”, calculated from the average price, with reference to a toe, weighted by the

relative quantities, only for transactions conducted during a market session and concluded at a price that is in a range of 312% compared with the previous market session relevant reference price. In order not to introduce retroactive amendments, the percentage parameter identified will be applied to market sessions after the date the Resolution came into force;

- the definition of a reference contribution (replacing the currently planned preliminary fee) for each obligation year from 2017, establishing:
- the calculation of the average definitive contributions for the two previous obligation years, through the weighting of the quantity of trades which took place on the market and the bilateral agreements in the previous two years, in order to also take into account these latest transactions;
- not to take into account, on the other hand, the trade prices via bilateral agreements;
- the confirmation of the elimination from the reference contribution formula of energy prices for domestic customers, no longer representative of the cost of the mechanism and the energy saving measures taken;
- through weighted coefficients which allow a better evaluation of the definitive contribution for the obligation year 2016, compared with 2015, because it is deemed more representative of the expected market liquidity for future years;
- the amendment of the parameters that make up the dimensionless coefficient  $k$  (to be applied, in the formula for calculating the definitive contribution, to the difference between the reference contribution and the average market trading prices), establishing, specifically, that: (i) the value  $\epsilon$  is amended progressively and, specifically, it remains unchanged at  $\epsilon/2/TEE$  for the next

obligation year 2017, in order to guarantee greater continuity with current provisions, and is defined at €4/TEE for subsequent years; (ii) the parameter € is immediately raised from 0.85 to 0.9 in order to achieve a more gradual approach to reaching the value € above or to ensure that the application of said € has a lesser impact;

- the introduction of an accruals basis in the definition of the tariff contribution made (i.e. its differentiation depending on whether certificates corresponding to the obligation year in progress are involved or recoveries from previous years, in which case the definitive contribution will be made for those obligation years), in place of the current cash criterion, starting from obligation year 2017 and excluding the recovery of residual targets, both for 2015 and for 2016;
- at the conclusion of the checks conducted by the GSE, the payment of a tariff fee on account with regard to distributors that send certificates for compliance with their obligations by 30 November each year, bringing forward the deadline of each obligation year pursuant to Article 14 of the Ministerial Decree of 11 January 2017, establishing, specifically: (i) the payment on account of the definitive unit tariff contribution for the previous year of obligation based on the quantity of certificates delivered by each distributor, in order to enable an initial recovery of the financial exposure of the distributors and limit the uncertainty due to market performance; (ii) a limit to the maximum quantity of certificates that can be handed over by distributors, set at 40% of the specific target for that obligation year and 100% (for gas distributors only, taking into consideration the increase pertaining to them for national targets and the difficulties related to the efficiency measures planned under the scope of the Ministerial Decree on gas tenders of 20 May 2015) for any residual portions of targets for previous obligation years that the distributor is responsible for.

In addition, with regard to the definitive unit tariff fee to be paid for the obligation year with reference to the quantity of certificates handed over by each company, by the end of 31 May set out in Article 14 of the Ministerial Decree of 11 January 2017, it is expected that from the obligation year 2017 the following will be paid:

- the definitive contribution for the current obligation year, in accordance with the certificates handed over for this year, until the respective obligations are met;
- the definitive contribution for the current obligation year (or the year in which the certificates are submitted), in compliance with any recoveries for each of the obligation years 2015 and 2016, until completed;
- the definitive contribution for the corresponding obligation year, in compliance with the certificates submitted for any recoveries for the obligation years after 2016, each until completed, also ensuring that the sums paid on the occasion of the checks conducted during the payment on account for each obligation years are deducted from these sums for each distributor.

Lastly, the Authority confirms two guidelines already expressed during the consultation, relating to:

- the absence of limits on the holding of TEEs, on accounts owned by voluntary parties, with no planned “expiry date” for TEEs issued by the GSE;
- the indication of no maximum reference value for the fee to be paid in an absolute sense, which would have constituted a “price signal” on the market.

Through **resolution DMRT/EFC/10/2017 of 14 July 2017**, the Authority established the following:

- the value of the definitive tariff contribution for 2016, equal to 191.40 €/TEE, calculated by applying the criteria pursuant to Resolution 13/2014/R/efr, and, specifically, the weighted average value of exchanges of certificates recorded on the organised market in the period between June 2016 and May 2017;
- the value of the reference contribution for 2017, equal to 170.29 €/TEE, calculated by applying the criteria pursuant to Resolution 435/2017/R/efr, and specifically the value of the definitive tariff contribution for 2015 and 2016 and the quantities of certificates exchanged on the market in the period between June 2015 and May 2017.

With reference to the energy saving obligations pertaining to Italgas, the minimum target for 2016, based on the quantities set by the rules and the calculations made by the regulator, is equal to 858,564 TEE; in the same year, Italgas acquired 662,413 TEE in its portfolio.

On conclusion of verification to confirm satisfaction of the energy saving obligation for 2016, including additional quotas deriving from offsetting for previous years, on 19 September 2017 the GSE announced details of the amounts of the advance for each electricity and natural gas distributor subject to the obligation, to cover the costs incurred. The amounts collected as at 30 September 2017 were: €114,790,810.20 for Italgas Reti, €10,189,179.00 for Napoletanagas and €1,805,859.00 for ACAM Gas.

Lastly, note that on 13 December 2017, on conclusion of verification to confirm satisfaction of the primary energy saving obligation for the 2017 advance session, the GSE announced details of the amounts of the advance for each electricity and natural gas distributor subject to the obligation, to cover the costs incurred in advance. The amounts recognised are: €138,621,067.20 for Italgas Reti and €17,849,581.20 for Toscana Energia.

Further decisions by the competent institutions are awaited.

## SAFETY OF THE GAS DISTRIBUTION AND METERING SERVICE

Through **Resolution 195/2017/S/gas of 30 March 2017, published on 4 April 2017**, the Authority imposed a fine of €204,000 on Italgas for violation of Article 12, paragraph 7, letter b) of the Consolidated Act on the regulation of the quality and tariffs for natural gas storage services for the 2009-2012 regulatory period (Annex A of Resolution ARG/gas 120/08 of 7 August 2008).

This provision stated that by 31 December 2010 distributors shall replace or recondition at least 50% of the lengths of any networks with cast-iron pipes with hemp- and lead-sealed joints, commissioned up to 31 December 2003. The replacement or reconditioning obligation refers to each distribution system.

The items acquired from the Authority Offices show that as at 31 December 2010, Italgas has had reconditioned approximately 21,308 metres out of a total of 53,533 metres of cast iron pipes with and hemp- and lead-sealed joints in commission as at 31 December 2003 on the Venice system, or approximately 39.79% of the total pipes to be reconditioned.

In the opinion of the Authority, the company was therefore in default with regard to the obligation set out in Article 12, paragraph 7, letter b) of the regulation.

On 29 May 2017, Italgas Reti filed an appeal before the Lombardy Regional Administrative Court of Milan, in order to annual Resolutions 195/2017/R/gas and 232/2017/R/gas, as well as all orders pertaining thereto and resulting therefrom.

## COMMERCIAL REGULATION OF THE GAS DISTRIBUTION AND METERING SERVICE

Through **Resolution 434/2017/R/gas** of 15 June 2017, in response to consultation paper 230/2017/R/gas of 6 April 2017, the Authority approved the provisions with regard to the launch of the trials concerning making the metering data with reference to the gas sector available to the Integrated Information System.

Law 129 of 13 August 2010, later supplemented by Law 27 of 24 March 2012, organised the establishment, at the Single Buyer, of an Integrated Information System (SII) for the management of information flows relating to the electricity and natural gas markets, based on a database of withdrawal points and identification data of end users, establishing that this System is also aimed at the management of information relating to electricity and gas consumption. It is therefore expected that in addition to information on withdrawal points and identification data for end users, the SII data base, the Official Central Register, will also collect data on electricity and gas consumption and that the SII will be responsible for managing them.

Through **Resolution 465/2017/R/gas** of 22 June 2017, the Authority launched a procedure aimed at the revision of the framework governing the gas distribution service network Code.

The Authority believes it is necessary to renew the framework governing service access and supply conditions in order to create a regulatory framework that responds better to the changes that have taken place in the economic climate and in the sector. Over the course of time, especially after the economic crisis, needs and problems have emerged (relating specifically to the management of the risk of default), which are not reflected in the clauses of the Code not impacted by later provisions by the Authority, such as invoicing for the service and user warranties.

The need to reform and update the Code has also been pointed out by various sector operators, including Italgas Reti; these reports highlight, among other things, two main areas of attention, which are distinct, but closely related:

- on the one side, the need to strengthen the instruments for containing credit risk, connected to violation of contractual terms and conditions by distribution users;
- on the other side, the need to clarify, and, in some cases, complete, the regulation in order to prevent the proliferation of conduct by several distribution companies to safeguard their receivables, with inappropriate consequences on sellers.

By **Resolution no. 522/2017/R/gas of 13 July 2017**, the Authority introduced measures to simplify and improve performance of the metering service for delivery points linked to the natural gas distribution network. As a result of the consultation developed through paper no.

518/2016/R/gas, the measure updates the Regulation of Service Quality in the Distribution and Metering of Gas for the period 2014-2019, making numerous amendments to Annex A to Resolution no. 574/2013/R/gas.

In particular, in relation to the accessible meters (traditional and smart):

- it introduces the definition of “successful reading” as a reading made by the distribution company of the measurement expressed by the numeric totalizer of an accessible meter. Meter readings performed directly by the end customer are excluded;
- it changes the specific standard relating to the metering frequency, envisaging that this standard refers to successful readings acquired by the company, and not to attempted readings in that, for accessible meters, the Authority considers that in general there is no external block on taking the reading and that, consequently, the effective carrying out of metering activities must be assessed on the basis of readings actually obtained and not attempts made;
- in order to monitor the performance of accessible meter readings, alongside the specific standard mentioned in the previous paragraph, a specific indicator is introduced, differentiated by consumer class based on the number of attempts envisaged in Article 14.1 of the Integrated Gas Sales Act.<sup>18</sup>

In order to simplify the formalities and therefore the costs to distribution companies, it is envisaged that partly accessible (traditional) meters are considered equivalent, for performance regulation purposes, to inaccessible meters, and therefore the same regulatory measures apply to such meters as defined for inaccessible (traditional meters).

In particular, it is envisaged that:

- the distribution company, in relation to every active delivery point with a partly accessible or inaccessible traditional meter, must guarantee at least one successful reading from 2018 onwards;
- if this obligation is not fulfilled, the distribution company must replace traditional meters with smart meters in the following year, guaranteeing that they become operative;
- these installation and operational start-up obligations are to be considered additional to the obligations already envisaged in Annex A to Resolution no. 631/2013/R/gas, in that the Authority considers the extra-cost associated with an individual replacement as opposed to mass replacement can be justified in terms of system-wide benefits;
- in line with the provisions of the tariff regulation, in the event of failure to comply with the replacement obligations, the distribution company is required to pay a lump-sum annual penalty of €4 for every partly accessible or inaccessible traditional meter not replaced with a smart meter.
- for each consumer band referred to in Article 14.1 of the Integrated Gas Sales Act, for meters not in service pursuant to Resolution no. 631/2013/R/gas (traditional), the number of active delivery points:
  - with meters partly accessible and partly inaccessible;

18 a) for delivery points with annual consumption of up to 500 Sm<sup>3</sup> per year: 1 attempted reading per year;  
 b) for delivery points with annual consumption of more than 500 Sm<sup>3</sup> and up to 1,500 Sm<sup>3</sup> per year: 2 attempted readings per year;  
 c) for delivery points with annual consumption of more than 1,500 Sm<sup>3</sup> and up to 5,000 Sm<sup>3</sup> per year: 3 attempted readings per year;  
 d) for delivery points with annual consumption of more than 5,000 Sm<sup>3</sup> per year: 1 attempted reading per month.



- with meters partly accessible and not inaccessible, and with no positive reading in the last year.

The Ordinary Supplement no. 62/L to Official Gazette no. 302 of 29 December 2017 published **Law no. 205 of 27 December 2017 (2018 State Budget)**.

Among the other provisions, the single article, paragraphs 4 to 10 of the Law introduced consumer protection measures as regards balancing invoices for the supply of electricity, gas and water services.

As a result of the new regulations, in electricity and gas supply contracts:

- the right to payment is prescribed as within two years, in relations between domestic users and the vendor and in relations between the distributor and the vendor, as well as in relations with the transport operator and other entities in the chain;
- if invoices are issued for payment of adjusting balances referring to periods of more than two years, where the Antitrust Authority has opened an investigation to ascertain violations of the Consumer Code pursuant to Legislative Decree 206/2005, relating to the consumption metering methods, enforcement of adjustments and invoicing, the user filing a complaint about the adjustment in the forms envisaged by the Authority has the right to withhold payment until the lawful nature of the operator's conduct has been verified;
- after such an investigation, the user in any event has the right to reimbursement within three months of any payments made against an unlawful adjustment;
- the previous provisions do not apply, however, when missing or incorrect consumption readings are confirmed as the liability of the user.

Through its own provisions, the Authority:

- within sixty days of the entry into force of the law, defines the measures on the timing of invoices between operators in the chain, necessary for the implementation of the new provisions;
- within three months of the entry into force of the law, defines consumer protection measures, determining the forms by which distributors guarantee that actual consumption data is ascertained and acquired;
- can define suitable measures to encourage self-reading, free of charge to the user;
- adopts provisions to ensure that, by 1 July 2019, the Integrated Information System (IIS) for managing information flows relating to the electricity and gas markets allows end customers to access data regarding their consumption, free of charge, subject to the adoption of necessary adjustments by the IIS manager.

These provisions apply to invoices with due dates, for the electricity sector, after 1 March 2018 and for gas after 1 January 2019.



## Sustainability and corporate responsibility

Italgas is a player of fundamental importance to the economic and social development of the country. The network span and roots across the country, in fact, allow the country to confirm itself to be a promoter of sustainable development, the result of connections and synergies between networks, geographical areas and the communities. This ensures that the company contributes to the creation of both social and economic value along the entire value chain, making skills, safety, reliability and innovation available to every stakeholder. Sustainability therefore becomes a crucial component of the business model. It agrees, in fact, with the definition of strategic and operating decisions, and guarantees long-term sustainable growth, without neglecting the expectations of shareholders and at the same time sharing the value generated, not only economic value but also social and environmental value, with all its stakeholders. Italgas activities are founded on the principles of transparency, honesty, fairness, good faith and full compliance with the rules on protecting competition, described in the Ethics Code adopted by all the Group companies, as guidelines for orientating the conduct of personnel and for responsible management of relationships with the stakeholders.



Business activities and processes are monitored through specific certified management systems, which cover aspects of occupational health and safety, environmental protection and the quality of services offered.

Ever since its establishment, Italgas has taken steps to prepare its Sustainability Report drawn up in accordance with the guidelines (GRI-G4) published by the Global Reporting Initiative. From 2017, Italgas includes non-financial information in a special report meeting the requirements of Legislative Decree no. 254 of 30 December 2016, issued in implementation of Directive 2014/95/EU on the disclosure of non-financial information by companies and large groups.

As regards, however, this report, the following provides some information related to personnel management, the environment, the fight against bribery and corruption, and the main social impacts relating to the business activities conducted by Italgas. To provide as full a disclosure as possible on the performance of these operations and guarantee comparability over time, the main operating data for 2017 of the Italgas Group is compared with 2016 figures, including consolidated figures for the conglomerate comprising Italgas S.p.A. since its incorporation (1 June 2016) and for Italgas Reti S.p.A., Napoletanagas S.p.A. and ACAM Gas S.p.A. from 1 January 2016<sup>19</sup>.

For further information with respect to the topics represented, see the Consolidated Non-Financial Statement.

### PEOPLE AND ORGANISATION

The Italgas business strategy is supported by a growth and development path that accompanies the Group's people to gaining specific skills, as well as by a culture of internal

<sup>19</sup> Certain data relating to personnel management also cover Enerco Distribuzione. Specifically: personnel as at 31 December 2017, breakdown of personnel by geographic area, by category, by contract type, by age range, by education level, average age of employees, percentages of female staff

sustainability. This, together with innovation and research, are required for the provision of an increasingly efficient, high quality service. Human capital development equates to the growth of the company itself.

## EMPLOYMENT

With a total increase of 14 compared to the previous year, Italgas had 3,584 personnel in service as at 31 December 2017. The changes in employment figures recorded during 2017 were as follows:

- the induction of 162 staff, of which 81 recruited from the job market, 70 Snam Group returns to service and 11 new staff from the acquisition of Enerco Distribuzione S.p.A.;
- a decrease of 148 staff relating to individual employment contract terminations.

The breakdown by category of personnel is as follows:

Breakdown of personnel by category (number)	2016	2017	Change
Executives	56	<b>60</b>	4
Managers	237	<b>251</b>	14
Office workers	1,896	<b>1,938</b>	42
Manual workers	1,381	<b>1,335</b>	(46)
	<b>3,570</b>	<b>3,584</b>	<b>14</b>

Almost all people at Italgas have an open-period employment contract; apprenticeships and access-to-work contracts represent around 4%.

172 individuals pertaining to protected categories work for Italgas and are included and integrated into the corporate processes.

## ORGANISATION

The achievement of objectives set in the strategic plan cannot disregard the capacity to actively respond to challenges in a continuously changing context and to constantly improve performance. The company has therefore launched organisational projects that will have an impact on processes and work methods. These included the Operations Reorganisation, the “Migliora” continuous improvement programme and the setup of the Professional Teams.

### The reorganisation of operations

In 2017, following an analysis carried out to define the best interaction methods between central and area units and to encourage simplification and streamlining of key operating processes, the central units (technical staff) and area units were reconfigured.

The reorganisation is an enormous opportunity for the professional development of resources, for addressing everyday problems in the area and to create skills centres for specialist activities and for business support.

### The Migliora Programme

The “Migliora” Continuous Improvement Programme is designed to increase efficiency and effectiveness of business activities and processes and to implement initiatives that can lead to tangible returns in terms of economic benefits and the

quality of service offered. The approach is characterised by a structured problem-solving method, based on the measurability of results and the use of Lean Six Sigma methodologies and tools, and a performance-based interfunctional operating method.



### The professional teams

15 professional teams were identified and created, designed to form a technical know-how pool and share operating methods, best practices and working tools, also through meetings and interaction between members.

### Training

Italgas training is aimed primarily at ensuring the growth of specific skills to guarantee that the business activities are conducted and the quality of service provided improves. Compared to 2016, the total volume of training activities (number of courses, training hours provided, attendees) increased with regard to managerial initiatives and those in support of organisational changes as a result of the new structure of the Italgas Group.

In 2017, 66 thousand hours of training were provided to 2,899 participants for a total of 9,175 participations. The number of hours' training per professional category were as follows:

Hours of training provided per category (number)	2016	2017	Change
Executives	792	<b>2,448</b>	1,656
Managers	7,563	<b>5,614</b>	(1,949)
Office workers	79,052	<b>38,050</b>	(41,002)
Manual workers	25,708	<b>19,888</b>	(5,820)
	<b>113,115</b>	<b>66,000</b>	<b>(47,115)</b>

Every Italgas employee has on average received around 18 hours of training in at least 2 different training opportunities during the year.

The most significant activities carried out in 2017 include the following:

- training on the history, expertise, values and distinguishing features of the Italgas identity, dedicated to graduates joining the Group in the last three years;
- inauguration of the Italgas Training Campus, designed to offer in-house training initiatives, workshops and projects in a welcoming, well-equipped structure;
- intercompany general management and knowledge sharing courses, courses on the main process optimisation methods, on digital innovation and on the improvement of soft skills;
- an induction course on the organisational context and the strategic guidelines of the Italgas growth plan, regulatory and operations aspects associated with the employment contract, the distribution operators, economics and finance basics for business and the key principles of teamwork;
- dissemination of the principles of the new Italgas organisational structure and the operations guidelines, the guidelines of the Italgas strategic plan and the introduction of professional teams;
- a training and change management course targeting Holding staff, designed to illustrate elements of the smart working methodology, principles of occupational health and safety and IT tools enabling remote working;
- a theory and practical training course on the awareness of legal, regulatory and procedural aspects of the safe management of emergency intervention activities and their application in business, with field testing exercises and continuous one-on-one activities;
- dissemination of C.I.G. Guidelines in application of UNI 11632;
- contact centre training on the use of workstations and the main processes and systems for call management, and the alignment of skills between operators;
- training on compliance issues (ethics code, model 231, internal control system on corporate information, enterprise risk management);
- technical training dedicated to system maintenance and know-how;
- “Safe Driving” courses.

In continuing with previous years, the commitment to training required by the applicable law on particular health issues, safety, environment and quality have been maintained.

All training courses on “health and safety” issues have been organised and delivered in accordance with the provisions of the State - Regions Agreement of 21 December 2011.

The foundations on which the development of human resources in Italgas is based are:

- the system of managerial skills, reference for the professional conduct of every member of staff, based on Initiative, Forward thinking, Relationships and Leadership;
- performance management, as an occasion dedicated to appraisal and gathering feedback on individual duties;
- the potential of every resource.

The human resource development activities are supported by occasions for assessment, which have proved to be fundamental even during the reorganisation of Italgas Reti S.p.A. in that they allowed a significant managerial turnover to be implemented: 60% have taken up new positions, 31 staff gained managerial roles.

#### **Initiatives in favour of employees**

To protect and encourage the well-being of its employees, Italgas makes services and



initiatives available that are designed to find a work-life balance. The initiatives undertaken during the year referred to:



- families, envisaging subsidies on spending, study grants and listening mechanisms;
- health and well-being through the signing of special agreements and the opportunity to arrange health check-ups;
- free time management schemes;
- sustainable mobility envisaging discounts on travel passes;
- savings and relations through the disbursement of bonuses, signing of special agreements and access to microcredit at preferential terms.

In November 2017 a survey of the entire corporate population was launched to analyse the needs and satisfaction of the initiatives currently offered with a view to identifying new services and strategies for implementation in 2018. Emerging from the survey was the importance of issues associated with health, income support and caring for family members, appreciation of the initiatives currently available and a request for solutions of benefit to older children and to care givers.

## HEALTH, SAFETY AND ENVIRONMENT

Through the Health Safety and Environment Policy, Italgas, in its prevention and protection principles, recognises the inalienable values and assumes a specific commitment for injury prevention, the protection of health and mitigation of the environmental impacts from its activities.



### HEALTH AND SAFETY

In 2017, a total of 24 accidents were recorded, of which 13 related to accidents at work and 11 while commuting. The total number of accidents corresponds to 1,246 days of total absence (829 without considering those while commuting) with a frequency index of 4.10 and a severity index of 0.21; excluding the commuting accidents, the frequency index is 2.22 and the severity index 0.14.

Workplace accidents	2016	2017
<b>Total non-commuting accidents</b>	<b>14</b>	<b>13</b>
- of which fatal	0	0
- of which work-related road accidents	4	5
- of which professional risks	1	2
- of which generic risks	9	6
<b>Total commuting accidents</b>	<b>9</b>	<b>11</b>
- of which fatal	0	0
<b>Total accidents</b>	<b>23</b>	<b>24</b>

Employee accident indices	2016	2017
Frequency index (non-commuting)	2.49	<b>2.22</b>
Severity index (non-commuting)	0.16	<b>0.14</b>
Frequency index (*)	4.09	<b>4.10</b>
Severity index (**)	0.23	<b>0.21</b>

(\*) accidents recorded / millions of hours worked; of which in 2017 3.75 male frequency index and 0.35 female frequency index.

(\*\*) days of absence due to accidents / thousands of hours worked; of which, in 2017, 0.20 male severity index and 0.01 female.

The company applies a regulatory system of rules, compliance standards, procedures and regulations with the aim of ensuring the health and safety of individuals (employees, end customers, contractors, etc.) and accident prevention, in terms of overall quality.

The organisational structure in terms of health, safety and environmental quality (HSEQ) envisages distinguishing general duties, centralised in Italgas, and specific duties, coordination and support for the operating units assigned to individual companies. These can operate with a suitable level of decision-making autonomy.

Italgas pays particular attention to raising staff awareness and training on the risks arising from operating activities and in implementing the safety requirements to be adopted to safeguard their own and others' safety. The growth of the "safety culture" is fuelled by many standard initiatives such as the "Italgas Safety Trophy" and the "Zero Accidents Award". The systematic recording of third-party operator accident figures continued in 2017 (7 workplace accidents for a total of 449 days' absence).

For staff exposed to specific risk factors Italgas implements periodic health surveillance. In 2017, 2,455 medical examinations were conducted on personnel exposed to specific risk factors.

#### ENVIRONMENTAL PROTECTION



All Italgas activities are conducted with maximum respect for the environment and natural resources, adopting a responsible and transparent approach that guarantees compatibility between its own infrastructures and the territory, efficiently managing natural and energy resources and limiting the environmental impact from its activities. This approach is explained in the HSEQ Policy. For environmental and energy management, the management systems adopted are those certified as compliant with ISO 14001 and ISO 50001, respectively.

In this reference context, Italgas promotes actions and projects designed to reduce environmental impact attributable to its own business processes, to improve system safety conditions, and the environmental restoration of sites that are potentially contaminated as a result of past gas production activities before the 1970s. The environmental revitalisation activities therefore continued at 31 sites for which environmental procedures are in progress pursuant to Legislative Decree 152/06.

The main initiatives include the conversion to natural gas of the vehicle fleet, the purchase

of electricity from renewable sources and the replace of old cast iron pipes with mechanical joints with equivalent pipes in PE/steel. Also note:

- launch of the conversions of LPG networks to natural gas for 8 districts in various parts of Italy, 2 of which already completed;
- launch of the final plans for a further 10 conversions to natural gas of networks currently using LPG.
- launch of the project to install gas supply columns for company vehicles, on Italgas operating premises, with 10 columns already installed at 4 locations which are added to the 7 already in operation at the Turin office.

The following is the main environmental impact data:

Emissions		2016	2017
Natural gas emissions	10 <sup>6</sup> Sm <sup>3</sup>	28.4	<b>28</b>
Total GHG emissions	10 <sup>3</sup> tonCO <sub>2</sub> eq	714	<b>657.3</b>
- of which Scope I (*)	10 <sup>3</sup> tonCO <sub>2</sub> eq	520	<b>513.9</b>
- of which Scope II	10 <sup>3</sup> tonCO <sub>2</sub> eq	9	<b>10.4</b>
- of which Scope III (**)	10 <sup>3</sup> tonCO <sub>2</sub> eq	185	<b>133.03</b>
<b>Carbon intensity (***)</b>	<b>tonCO<sub>2</sub>eq *10<sup>6</sup>Sm<sup>3</sup></b>	<b>69.6</b>	<b>66.2</b>
<b>NOx emissions</b>	<b>ton</b>	<b>32.8</b>	<b>32.2</b>

(\*) CO<sub>2</sub>eq emissions have been consolidated according to the operational control approach. The GHG gas included in the calculation are CO<sub>2</sub> and CH<sub>4</sub> and the emissions are calculated with a GWP of methane equal to 28, as indicated in the scientific study of the Intergovernmental Panel on Climate Change (IPCC) "Fifth Assessment Report IPCC".

(\*\*) Includes emissions associated with legal and business travel.

(\*\*\*) Calculated as Scope I emissions/gas distributed.

Energy consumption		2016	2017
Direct consumption primary of energy from renewable sources (A)	TJ	0	<b>0</b>
Direct consumption primary of energy from non-renewable sources (B)	TJ	475.6	<b>478.7</b>
- of which natural gas (C)	TJ	378.4	<b>381.4</b>
- of which diesel (D)	TJ	82.8	<b>79.6</b>
- of which petrol (E)	TJ	14.4	<b>17.7</b>
Electricity purchased (F)	TJ	99.8	<b>112.7</b>
Electricity self-generated from renewable sources (G)	TJ	0.13	<b>0.13</b>
Electricity sold (H)	TJ	0.06	<b>0.07</b>
<b>Total energy consumption (B+F+G-H)</b>	<b>TJ</b>	<b>575.4</b>	<b>591.4</b>
<b>Energy intensity (*)</b>	<b>TJ/10<sup>6</sup>Sm<sup>3</sup></b>	<b>77.03</b>	<b>76.14</b>

(\*) Total energy consumption out of the total gas distributed.

Italgas Reti and its subsidiaries are subject to reclamation obligations on certain sites where industrial activities have been carried out in the past, such as gas distillation or oil cracking for gas production. In 2017, the reclamation, environmental revitalisation and monitoring activities, conducted in compliance with the reclamation procedure in progress with the Public Administration, involved 32 sites.

## TECHNOLOGICAL INNOVATION AND RESEARCH



The innovation and technological development activities carried out by Italgas aim to improve the quality and safety standards of the service, to reduce the environmental impact of distribution and to increase overall efficiency of the distribution system.

In particular, a number of action areas were identified, including:

- **Digitisation of the gas networks**, through gas distribution networks that are not interconnected (via antenna) and which will be monitored using transducers, sensors and data capture devices that will transmit the information to a supervision centre. The information will be processed using algorithms that will allow any disservice due to breakdown and/or malfunction of the network to be predicted.
- **Pressure monitoring**, to identify the efficiency benchmark of the distribution system on the gas networks at low pressure.
- **Location of underground pipes**, using RFID markers, electronic labels comprising an integrated circuit and a short-wave data broadcasting antenna, which allow information to be obtained that can be used by the network owner and by companies operating on their behalf or for third parties (accurate reporting of the presence of other services adjacent to the gas pipes).
- **Targeted suspension of domestic gas supply in cases of default**, with the prototype development of a robot, in partnership with the biorobotics institute of the Sant'Anna School of Advanced Studies in Pisa, able to move inside the assembly columns to cut off gas services to customers in default.

The following projects also continued:

- the optimisation of odourising volume, with experimental evidence relating to an innovative system for the odourising levels to vary the gas delivery conditions or the network's fluid-dynamic structure;
- field testing of an injection system to optimise the odourising process of the LPG distribution networks, with the aim of guaranteeing the degree of saturation of the TBM odourising mix into the outflow from LPG stations, especially in the presence of very low flow capacities

Again in 2017, at the Italgas Reti Laboratory - technological centre of excellence able to operate to ISO standards - which has developed innovative systems and products for each production process and which oversees the various specialist activities associated with gas distribution, the following continued: rhino-analytical tests; gas odourisation instrument testing; calibration of gas meters and other support tools for gas distribution activities; mechanical testing on network materials. In particular, during the year the Italgas Reti LAB completed 23,585 actions, of which 10,382 accredited tests and 32 accredited calibrations.

## STAKEHOLDER RELATIONS

The Italgas Engagement system is present at all levels of the company.

Italgas maintains extensive relationships with investors, institutions and companies with the intention of offering a consistent service for the national and local needs and growth plans and encourage the continuous improvement of the reliability of the plant and the quality of services offered.

### INTERNAL COMMUNICATIONS AND CHANGE MANAGEMENT

Communication sent to Italgas staff strives to be a “change agent” acting on values, stimulating new views, contributing to the change of the corporate culture and inspiring new behaviours.

The Group’s intranet portal was immediately created and updated, right away becoming the preferred channel to disperse a new means of communicating: the home page has become the space where there is an alternation between news “in the foreground”, “highlighted” topics, the launch of corporate initiatives and pop-ups; innovations were introduced on the portal such as the gallery with videos and photos, as a tool to share, with the directness of pictures, experiences and company events.

Italgas has also decided to support the innovations in its organisation, systems and procedures with an articulated and consistent staff Training and Change Management Plan.

### INDUSTRIAL RELATIONS

In 2017, Italgas’s relations with trade unions focused on renewing the Gas and Water National Pay Agreement applying to the Italgas Group, signed on 18 May 2017, further studying numerous issues associated with topics referred to in the Decree, such as:

- the introduction of the concept of smart working;
- the introduction of “solidarity leave”, i.e. the option for employees to transfer flexible working hours, national holidays and annual leave without penalty, to allow colleagues to provide support to children requiring constant care;
- expansion of the concept of “safety” to also include environmental protection and sustainable development of production activities, with subsequent updating of the role of Workers Safety Representative, which has now become the Worker and Environmental Safety Representative;
- expansion of the contractual topics reported and any negotiations with the trade union representatives.

In 2017, Italgas was invited to form part of an important Work Group on Industrial Relations established by the Ministry of Economic Development.

The Work Group, composed by members from the Ministry of Economic Development, the Ministry for Labour and Social Policy and leading companies expressing different experiences and sensitivity, focused on analysing current trends in the country’s systems of industrial relations. In particular, the work group has prepared a document for the Government, useful in potentially identifying legislative intervention and actions which, in the short and medium terms, could orient the various stakeholders towards

an industrial relations model of real support to the Italian business system in a context of major change.

The involvement and effective participation of the Trade Unions, at national and local level, is fundamental to the signing of important agreements:

- geographical reorganisation of Italgas Reti and setup of the new Operating Hubs;
- launch of the pilot project in Italgas S.p.A. for smart working. At the end of 2017 an expansion of the aforementioned pilot project was agreed with the trade unions, and in 2018 will also involve the technical staff of Italgas Reti S.p.A.;
- extraordinary corporate transactions such as: the merger of Napoletanagas into Italgas Reti; the partial demerger of Italgas Reti due to the segregation of the water segment and incorporation of the new company Italgas Acqua S.p.A.;
- definition of the agreement relating to the payment of Group “Performance Bonus” which will also take into account the new Italgas welfare plan;
- launch of discussions for preparation of the new “Industrial Relations Protocol”.

In total, 67 meetings were held with the trade unions in 2017 (7 national and 60 local). Certain periods of tension with the trade unions at the launch of the new organisational structure of operations were overcome as a result of agreement on a national level procedures that saw the effective participation of the areas in implementing the new operations model of Italgas Reti.

At the end of 2017, 54% of employees were members of a trade union.

The legal dispute with employees and former employees of the Italgas Group has reached a number, on average remaining steady over time but reducing slightly in 2017. The typical cases refer to category differences and related remuneration, economic claims and claims against disciplinary measures inflicted, including cases of dismissal.

### INVESTOR RELATIONS

Italgas, since its listing on the stock market, has placed transparency in its relationships with investors and the entire financial community among its top priorities. The Company's plans and objectives, and likewise the quarterly and annual results, were presented to shareholders and to the market to allow an assessment of the value creation levers. In 2017, a roadshow was held, reaching the major European and North American financial markets. Management presented the 2017-2023 Business Plan to over 260 investors in 90 one-to-one meetings, 37 group meetings and a number of sector conferences.

At the beginning of 2017, at the launch of the first bond issue in implementation of the EMTN programme approved by the Italgas Board of Directors on 18 October 2016, major promotional activity was carried out for the bond investors and credit analysts through a dedicated roadshow in major European financial centres. Management presented the company's plans and objectives to over 110 investors in 17 one-to-one meetings and 7 group meetings.

The information of interest to shareholders and investors, including the quarterly/semi-annual reports, both in Italian and in English, will be available in the Investor Relations section of the corporate website [www.italgas.it](http://www.italgas.it).



### COMMUNITIES AND LOCAL AREAS

Italgas, consistent with its role as the provider of gas distribution services, with the principles of sustainable development and its growth plans, is constantly engaged in a continuous and effective dialogue with the communities in which it operates. In relations to the European, national and local authorities, Italgas operates on the principles of sincere cooperation and transparency by providing its skills and abilities, conscious of the social utility of its role. The commitment to openness has resulted in joining Registries for formal transparency as formally instituted by the European Parliament, the Register of Stakeholders of the Chamber of Deputies, the Ministry of Economic Development and the Region of Lombardy.

Italgas also attaches great importance to cooperation in the field associated with the other operators in the energy sector, on an equal and fair field of comparison. Finally, the construction of cooperative relationships with the associations representing consumers helps people understand and respond as best as possible to the needs and expectations of the users of its services.



In 2017, Italgas also signed an agreement with 14 of the largest consumer associations recognised by the Italian National Consumer and User Council (CNCU). The aim of the agreement is to disseminate a culture about gas that makes the consumer increasingly aware and informed on the correct use of energy resources and the programme for replacing traditional gas meters with smart meters. The protocol also aims to identify the most suitable forms of cooperation to mitigate the phenomenon and manage any reports in as short a time as possible.

### CUSTOMERS AND THE REGULATORY AUTHORITY FOR ENERGY, NETWORKS AND ENVIRONMENT

Italgas pays special attention to the relationship with the sales company, constantly updating the tools and procedures that allow access to services.

The operating and commercial activities are carried out with an increasingly sophisticated computer systems that allow for a rapid flow of information in contract management. These systems are constantly updated on the basis of regulations issued by the ARERA, which are constantly regulating the services of the Italgas Group.

Relations with the ARERA are of key importance for companies operating in the energy business. Since its establishment, Italgas has presented the Authority, continuously as in the past, a constructive and purposeful relationship, which translates for example into ensuring the Group's contribution to the consultation processes for preparing Resolutions and illustrating specific issues in the sector and supplying the information required by the regulator.



### SUPPLIERS

Italgas adopts purchasing practices based on the principles of transparency, fairness and responsibility, respect for free competition and pursuing the achievement of economic objectives and performance also in the long run.

Italgas requires suppliers to adopt Model 231 and the principles of the Ethics Code in compliance with the law on safety at the workplace, health protection, environmental protection and respect for the international standards concerning the right to work.

Suppliers are also involved in a process of improving and optimising the procedures that regulate subcontracting, which leads to greater empowerment of the subcontractor ensuring growth of the supplier and a better quality of work carried out for the Company. Arrangements were made in 2017 to streamline the Vendor List, adapting to Italgas requirements and therefore maintaining different Suppliers and their associated Product Groups. In addition, a development project was launched for the proprietary Vendor Management System to assess supplier performance. The suppliers' portal was supplemented in various sections to improve and optimise the day-to-day operations of everyone involved in the management of the entire supply chain.



## Glossary

A glossary of financial, commercial and technical terms, as well as units of measurement, is available online at [www.italgas.it](http://www.italgas.it).

### ECONOMIC AND FINANCIAL TERMS

#### NON-CURRENT ASSETS

Balance sheet item which shows long-lasting assets, net of amortisation, depreciation and impairment losses. They are divided into the following categories: "Property, plant and equipment", "Compulsory inventories", "Intangible assets", "Equity investments", "Financial assets" and "Other non-current assets".

#### CASH FLOW

Net cash flow from operating activities is represented by the cash generated by a company over a certain period of time. Specifically, the difference between current inflows (mainly cash revenue) and current cash outflows (costs in the period that generated cash outflows).

#### CONTROLLABLE FIXED COSTS

Fixed operating costs of regulated activities, represented by the sum of "Total recurring personnel costs" and "Recurring external operating costs".

#### COVENANTS

A covenant is an undertaking within a loan agreement whereby certain activities can or cannot be carried out by the borrower. Specifically, a covenant is defined as "financial" when it imposes a limit relating to the possibility of taking out a further loan, while in covenants relating to property, the clauses are aimed, inter alia, at limiting the use of financial leverage by the company, involving the obligation of maintaining a given ratio between balance sheet debt and capitalisation.

These obligations are imposed by lenders to prevent the financial conditions of the

borrower from deteriorating and, where this does happen, to be able to request the early repayment of the loan.

#### CREDIT RATING

Represents the opinion of the rating agency with respect to a debtor's general credit or the debtor's creditworthiness with specific reference to a particular debt instrument or another form of financial obligation, based on the relevant risk factors; the classification of various risk levels is made using letters of the alphabet and with essentially the same procedures by the various agencies.

#### DIVIDEND PAYOUT

Ratio between the dividend and net profit for the period, and equal to the percentage of profits paid out to shareholders in the form of dividends.

#### OUTLOOK

The outlook indicates the future rating prospects over a long period of time, usually two years. When it is "negative" it means that the rating is weak and that the rating agency has detected some critical elements. If the weakness factors persist or worsen, the rating may be downgraded.

#### NOTCH

Risk level assigned by the rating agency, as part of the process of assigning the credit rating, which corresponds to a probability of default, i.e. of the issuer.

#### CONSOLIDATED FINANCE ACT (TUF)

Legislative Decree No. 58 of 24 February 1998, as amended.

#### COMPREHENSIVE INCOME

Includes both net income for the period and changes in equity, which are recognised in equity in accordance with international accounting standards (Other components of comprehensive income).

## COMMERCIAL AND TECHNICAL TERMS

### THERMAL YEAR

Time period into which the regulatory period is divided. Starting from the third regulatory period, the thermal year coincides with the calendar year.

### ARERA

The Italian Regulatory Authority for Energy, Networks and Environment (ARERA), formerly the Electricity, Gas and Water System Authority (AEEGSI), is an independent body set up by Law no. 481 of 14 November 1995 to protect the interests of consumers and promote competition, efficiency and dissemination of services with adequate levels of quality, through regulation and control activities. The Authority's action, initially limited to the electricity and natural gas sectors, was later extended through a number of regulatory measures, in particular through Law Decree 201/11, converted to Law 214/11, to assign responsibility also for water services.

### ATEM

Minimum Geographical Areas (ATEMs) for conducting tenders and assigning the gas distribution service, calculated as 177 pursuant to the definition of Article 1 of the Ministerial Decree of 19 January 2011. The Municipalities belonging to each area are listed in the Ministerial Decree of 18 October 2011.

### ENERGY AND ENVIRONMENTAL SERVICES FUND - CSEA

Public economic institution that operates in the fields of electricity, gas and water. Its primary mission is the collection of certain tariff components by operators; these components are collected in dedicated management accounts and subsequently disbursed to businesses according to the rules issued by the Authority. The CSEA is supervised by the Authority and the Ministry of Economy and Finance. The CSEA also, in relation to the entities administered, performs inspection activities aimed at administrative, technical, accounting

and management assessments, consisting in hearing and comparing the entities involved, with recognition of locations and systems, research, testing and comparison of documents.

### END USER

The consumer who buys gas for their own use.

### NETWORK CODE

The document governing the rights and obligations of the parties involved in providing the gas distribution service.

### GAS DISTRIBUTION CONCESSION

The deed by which a local authority entrusts to a company the management of a natural gas distribution service which falls within the remit of said authority, and for which said company assumes the operational risk.

### LOCAL TENDER

The local tender is the sole tender process for the provision of gas distribution services held in each of the 177 minimum geographical areas (ATEM) identified pursuant to Articles 1 and 2 of the Decree of the Ministry of Economic Development of 19 January 2011.

### GAS DISTRIBUTED OR CIRCULATED

Amount of gas delivered to users of the distribution network at the delivery points.

### EQUALISATION

Difference between revenues for the period (annual TRL) and those invoiced to retail companies. The net position with the CSEA is established at the end of the thermal year and settled over the course of the year on the basis of advance payments.

### REGULATORY PERIOD

This is the time period for which criteria are defined for setting tariffs for gas distribution services. The third regulatory period ended on 31 December 2013. The fourth regulatory period is now in progress, beginning on 1 January 2014 and ending on 31 December 2019.

**DELIVERY POINT**

This is the point of demarcation between the gas distribution plant and the plant owned or managed by the end user at which the distribution company redelivers gas transported for supply to the end user, and at which metering occurs.

**GAS DISTRIBUTION SERVICE**

Service of transporting natural gas through networks of local methane pipelines from one or more delivery points to redelivery points, generally at low pressure and in urban areas, for delivery to end users.

**RETAIL COMPANY OR RELCO (RETAIL COMPANY)**

Company which, by way of a contract giving it access to the networks managed by a distributor, sells the gas.

**REGULATORY ASSET BASE (RAB)**

The term RAB (Regulatory Asset Base) refers to the value of net invested capital for regulatory purposes, calculated on the basis of the rules defined by the Regulatory Authority for Energy, Networks and Environment (ARERA) for determining the reference tariff.

**CENTRALISED RAB**

The Centralised Regulatory Asset Base is made up of tangible fixed assets other than those included under local tangible fixed assets and intangible fixed assets (in other words non-industrial buildings and property, other tangible fixed assets and intangible fixed assets, such as, for example, remote management and remote-control systems, equipment, vehicles, IT systems, furniture and furnishings, software licenses).

**LOCAL RAB**

The Local Regulatory Asset Base for the distribution service consists of the following types of tangible fixed assets: land on which industrial buildings, manufacturing buildings, major and minor plants, road

and pipeline installations (connections) are located. Local Regulatory Asset Base relating to the metering service is made up of the following types of tangible fixed assets: traditional metering equipment and electronic metering equipment.

**REIMBURSEMENT VALUE**

The Reimbursement Value is the amount owed to outgoing operators on the termination of the service pursuant to Article 5 of the Decree of the Ministry of Economic Development No. 226 of 12 November 2011 in the absence of specific different calculation method forecasts contained in the documents of the individual concessions stipulated before 11 February 2012 (the date when Ministerial Decree No. 226/2011 came into force).

**RIV OR RESIDUAL INDUSTRIAL VALUE**

The residual industrial value of the part of the plant owned by the outgoing operator. It is equal to the cost that should be incurred for its reconstruction as new, reduced by the value of the physical degradation and also including non-current assets under construction as indicated from the accounting records (Article 5(5) of Ministerial Decree No. 226/2011).

**TRL (TOTAL REVENUE LIMIT)**

Total revenue allowed for distribution companies by the regulatory body to cover costs for providing distribution and metering services.

**WACC**

Weighted Average Cost of Capital. Rate of return on net invested capital.







# **CONSOLIDATED FINANCIAL STATEMENTS**



## STATEMENT OF FINANCIAL POSITION

(€ thousands)

31.12.2016

31.12.2017

	Note	Total	of which related parties	Total	of which related parties
<b>ASSETS</b>					
<b>Current assets</b>					
Cash and cash equivalents	(8)	1,544		2,831	
Other financial assets held for trading or available for sale	(9)	119		119	
Trade and other receivables	(10)	579,090	255,856	619,202	225,387
Inventories	(11)	32,581		22,410	
Current income tax assets	(12)	34,607		8,571	
Other current tax assets	(12)	3,318		21,139	
Other current assets	(13)	4,410	18	5,944	30
		<b>655,669</b>		<b>680,216</b>	
<b>Non-current assets</b>					
Property, plant and equipment	(14)	227,476		224,651	
Intangible assets	(15)	4,486,511		4,676,561	
Investments valued using the equity method	(16)	175,707	175,707	184,829	184,829
Other investments	(16)	54	54	54	54
Other financial assets	(10)	156		156	
Other non-current assets	(13)	37,874	706	77,891	702
		<b>4,927,778</b>		<b>5,164,142</b>	
<b>Non-current assets held for sale</b>	(17)	<b>24,949</b>		<b>11</b>	
<b>TOTAL ASSETS</b>		<b>5,608,396</b>		<b>5,844,369</b>	

(€ thousands)

31.12.2016

31.12.2017

	Note	Total	of which related parties	Total	of which related parties
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>					
<b>Current liabilities</b>					
Short-term financial liabilities	(18)	2,695,603		81,133	
Short-term portions of long-term financial liabilities	(18)	435		25,043	
Trade and other payables	(19)	443,112	73,023	498,174	72,469
Current income tax liabilities	(12)	945		4,489	
Other current tax liabilities	(12)	12,515		11,424	
Other current liabilities	(20)	193	190	182	175
		<b>3,152,803</b>		<b>620,445</b>	
<b>Non-current liabilities</b>					
Long-term financial liabilities	(18)	923,005		3,617,044	
Provisions for risks and charges	(21)	230,524		208,246	
Provisions for employee benefits	(22)	120,648		116,149	
Deferred tax liabilities	(23)	106,276		94,790	
Other non-current liabilities	(20)	4,876	165	2,055	165
		<b>1,385,329</b>		<b>4,038,284</b>	
<b>Liabilities directly associated with assets held for sale</b>	(17)	<b>5,970</b>			
<b>TOTAL LIABILITIES</b>		<b>4,544,102</b>		<b>4,658,729</b>	
<b>SHAREHOLDERS' EQUITY</b>					
	(24)				
<b>Italgas shareholders' equity</b>					
Share capital		1,001,232		1,001,232	
Reserves		134,383		(108,358)	
Profit (loss) for the year		(72,209)		292,766	
Treasury shares					
<b>Total Italgas shareholders' equity</b>		<b>1,063,406</b>		<b>1,185,640</b>	
<b>Minority interests</b>		<b>888</b>			
<b>TOTAL SHAREHOLDERS' EQUITY</b>		<b>1,064,294</b>		<b>1,185,640</b>	
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>		<b>5,608,396</b>		<b>5,844,369</b>	

INCOME STATEMENT<sup>20</sup>

(€ thousands)		Jun-Dec 2016 (*)		2017	
	Note	Total	of which related parties	Total	of which related parties
<b>REVENUE</b>	(26)				
Core business revenue		247,672	202,300	1,570,929	749,397
Other revenue and income		26,050	5,556	50,112	24,999
		<b>273,722</b>		<b>1,621,041</b>	
<b>OPERATING COSTS</b>	(27)				
Purchases, services and other costs		(110,497)	(15,206)	(613,112)	(44,623)
Personnel cost		(57,269)	1,311	(231,685)	6,458
		<b>(167,766)</b>		<b>(844,797)</b>	
<b>AMORTISATION, DEPRECIATION AND IMPAIRMENT</b>	(28)	<b>(76,802)</b>		<b>(358,342)</b>	
<b>EBIT</b>		<b>29,154</b>		<b>417,902</b>	
<b>FINANCIAL INCOME (EXPENSE)</b>	(29)				
Financial expense		(123,159)	(121,317)	(37,334)	(466)
Financial income		359		1,085	
<b>INCOME (EXPENSE) FROM EQUITY INVESTMENTS</b>	(30)	<b>(122,800)</b>		<b>(36,249)</b>	
Equity method valuation effect		3,105		22,958	
Other income (expense) from equity investments				15	
		<b>3,105</b>		<b>22,973</b>	
<b>PRE-TAX PROFIT</b>	(31)	<b>(90,541)</b>		<b>404,626</b>	
Income taxes		18,332		111,860	
<b>Profit (loss) for the year</b>		<b>(72,209)</b>		<b>292,766</b>	
Attributable to:					
- Italgas		(72,209)		292,766	
- Minority interests					
<b>Net profit (loss) per share (€ per share)</b>	(32)				
- basic		(0.09)		0.36	
- diluted		(0.09)		0.36	

20 The consolidated Income Statement for 2016 is prepared on the basis of the figures for Italgas S.p.A. from the date of establishment (1 June 2016) and the subsidiaries from the date of acquisition of control (7 November 2016).

## STATEMENT OF COMPREHENSIVE INCOME

(€ thousands)	Jun-Dec 2016	2017
Net profit	(72,209)	292,766
Other components of comprehensive income		
Components that can be reclassified to the income statement:		
Components that cannot be reclassified to the income statement:		
Actuarial gains (losses) on remeasurement of defined-benefit plans for employees	3,696	(1,457)
Tax effect	(1,042)	411
	2,654	(1,046)
Total other components of comprehensive income, net of tax effect		
Total comprehensive income for the year	(69,555)	291,720
Attributable to:		
- Italgas	(69,555)	291,720
- Minority interests		
	(69,555)	291,720

(€ thousands)

	Shareholders' equity pertaining to owners of the parent		
	Share capital	Consolidation reserve	Share premium reserve
<b>Balance as at 1 June 2016 (a)</b> (Note 24)			
<b>2016 profit for the year</b>			
<b>Other components of comprehensive income:</b>			
<b>Components that cannot be reclassified to the income statement:</b>			
- Actuarial gains on remeasurement of defined-benefit plans for employees			
<b>Total comprehensive income 2016 (b)</b>			
<b>Transactions with shareholders:</b>			
- Effect of the acquisition of Italgas Reti from Snam S.p.A.	1,001,232	(316,385)	620,130
<b>Total transactions with shareholders (c)</b>	<b>1,001,232</b>	<b>(316,385)</b>	<b>620,130</b>
<b>Other changes in shareholders' equity (d)</b>			
<b>Balance as at 31 December 2016 (e=a+b+c+d)</b> (Note 24)	<b>1,001,232</b>	<b>(316,385)</b>	<b>620,130</b>



Legal reserve	Reserve for defined benefit plans for employees, net of tax effect	Reserve for business combinations under common control	Net profit for the year	Total	Minority interests	Total shareholders' equity
			(72,209)	(72,209)		(72,209)
	2,654					
	<b>2,654</b>		<b>(72,209)</b>	<b>(69,555)</b>		<b>(69,555)</b>
192,236	(14,398)	(349,854)		<b>1,132,961</b>	888	<b>1,133,849</b>
<b>192,236</b>	<b>(14,398)</b>	<b>(349,854)</b>		<b>1,132,961</b>	<b>888</b>	<b>1,133,849</b>
<b>192,236</b>	<b>(11,744)</b>	<b>(349,854)</b>	<b>(72,209)</b>	<b>1,063,406</b>	<b>888</b>	<b>1,064,294</b>

## STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

(€ thousands)

	Shareholders' equity pertaining to owners of the parent			
	Share capital	Consolidation reserve	Share premium reserve	Legal reserve
<b>Balance as at 31 December 2016 (a)</b> (Note 24)	1,001,232	(316,385)	620,130	192,236
<b>2017 profit for the year</b>				
<b>Other components of comprehensive income:</b>				
<b>Components that can be reclassified to the income statement</b>				
<b>Components that cannot be reclassified to the income statement:</b>				
Actuarial gains on remeasurement of defined-benefit plans for employees				
<b>Total comprehensive income 2017 (b)</b>				
<b>Transactions with shareholders:</b>				
- Allocation of 2016 profit for the year				
- Allocation of Italgas S.p.A. dividend for 2016 (€0.20 per share)				
- Allocation of residual Italgas S.p.A. profit for 2016				8,010
- Effect of 100% acquisition of Napoletanagas				
- Earn-out effect Roma Ostiense		(7,522)		
- Reserve reclassification				
<b>Total transactions with shareholders (c)</b>		(7,522)		8,010
<b>Other changes in shareholders' equity (d)</b>				
<b>Balance as at 31 December 2017 (e=a+b+c+d)</b> (Note 24)	1,001,232	(323,907)	620,130	200,246

	Reserve for defined benefit plans for employees, net of tax effect	Reserve for business combinations under common control	Other reserves	Retained earnings	Net profit for the year	Total	Minority interests	Total shareholders' equity
	(11,744)	(349,854)			(72,209)	1,063,406	888	1,064,294
					292,766	292,766		292,766
	(1,046)					(1,046)		(1,046)
	(1,046)				292,766	291,720		291,720
				(72,209)	72,209			
			(161,827)			(161,827)		(161,827)
			(8,010)					
			(137)			(137)	(888)	(1,025)
						(7,522)		(7,522)
	(561)		561					
	(561)		(169,413)	(72,209)	72,209	(169,486)	(888)	(170,374)
	(13,351)	(349,854)	(169,413)	(72,209)	292,766	1,185,640		1,185,640

## STATEMENT OF CASH FLOWS

(€ thousands)	Note	Jun-Dec 2016	2017
Profit (loss) for the period		(72,209)	292,766
Adjustments for reconciling net profit with cash flows from operating activities:			
Amortisation and depreciation		76,802	352,001
Net impairments of property, plant and equipment and intangible assets			6,341
Equity method valuation effect	(16)	(3,105)	(22,958)
Net capital losses (capital gains) on asset sales, cancellations and eliminations		667	4,124
Dividends			(15)
Interest income		(355)	(836)
Interest expense		121,908	30,423
Income taxes	(31)	(18,332)	111,860
Changes in working capital:			
- Inventories		(7,651)	10,306
- Trade receivables		(33,550)	12,423
- Trade payables		51,942	8,365
- Provisions for risks and charges		20,857	(22,456)
- Other assets and liabilities (*)		7,999	(112,193)
Cash flow from working capital		39,597	(103,555)
Change in provisions for employee benefits		(4,547)	(4,907)
Dividends collected			13,820
Interest income		355	836
Interest expense		(121,908)	(30,423)
Income taxes paid net of reimbursed tax credits		(64,428)	(102,765)
<b>Net cash flow from operating activities</b>		<b>(45,555)</b>	<b>546,712</b>
- of which, related parties	(33)	(110,017)	766,791

(€ thousands)	Note	Jun-Dec 2016	2017
Investments:			
- Property, plant and equipment	(14)	(5,674)	(10,867)
- Intangible assets	(15)	(73,782)	(482,435)
- Change in scope of consolidation and business units (**)		(1,502,950)	(35,941)
- Change in payables and receivables for investments		14,844	30,754
Cash flow from investments		(1,567,562)	(498,489)
Disinvestments:			
- Property, plant and equipment		73	
- Intangible assets			419
- Disposals of operating assets			21,961
- Change in receivables relating to disinvestment activities		(1)	(1)
Cash flow from disinvestments		72	22,379
<b>Net cash flow from investment activities</b>		<b>(1,567,490)</b>	<b>(476,110)</b>
- of which, related parties	(33)	(1,502,950)	
Assumption of long-term financial payables		927,528	3,011,855
Repayment of long-term financial payables		(1,441,400)	(300,355)
Increase (decrease) in short-term financial payables		2,128,461	(2,618,988)
Dividends distributed to Italgas shareholders			(161,827)
<b>Net cash flow from financing activities</b>		<b>1,614,589</b>	<b>(69,315)</b>
- of which, related parties	(33)		(64,003)
<b>Net cash flow for the year</b>		<b>1,544</b>	<b>1,287</b>
<b>Cash and cash equivalents at the beginning of the year</b>	<b>(8)</b>		<b>1,544</b>
<b>Cash and cash equivalents at the end of the year</b>	<b>(8)</b>	<b>1,544</b>	<b>2,831</b>

(\*) For 2017, the item includes the payables taken over by Italgas Reti on behalf of Enerco Distribuzione for €2,799 thousand.

(\*\*) For 2017, the item includes the investment in Enerco Distribuzione, net of cash received and the purchase of the residual minority interest of Napoletana Gas S.p.A.





## Notes to the consolidated financial statements

### COMPANY INFORMATION

On 7 November 2016 the transaction of acquiring the gas distribution sector from Snam was brought to a conclusion following the transfer of the 100% stakeholding of Italgas Reti S.p.A. (previously called Italgas S.p.A.) from Snam S.p.A. to Italgas S.p.A., a company that was incorporated on 1 June 2016 and which took that name on 12 September 2016.

The 2016 figures refer to the period from 1 June 2016 (date of establishment of Italgas S.p.A.) to 31 December 2016 and include the consolidation of the subsidiaries from the date of acquisition of control (7 November 2016); therefore the 2017 financial figures are not comparable with those of the previous year.

The Italgas Group, consisting of Italgas S.p.A., the consolidating company, and its subsidiaries Italgas Reti S.p.A., ACAM Gas S.p.A., Enerco Distribuzione S.p.A. and S.G.S. S.r.l. (hereinafter referred to as "Italgas", the "Italgas Group" or the "Group"), is an integrated group at the forefront of the regulated natural gas sector and a major player in terms of its regulatory asset base (RAB<sup>21</sup>) in the sector.

Italgas S.p.A. is a joint-stock company incorporated under Italian law and listed on the Milan Stock Exchange, with registered offices in Milan at 11 via Carlo Bo.

CDP S.p.A. has "de facto" control over Italgas S.p.A. pursuant to the accounting principle IFRS 10 "Consolidated Financial Statements".

As at 31 December 2017, CDP S.p.A., via CDP Reti S.p.A.<sup>22</sup>, owns 26.05% of the share capital of Italgas S.p.A.

On 20 October 2016, Snam, CDP Reti and CDP Gas signed a shareholders' agreement covering all the shares that the respective parties would hold in Italgas as a result of the partial and proportional spin-off of Snam in favour of Italgas and as a result of the simultaneous admission to listing of Italgas shares, i.e. by 7 November 2016.

### 1. BASIS OF PREPARATION

The consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB) and adopted by the European Commission according to the procedure pursuant to Article 6 of (EC) Regulation No. 1606/2002 of the European Parliament and Council of 19 July 2002 and pursuant to Article 9 of Legislative Decree 38/2005. The IFRS also include the International Accounting Standards (IAS) as well as the interpretive documents still in force issued by the IFRS Interpretation Committee (IFRS IC), including those previously issued by the International Financial Reporting Interpretations Committee (IFRIC) and, before that, by the Standing Interpretations Committee (SIC). For simplicity,

<sup>21</sup> The term RAB (Regulatory Asset Base) refers to the value of net invested capital for regulatory purposes, calculated on the basis of the rules defined by the Italian Electricity, Gas and Water Authority (AEEGSI) for determining base revenues for the regulated businesses.

<sup>22</sup> CDP S.p.A. holds 59.10%.

all of the aforementioned standards and interpretations will hereafter be referred to as “IFRS” or “International Accounting Standards”.

The consolidated financial statements are prepared on a going-concern basis, using the historical cost method, taking into account value adjustments where appropriate, with the exception of the items which, according to IFRS, must be measured at fair value, as described in the measurement criteria.

The consolidated financial statements as at 31 December 2017, approved by the Board of Directors of Italgas S.p.A. at the meeting of 12 March 2018 were subjected to an audit by PricewaterhouseCoopers S.p.A., that - as the main auditor - is entirely responsible for the auditing of the Italgas Group consolidated financial statements.

The consolidated financial statements are presented in Euro. Given their size, amounts in the financial statements and respective notes are expressed in thousands of Euro, unless otherwise specified.

#### **ACCOUNTING PRINCIPLES AND INTERPRETATIONS APPLICABLE FROM 2017**

The accounting principles and interpretations, issued by the IASB/IFRIC, endorsed by the European Commission and which came into force from 2017 are listed below.

(EU) Regulation 2017/1990 of the European Commission of 6 November 2017, published in Official Journal L. 291 of 9 November 2017, adopted the document “Disclosure initiative - Amendments to IAS 7”, issued by the IASB on 29 January 2016. Amendments to the international accounting standard “IAS 7 - Statement of Cash Flows” were introduced with this document in order to improve reporting on the liabilities arising from the financing activities. In particular, users of financial statements are required

to be provided with information that allows them to assess what changes have taken place to the liabilities and assets originating from financing activities, both as a result of monetary movements and otherwise (by way of example, gains or losses following changes in exchange rates after the acquisition or loss of control of a subsidiary or business).

(EU) Regulation 2017/1989 of the European Commission of 6 November 2017, published in Official Journal L. 291 of 9 November 2017, approved the document “Recognition of Deferred Tax Assets for Unrealised Losses - Amendments to IAS 12”, issued by the IASB on 19 January 2016. With this document, the IASB clarified that unrealised losses on debt financial instruments recorded at fair value and whose tax base on the other hand refers to the cost, give rise to temporary tax differences, independently of the fact that the owner of the instrument expects to recover the actual value through ownership until expiry or alternatively through the sale of the actual instrument. The changes introduced also clarify that the estimate of future taxable income, whose valuation is necessary in order to record deferred tax assets: (i) includes income arising from the realisation of assets for amounts higher than the relative book value; (ii) excludes the reversal of deductible temporary tax differences; (iii) should take into consideration any limits imposed by tax regulations on the types of taxable income in response to which the tax deductions operate.

## **2. CONSOLIDATION PRINCIPLES**

The consolidated financial statements comprise the financial statements of Italgas S.p.A. and of the companies over which the Company has the right to exercise direct or indirect control, as defined by IFRS 10 - “Consolidated Financial Statements”.

Specifically, control exists where the controlling entity simultaneously:

- has the power to make decisions concerning the investee entity;
- is entitled to receive a share of or is exposed to the variable profits and losses of the investee entity;
- is able to exercise power over the investee entity in such a way as to affect the amount of its economic returns.

The proof of control must be verified on an ongoing basis by the Company, with a view to identifying all the facts or circumstances that may imply a change in one or more of the elements on which the existence of control over an investee entity depends.

Consolidated companies, joint ventures, associates and other significant equity investments are indicated separately in the Appendix “Subsidiaries, associates and equity investments of Italgas S.p.A. at 31 December 2017”, which is an integral part of these notes.

All financial statements of consolidated companies close at 31 December and are presented in Euro.

#### COMPANIES INCLUDED IN THE SCOPE OF CONSOLIDATION

Figures relating to subsidiaries are included in the consolidated financial statements from the date on which the Company assumes direct or indirect control over them until the date on which said control ceases to exist.

The assets, liabilities, income and expenses of the consolidated companies are consolidated line-by-line in the consolidated financial statements (full consolidation); the book value of the equity investments in each of the subsidiaries is derecognised against the corresponding portion of shareholders' equity of each of the investee entities, inclusive of any adjustments to the fair value of the assets and liabilities on the date of acquisition of control.

The portions of equity and profit or loss attributable to minority interests are recorded separately in the appropriate items of shareholders' equity, the income statement and the statement of comprehensive income.

Changes in the equity investments held directly or indirectly by the Company in subsidiaries that do not result in a change in the qualification of the investment as a subsidiary are recorded as equity transactions. The book value of the shareholders' equity pertaining to shareholders of the parent company and minority interests are adjusted to reflect the change in the equity investment. The difference between the book value of minority interests and the fair value of the consideration paid or received is recorded directly under equity pertaining to shareholders of the parent company.

Otherwise, the selling of interests entailing loss of control requires the posting to the income statement of: (i) any capital gains or losses calculated as the difference between the consideration received and the corresponding portion of consolidated shareholders' equity transferred; (ii) the effect of the revaluation of any residual equity investment maintained, to align it with the relative fair value; and (iii) any amounts posted to other components of comprehensive income relating to the former subsidiary which will be reversed to the income statement. The fair value of any equity investment maintained at the date of loss of

control represents the new book value of the equity investment, and therefore the reference value for the successive valuation of the equity investment according to the applicable valuation criteria.

#### **EQUITY INVESTMENTS IN ASSOCIATES AND JOINT VENTURES**

An associate is an investee company in relation to which the investor holds significant influence or the power to participate in determining financial and operating policies, but does not have control or joint control<sup>23</sup>. It is assumed that the investor has significant influence (unless there is proof to the contrary) if it holds, directly or indirectly through subsidiaries, at least 20% of the exercisable voting rights.

A joint venture is a joint arrangement in which the parties that hold joint control have rights to the net assets subject to the arrangement and, therefore, have an interest in the jointly controlled corporate vehicle.

Equity investments in associates and joint ventures are measured using the equity method, as described under "Investments valued using the equity method".

#### **BUSINESS COMBINATIONS**

Business combinations are recorded using the acquisition method in accordance with IFRS 3 - "Business Combinations". Based on this standard, the consideration transferred in a business combination is determined at the date on which control is assumed, and equals the fair value of the assets transferred, the liabilities incurred or assumed, and any equity instruments issued by the acquirer. Costs directly attributable to the transaction are posted to the income statement when they are incurred.

The shareholders' equity of these investee companies is determined by attributing to each asset and liability its fair value at the date of acquisition of control. If positive, any difference from the acquisition or transfer cost is posted to the asset item "Goodwill"; if negative, it is posted to the income statement.

Where total control is not acquired, the share of equity attributable to minority interests is determined based on the share of the current values attributed to assets and liabilities at the date of acquisition of control, net of any goodwill (the "partial goodwill method"). Alternatively, the full amount of the goodwill generated by the acquisition is recognised, therefore also taking into account the portion attributable to minority interests (the "full goodwill method"). In this case, minority interests are expressed at their total fair value, including the attributable share of goodwill. The choice of how to determine goodwill (partial goodwill method or full goodwill method) is made based on each individual business combination transaction.

If control is assumed in successive stages, the acquisition cost is determined by adding together the fair value of the equity investment previously held in the acquired company and the amount paid for the remaining portion. The difference between the fair value of the previously held equity investment (redetermined at the time of acquisition of control) and the

<sup>23</sup> Joint control is the contractual sharing of control pursuant to an agreement, which exists only where the unanimous consent of all the parties that share power is required for decisions relating to significant activities.

relative book value is posted to the income statement. Upon acquisition of control, any components previously recorded under other components of comprehensive income are posted to the income statement or to another item of shareholders' equity, if no provisions are made for reversal to the income statement.

When the values of the assets and liabilities of the acquired entity are determined provisionally in the financial year in which the business combination is concluded, the figures recorded are adjusted, with retroactive effect, no later than 12 months after the acquisition date, to take into account new information about facts and circumstances in existence at the acquisition date.

#### **Business combinations involving entities under joint control**

Business combinations involving companies that are definitively controlled by the same company or companies before and after the transaction, and where such control is not temporary, are classed as "business combinations of entities under common control". Such transactions do not fall within the scope of application of IFRS 3, and are not governed by any other IFRS. In the absence of a reference accounting standard, the selection of an accounting standard for such transactions, for which a significant influence on future cash flows cannot be established, is guided by the principle of prudence, which dictates that the principle of continuity be applied to the values of the net assets acquired. The assets are measured at the book values from the financial statements of the companies being acquired predating the transaction or, where available, at the values from the consolidated financial statements of the common ultimate parent. With regard to business transfers under common control, the transferee entity should record the business transferred at its historical book

value increasing its shareholders' equity by this amount; the transferring entity will record the investment in the transferee entity for the same amount as the increase in the shareholders' equity of the latter.

This accounting treatment is based on the Preliminary Guidelines on IFRS (OPI 1 Revised) - "Accounting treatment of business combinations of entities under common control in the separate and consolidated financial statements" issued by Assirevi in October 2016.

#### **Intragroup transactions that are eliminated in the consolidation process**

Unrealised gains from transactions between consolidated companies are derecognised, as are receivables, payables, income, expenses, guarantees, commitments and risks between consolidated companies. The portion pertaining to the Group of unrealised gains with companies valued using the equity method is derecognised. In both cases, intragroup losses are not derecognised because they effectively represent impairment of the asset transferred.

### **3. MEASUREMENT CRITERIA**

The most significant measurement criteria adopted when preparing the consolidated financial statements are described below.

#### **PROPERTY, PLANT AND EQUIPMENT**

Property, plant and equipment is recognised at cost and recorded at the purchase, transfer or production cost, including directly allocable ancillary costs needed to make the assets available for use. When a significant period of time is needed to make the asset ready for use, the purchase, transfer or production cost includes the financial expense which theoretically would have been saved during the period needed to make the asset ready for use if the investment had not been made.

Property, plant and equipment may not be revalued, even through the application of specific laws.

The costs of incremental improvements, upgrades and transformations to/value of property, plant and equipment are posted to assets when it is likely that they will increase the future economic benefits expected. The costs of replacing identifiable components of complex assets are allocated to balance sheet assets and depreciated over their useful life. The remaining book value of the component being replaced is allocated to the income statement. Ordinary maintenance and repair expenses are posted to the income statement in the period when they are incurred.

#### DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

Starting when the asset is available and ready for use, property, plant and equipment is systematically depreciated on a straight-line basis over its useful life, defined as the period of time in which it is expected that the company may use the asset.

The amount to be depreciated is the book value, reduced by the projected net realisable value at the end of the asset's useful life, if this is significant and can be reasonably determined.

The table below shows the annual depreciation rates used for the year in question, broken down into homogeneous categories, together with the relevant period of application:

Annual depreciation rate (%)	
<b>Land and building</b>	
- Industrial buildings	2%
- Civil buildings	3%
<b>Plant and equipment</b>	
- Other plant and equipment	4%
<b>Industrial and commercial equipment</b>	
- Office furniture and machinery	12% - 33.3%
- Transportation vehicles	20% - 25%

When an item recorded under property, plant and equipment consists of several significant components with different useful lives, a component approach is adopted, whereby each individual component depreciates separately.

Land is not depreciated, even if purchased in conjunction with a building; neither is property, plant and equipment held for sale (see the "Non-current assets held for sale and discontinued operations" section).



Depreciation rates are reviewed each year and are altered if the current estimated useful life of an asset differs from the previous estimate. Any changes to the depreciation plan arising from revision of the useful life of an asset, its residual value or ways of obtaining economic benefit from it are recognised prospectively.

Freely transferable assets are depreciated during the period of the concession or of the useful life of the asset, if lower.

#### **ASSETS UNDER FINANCE LEASES**

Assets under finance leases, or under agreements which may not take the specific form of a finance lease, but call for the essential transfer of the benefits and risks of ownership, are recorded at the lower of fair value less fees payable by the lessee and the present value of minimum lease payments, including any sum payable to exercise a call option, under property, plant and equipment as a contra-entry to the financial debt to the lessor. The assets are depreciated using the criteria and rates adopted for owned property, plant and equipment. When there is no reasonable certainty that the right of redemption can be exercised, depreciation takes place during the shorter of the term of the lease and the useful life of the asset.

Leases under which the lessee maintains nearly all of the risks and benefits associated with ownership of the assets are classified as operating leases. In this case, the lessee incurs only costs for the period in the amount of the lease expenses set out in the contract, and does not record fixed assets.

#### **INTANGIBLE ASSETS**

Intangible assets are those assets without identifiable physical form which are controlled by the company and capable of producing future economic benefits, as well as goodwill, when purchased for consideration. The ability to identify these assets rests in the ability to distinguish intangible assets purchased from goodwill. Normally this requirement is satisfied when: (i) the intangible assets are related to a legal or contractual right, or (ii) the asset is separable, i.e. it can be sold, transferred, leased or exchanged independently, or as an integral part of other assets. The company's control consists of the power to utilise future economic benefits deriving from the asset and the ability to limit access to it by others. Intangible assets are recorded at cost, which is determined using the criteria indicated for property, plant and equipment. They may not be revalued, even through the application of specific laws.

Technical development costs are allocated to the balance sheet assets when: (i) the cost attributable to the intangible asset can be reliably determined; (ii) there is the intent, availability of financial resources and technical capability to make the asset available for use or sale; and (iii) it can be shown that the asset is capable of producing future economic benefits.

Alternatively, costs for the acquisition of new knowledge or discoveries, investigations into products or alternative processes, new techniques or models, or the design and construction of prototypes, or incurred for other scientific research or technological developments, which do not meet the conditions for disclosure under balance sheet assets are considered current costs and charged to the income statement for the period in which they are incurred.

Intangible assets are eliminated at the time they are decommissioned, or when no future economic benefit is expected from their use; the related profit or loss is posted in the income statement.

**Service concession agreements**

Intangible assets include service concession agreements between the public and private sectors for the development, financing, management and maintenance of infrastructures under concession in which: (i) the grantor controls or regulates the services provided by the operator through the infrastructure and the related price to be applied; and (ii) the grantor controls any significant remaining interest in the infrastructure at the end of the concession by owning or holding benefits, or in some other way. The provisions relating to the service concession agreements are applicable for Italgas in its role as a public service natural gas distributor, i.e. they are applicable to the agreements under which the operator is committed to providing the public natural gas distribution service at the tariff established by the Autorità di Regolazione per Energia Reti e Ambiente (ARERA), formerly Autorità per l'Energia Elettrica il Gas e il Sistema Idrico (AEEGSI), holding the right to use the infrastructure, which is controlled by the grantor, for the purposes of providing the public service.

**Amortisation of intangible assets**

Intangible assets with a finite useful life are amortised systematically over their useful life, which is understood to be the period of time in which it is expected that the company may use the asset.

The amount to be depreciated is the book value, reduced by the projected net realisable value at the end of the asset's useful life, if this is significant and can be reasonably determined.

The table below shows the annual depreciation rates used for the year in question, broken down into homogeneous categories, together with the relevant period of application:

	Annual depreciation rate (%)
<b>Patent rights and intellectual property rights</b>	20% - 33.3%
<b>Concession expenses</b>	Depending on the duration of the agreement
<b>Land and buildings (concession agreements)</b>	
- Industrial buildings	2.5% - 5%
- Light constructions	9% - 10%
<b>Plant and equipment (concession agreements)</b>	
- Gas distribution network	2% - 5%
- Principal and secondary facilities	5% - 6%
- Gas derivation plants	2.5% - 5.4%
<b>Industrial and commercial equipment (concession agreements)</b>	
- Metering and control equipment	6.7% - 20%

Goodwill and other intangible assets with an indefinite useful life are not subject to amortisation.

## GRANTS

Capital grants given by public authorities are recognised when there is reasonable certainty that the conditions imposed by the granting government agencies for their allocation will be met, and they are recognised as a reduction to the purchase, transfer or production cost of the related assets. Similarly, capital grants received from private entities are recognised in accordance with the same regulatory provisions.

Operating grants are recognised in the income statement on an accruals basis, consistent with the relative costs incurred.

## IMPAIRMENT OF NON-FINANCIAL FIXED ASSETS

### Impairment of property, plant and equipment and intangible assets with a finite useful life

When events occur leading to the assumption of impairment of property, plant and equipment or intangible assets with a finite useful life, their recoverability is tested by comparing the book value with the related recoverable value, which is the fair value adjusted for disposal costs (see "Measurement at fair value") or the value in use, whichever is greater.

Value in use is determined by discounting projected cash flows resulting from the use of the asset and, if they are significant and can be reasonably determined, from its sale at the end of its useful life, net of any disposal costs. Cash flows are determined based on reasonable, documentable assumptions representing the best estimate of future economic conditions which will occur during the remaining useful life of the asset, with a greater emphasis on outside information. Discounting is done at a rate reflecting current market conditions for the time value of money and specific risks of the asset not reflected in the estimated cash flows. The valuation is done for individual assets or for the smallest identifiable group of assets which, through ongoing use, generates incoming cash flow that is largely independent of those of other assets or groups of assets ("cash-generating units" or CGUs).

The value of property, plant and equipment classed under regulated assets is determined by taking into consideration: (i) the amount quantified by the Authority based on the rules used to define the tariffs for provision of the services for which they are intended; and (ii) any value that the group expects to recover from their sale or at the end of the concession governing the service for which they are intended. As with the quantification of tariffs, the quantification of the recoverable value of property, plant and equipment classed under regulated assets is done on the basis of the regulatory provisions in force.

If the reasons for impairment losses no longer apply, the assets are revalued and the adjustment is posted to the income statement as a revaluation (recovery of value). The recovery of value is applied to the lower of the recoverable value and the book value before any impairment losses previously carried out, less any depreciation that would have been recorded if an

impairment loss had not been recorded for the asset.

#### **Impairment of goodwill, intangible assets with an indefinite useful life and intangible assets not yet available for use**

The recoverability of the book value of goodwill, intangible assets with an indefinite useful life and intangible assets not yet available for use is tested at least annually, and in any case when events occur leading to an assumption of impairment. Goodwill is tested at the level of the smallest aggregate, on the basis of which the Company's management directly or indirectly assesses the return on investment, including goodwill. When the book value of the CGU, including the goodwill attributed to it, exceeds the recoverable value, the difference is subject to impairment, which is attributed by priority to the goodwill up to its amount; any surplus in the impairment with respect to the goodwill is attributed pro rata to the book value of the assets which constitute the CGU. Goodwill impairment losses cannot be reversed.

#### **INVESTMENTS VALUED USING THE EQUITY METHOD**

Equity investments in joint ventures and associates are valued using the equity method.

In applying the equity method, investments are initially recognised at cost and subsequently adjusted to take into account: (i) the participant's share of the results of operations of the investee after the date of acquisition, and (ii) the share of the other components of comprehensive income of the investee. Dividends paid out by the investee are recognised net of the book value of the equity investment. For the purposes of applying the equity method, the adjustments provided for the consolidation process are taken into account (see also the "Consolidation principles" section).

In the case of assumption of an association (joint control) in successive phases, the cost

of the equity investment is measured as the sum of the fair value of the interests previously held and the fair value of the consideration transferred on the date on which the investment is classed as associated (or under joint control). The effect of revaluing the book value of the investments previously held at assumption of association is posted to the income statement, including any components recognised under other components of comprehensive income. When the transfer of equity investments entails loss of joint control or significant influence over the investee company, the following are recognised in the income statement: (i) any capital gains or losses calculated as the difference between the consideration received and the corresponding portion of the booked amount transferred; (ii) the effect of the revaluation of any residual equity investment maintained, to align it with the relative fair value; and (iii) any amounts posted to other components of comprehensive income relating to the investee company that will be taken to the income statement. The value of any equity investment maintained, aligned with the relative fair value at the date of loss of joint control or significant influence, represents the new book value, and therefore the reference value for the successive valuation according to the applicable valuation criteria.

If there is objective evidence of impairment, the recoverability of the amount recognised is tested by comparing the book value with the related recoverable value determined using the criteria indicated in the section "Impairment of non-financial fixed assets".

When the reasons for the impairment losses entered no longer apply, equity investments are revalued up to the amount of the impairment losses entered with the effect posted to the income statement under "Income (expense) from equity investments".

The parent company's share of any losses of the investee company, greater than the investment's book value, is recognised in a special provision to the extent that the parent company is committed to fulfilling its legal or implied obligations to the subsidiary/associate, or, in any event, to covering its losses.

## INVENTORIES

Inventories, including compulsory inventories, are recorded at the lower of purchase or production cost and net realisation value, which is the amount that the company expects to receive from their sale in the normal course of business.

The cost of natural gas inventories is determined using the weighted average cost method.

## FINANCIAL INSTRUMENTS

The financial instruments held by Italgas are included in the following balance sheet items:

### Cash and cash equivalents

Cash and cash equivalents include cash amounts, on demand deposits, and other short-term financial investments with a term of less than three months, which are readily convertible into cash and for which the risk of a change in value is negligible.

They are recorded at their nominal value, which corresponds to the fair value.

### Trade and other receivables and other assets

Trade and other receivables and other assets are valued when the comprehensive fair value

of the costs of the transaction (e.g. commission, consultancy fees, etc.) are first recognised. The initial book value is then adjusted to account for repayments of principal, any impairment losses and the amortisation of the difference between the repayment amount and the initial book value.

Amortisation is carried out using the effective internal interest rate, which represents the rate that would make the present value of projected cash flows and the initial book value equal at the time of the initial recording (the “amortised cost method”).

Where there is actual evidence of impairment, the impairment loss is calculated by comparing the book value with the current value of anticipated cash flows discounted at the effective interest rate defined at the time of the initial recognition, or at the time of its updating to reflect the contractually defined repricing. There is objective evidence of impairment when, among other things, there are significant breaches of contract, major financial difficulties or the risk of the counterparty’s insolvency.

Receivables are shown net of provisions for impairment losses; this provision, which is previously created, may be used if there is an assessed reduction in the asset’s value or due to a surplus. If the reasons for a previous write-down cease to be valid, the value of the asset is restored up to the value of applying the amortised cost if the write-down had not been made.

The economic effects of measuring at amortised cost are recorded in the “Financial income (expense)” item.

Financial assets are derecognised in the balance sheet when the contractual rights connected to obtaining the cash flows associated with the financial instrument are realised, expire or are transferred to third parties by transferring all risks and benefits of ownership of the financial asset.

Trade and other receivable are classified in the balance sheet under current assets, except for those having a contractual deadline longer than twelve months from the balance sheet date, which are classified as non-current assets.

### **Financial liabilities**

Financial liabilities, including financial debt, trade payables, other payables and other liabilities, are initially recorded at fair value less any transaction-related costs; they are subsequently recognised at amortised cost using the effective interest rate for discounting, as demonstrated in “Trade and other receivables and other assets” above.

Financial liabilities are derecognised upon extinguishment or upon fulfilment, cancellation or maturity of the contractual obligation.



### NON-CURRENT ASSETS HELD FOR SALE AND DISCONTINUED OPERATIONS

Non-current assets and current and non-current assets of disposal groups are classified as held for sale if the relative book value will be recovered mainly by their sale rather than through their continued use. This condition is regarded as fulfilled when the sale is highly probable and the asset or discontinued operations are available for immediate sale in their current condition.

Non-current assets held for sale, current and non-current assets related to disposal groups and directly associated liabilities are recognised in the Statement of Financial Position separately from the Company's other assets and liabilities.

Non-current assets held for sale and non-current assets in disposal groups are not amortised or depreciated, and are measured at the lower between the book value and the related fair value, less any sales costs.

The fair value is the amount that may be received for the sale of an asset or that may be paid for the transfer of a liability in a regular transaction between market operators as at the valuation date (i.e. exit price).

The fair value of an asset or liability is determined by adopting the valuations that market operators would use to determine the price of the asset or liability. A fair value measurement also assumes that the asset or liability would be traded on the main market or, failing that, on the most advantageous market to which the Company has access.

The fair value of a non-financial asset is determined by considering the capacity of market operators to generate economic benefits by putting the asset to its maximum and best use or by selling it to another market participant capable of using it in such a way as to maximise its value. The maximum and best use of an asset is determined from the perspective of market operators, also hypothesising that the company intends to put it to a different use; the current use by the company of a non-financial asset is assumed to be the maximum and best use of this asset, unless the market or other factors suggest that a different use by market operators would maximise its value.

The fair-value measurement of a financial or non-financial liability, or of an equity instrument, takes into account the quoted price for the transfer of an identical or similar liability or equity instrument; if this quoted price is not available, the valuation of a corresponding asset held by a market operator as at the valuation date is taken into account. The determination of the fair value of a liability takes into account the risk that the company may not be able to honour its obligations ("Debit Valuation Adjustment" (DVA)).

When determining fair value, a hierarchy is set out consisting of criteria based on the origin, type and quality of the information used in the calculation. This classification aims to establish a hierarchy in terms of the reliability of the fair value, giving precedence to the use of parameters that can be observed on the market and that reflect the assumptions that market participants would use when valuing the asset/liability. The fair value hierarchy includes the following levels:

- level 1: inputs represented by (unmodified) quoted prices on active markets for assets or liabilities identical to those that can be accessed as at the valuation date;

- level 2: inputs, other than the quoted prices included in Level 1, that can be directly or indirectly observed for the assets or liabilities to be valued;
- level 3: inputs that cannot be observed for the asset or liability.

In the absence of available market quotations, the fair value is determined by using valuation techniques suitable for each individual case that maximise the use of significant observable inputs, whilst minimising the use of non-observable inputs.

The classification as “held for sale” of equity investments valued using the equity method implies suspended application of this measurement criterion. Therefore, in this case, the book value is equal to the value resulting from the application of the equity method at the date of reclassification.

Any negative difference between the book value and the fair value less selling costs is posted to the income statement as an impairment loss; any subsequent recoveries in value are recognised up to the amount of the previously recognised impairment losses, including those recognised prior to the asset being classified as held for sale.

Non-current assets and current and non-current assets (and any related liabilities) of disposal groups, classified as held for sale, constitute discontinued operations if, alternatively: (i) they represent a significant independent business unit or a significant geographical area of business; (ii) they are part of a programme to dispose of a significant independent business unit or a significant geographical area of business; or (iii) they pertain to a subsidiary acquired exclusively for the purpose of resale. The results of discontinued operations, as well as any capital gains/losses realised on the disposal, are disclosed separately in the income statement as a separate item, net of related tax effects, including for the periods under comparison.

In the case of a programme for the sale of a subsidiary that results in loss of control, all assets and liabilities of that subsidiary are classified as held for sale, regardless of whether an investment is maintained following the sale.

#### PROVISIONS FOR RISKS AND CHARGES

Provisions for risks and charges concern costs and charges of a certain nature which are certain or likely to be incurred, but for which the amount or date of occurrence cannot be determined at the end of the year.

Provisions are recognised when: (i) the existence of a current legal or implied obligation arising from a past event is probable; (ii) it is probable that the fulfilment of the obligation will involve a cost; and (iii) the amount of the obligation can be reliably determined. Provisions are recorded at a value representing the best estimate of the amount that the company would reasonably pay to fulfil the obligation or to transfer it to third parties at the end of the reporting period. Provisions related to contracts with valuable consideration are recorded at the lower of the cost necessary to fulfil the obligation, less the expected economic benefits deriving from the contract, and the cost to terminate the contract.

When the financial impact of time is significant, and the payment dates of the obligations can be reliably estimated, the provision is calculated by discounting the anticipated cash flows in consideration of the risks associated with the obligation at the Company's average

debt rate; the increase in the provision due to the passing of time is posted to the income statement under “Financial income (expense)”.

When the liability is related to items of property, plant and equipment (e.g. site dismantlement and restoration), the provision is recognised as a counter-entry to the related asset, and posting to the income statement is accomplished through amortisation. The costs that the Company expects to incur to initiate restructuring programmes are recorded in the period in which the programme is formally defined, and the parties concerned have a valid expectation that the restructuring will take place.

Provisions are periodically updated to reflect changes in cost estimates, selling periods and the discount rate; revisions in provision estimates are allocated to the same item of the income statement where the provision was previously reported or, when the liability is related to property, plant and equipment (e.g. site dismantling and restoration), as a contra-entry to the related asset, up to the book value; any surplus is posted to the income statement.

The notes to the financial statements describe contingent liabilities represented by: (i) possible (but not probable) obligations resulting from past events, the existence of which will be confirmed only if one or more future uncertain events occur which are partially or fully outside the Company's control; and (ii) current obligations resulting from past events, the amount of which cannot be reliably estimated, or the fulfilment of which is not likely to involve costs.

#### PROVISIONS FOR EMPLOYEE BENEFITS

##### Post-employment benefits

Post-employment benefits are defined according to programmes, including non-

formalised programmes, which, depending on their characteristics, are classed as “defined-benefit” or “defined-contribution” plans.

##### - *Defined-benefit plans*

The liability associated with defined-benefit plans is determined by estimating the present value of the future benefits accrued by the employees during the current year and in previous years, and by calculating the fair value of any assets servicing the plan. The present value of the obligations is determined based on actuarial assumptions and is recognised on an accruals basis consistent with the employment period necessary to obtain the benefits.

Actuarial gains and losses relating to defined-benefit plans arising from changes in actuarial assumptions or experience adjustments are recognised in other comprehensive income in the period in which they occur, and are not subsequently recognised in the income statement. When a plan is changed, reduced or extinguished, the relative effects are recognised in the income statement.

Net financial expense represents the change that the net liability undergoes during the year due to the passing of time. Net interest is determined by applying the discount rate to the liabilities, net of any assets servicing the plan. The net financial expense of defined-benefit plans is recognised in “Financial Income (Expense)”.

##### - *Defined-contribution plans*

In defined-contribution plans, the Company's obligation is calculated, limited to the payment of state contributions or to equity or a legally separate entity (fund), based on contributions due.

The costs associated with defined-benefit contributions are recognised in the income statement as and when they are incurred.

#### OTHER LONG-TERM PLANS

Obligations relating to other long-term benefits are calculated using actuarial assumptions; the effects arising from the amendments to the actuarial assumptions or the characteristics of the benefits are recognised entirely in the income statement.

#### DISTRIBUTION OF DIVIDENDS

The distribution of dividends to the Company's Shareholders entails the recording of a payable in the financial statements for the period in which distribution was approved by the Company's Shareholders or, in the case of interim dividends, by the Board of Directors.

#### REVENUE

Revenue from sales and the provision of services is recognised upon the effective transfer of the risks and benefits typically relating to ownership or on the fulfilment of the service when it is likely that the financial benefits deriving from the transaction will be realised by the vendor or the provider of the service.

Revenue is recognised at the fair value of the payment received or to be received.

As regards the activities carried out by the Italgas Group, revenue is recognised when the service is provided. The largest share of core revenue relates to regulated revenue, which is governed by the regulatory framework established by the Autorità di Regolazione per Energia Reti e Ambiente (ARERA). Therefore, the economic terms and conditions of services provided are defined in accordance with regulations rather than negotiations. With regard to the natural gas distribution segment, the difference between the revenue recognised by the regulator (so-called revenue cap) and the effectively accrued revenue is recognised in the Statement of Financial Position item "Trade and other receivables", if positive, and in the item "Trade and other payables", if negative, inasmuch as it will be subject to cash settlement with the Cassa per i Servizi Energetici e Ambientali (CSEA)<sup>24</sup>.

Allocations of revenue relating to services partially rendered are recognised by the fee accrued, as long as it is possible to reliably determine the stage of completion and there are no significant uncertainties over the amount and the existence of the revenue and the relative costs; otherwise they are recognised within the limits of the actual recoverable costs.

<sup>24</sup> Law No. 208 of 28 December 2015 (2016 Stability Law) makes provision, in Article 1, paragraph 670, for the transformation of the Cassa Conguaglio per il Settore Elettrico (CCSE) into a state-controlled Cassa per i Servizi Energetici e Ambientali (CSEA) as of 1 January 2016. The transformation of the CCSE into a state-controlled company and the change of name do not, in any way, either cause discontinuity in the functional relations of the CSEA (formerly the CCSE) with regulated parties or with suppliers.

Items of property, plant and equipment not used in concession services, transferred from customers (or realised with the cash transferred from customers) and depending on their connection to a network for the provision of supply, are recognised at fair value as a contra-entry to revenue in the income statement. When the agreement stipulates the provision of multiple services (e.g. connection and supply of goods), the service for which the asset was transferred from the customer is checked and, accordingly, the disclosure of the revenue is recognised on connection or for the shorter of the term of the supply and the useful life of the asset.

Revenue is recorded net of returns, discounts, allowances and bonuses, as well as directly related taxes.

Revenue is reported net of items involving tariff components, in addition to the tariff, applied to cover gas system expenses of a general nature. Amounts received from Italgas are paid in full to the Energy and Environmental Services Fund. Gross and net presentation of revenue is described in more detail in the Notes to the consolidated financial statements (see "Revenue" note).

Since they do not represent sales transactions, exchanges between goods or services of a similar nature and value are not recognised in revenue and costs.

#### **DIVIDENDS RECEIVED**

Dividends are recognised at the date of the resolution passed by the Shareholders' Meeting, unless it is not reasonably certain that the shares will be sold before the ex-dividend date.

#### **COSTS**

Costs are recognised in the period when they relate to goods and services sold or consumed during the same period or when it is not possible to identify their future use.

Fees relating to operating leases are charged to the income statement for the duration of the contract.

Costs sustained for share capital increases are recorded as a reduction of shareholders' equity, net of taxes.

#### **ENERGY EFFICIENCY CERTIFICATES**

The Energy Efficiency Certificates purchased during the year are entered in the income statement at the cost borne. The relevant contribution that CSEA will pay at the time the certificates are cancelled is booked as a reduction of the cost borne and is calculated based on the repayment price scheduled at year-end. A special risk provision is allocated to cover the future expected charges to fulfil the year's objective calculated as the difference between the cost to be borne and its cancellation contribution.

#### **INCOME TAXES**

Current income taxes are calculated by estimating the taxable income. Receivables and payables for current income taxes are recognised based on the amount which is expected to be paid/recovered to/from the tax authorities under the prevailing tax regulations and rates or those essentially approved at the reporting date.

Regarding corporation tax (IRES), Italgas has exercised the option to join the national tax consolidation scheme, to which all the consolidated companies have officially signed up. The projected payable is recognised under “Current income tax liabilities”.

The regulations governing Italgas Group companies’ participation in the national tax consolidation scheme stipulates that:

- subsidiaries with positive taxable income pay the amount due to Italgas. The taxable income of the subsidiary, used to determine the tax, is adjusted to account for the recovery of negative components that would have been non-deductible without the consolidation scheme (e.g. interest expense), the so-called ACE (help for economic growth) effect and any negative taxable income relating to the subsidiary’s equity investments in consolidated companies;
- subsidiaries with negative taxable income, if and insofar as they have prospective profitability which, without the national tax consolidation scheme, would have enabled them to recognise deferred tax assets related to the negative taxable income on the separate financial statements, receive from their shareholders – in the event that these are companies with a positive taxable income or a negative taxable income with prospective profitability – or from Italgas in other cases, compensation amounting to the lower of the tax saving realised by the Group and the aforementioned deferred tax assets.

Regional production tax (IRAP) is recognised under the item “Current income tax liabilities”/“Current income tax assets”.

Deferred and prepaid income taxes are calculated on the timing differences between the values of the assets and liabilities entered in the balance sheet and

the corresponding values recognised for tax purposes, based on the prevailing tax regulations and rates or those essentially approved for future years. Prepaid tax assets are recognised when their recovery is considered probable; specifically, the recoverability of prepaid tax assets is considered probable when taxable income is expected to be available in the period in which the temporary difference is cancelled, allowing the activation of the tax deduction. Similarly, unused tax receivables and prepaid taxes on tax losses are recognised up to the limit of recoverability.

Prepaid tax assets and deferred tax liabilities are classified under non-current assets and liabilities and are offset at individual company level if they refer to taxes which can be offset. The balance of the offsetting, if it results in an asset, is recognised under the item “Prepaid tax assets”; if it results in a liability, it is recognised under the item “Deferred tax liabilities”. When the results of transactions are recognised directly in equity, prepaid and deferred current taxes are also posted to equity.

Income tax assets with elements of uncertainty are recognised when they are regarded as likely to be obtained.

#### OPERATING SECTORS

The Group mainly works in Gas Distribution and Metering, and residually works in the distribution and sale of water; owing to the irrelevance of this residual line of business, a single operating sector was identified pursuant to IFRS, which is Gas Distribution and Metering.



## 4. FINANCIAL STATEMENTS

The formats adopted for the preparation of the financial statements are consistent with the provisions of IAS 1 - "Presentation of financial statements" (hereinafter "IAS 1"). In particular:

- the Statement of Financial Position items are broken down into assets and liabilities, and then further into current or non-current items<sup>25</sup>;
- the Income Statement classifies costs by type, since this is deemed to be the best way of representing the Group's operations and is in line with international best practice;
- the Statement of Comprehensive Income shows the profit or loss in addition to the income and expense recognised directly in shareholders' equity as expressly provided for by the IFRS;
- the Statement of Changes in Shareholders' Equity reports the total income (expense) for the financial year, shareholder transactions and the other changes in Shareholders' equity;
- the Statement of Cash Flows is prepared using the "indirect" method, adjusting the profit for the year of non-monetary components.

It is believed that these statements adequately represent the Group's situation with regard to its Statement of Financial Position, Income Statement and Statement of Cash Flows.

Moreover, pursuant to Consob Resolution No. 15519 of 28 July 2006, any income and expense from non-recurring operations is shown separately in the income statement.

With regard to the same Consob Resolution, the balances of receivables/payables and transactions with related parties, described in more detail in the note - "Related-party transactions", are shown separately in the financial statements.

## 5. USE OF ESTIMATES

The application of generally accepted accounting principles for the preparation of financial statements involves management making accounting estimates based on complex and/or subjective judgements, estimates based on past experience and assumptions regarded as reasonable and realistic on the basis of the information known at the time of the estimate. The use of these accounting estimates has an influence on the book value of the assets and liabilities and on the information about potential assets and liabilities at the reporting date, as well as the amount of revenue and costs in the reference period. The actual results may differ from the estimated results owing to the uncertainty that characterises the assumptions and the conditions on which the estimates are based.

<sup>25</sup> The assets and liabilities are classified as current if: (i) their realisation is expected in the normal corporate operating cycle or in the twelve months after the financial year-end; (ii) they are composed of cash or cash equivalents which do not have restrictions on their use over the twelve months following the year-end date; or (iii) they are mainly held for trading purposes.

Details are given below about the critical accounting estimates involved in the process of preparing the financial statements and interim reports, since they involve a high degree of recourse to subjective judgements, assumptions and estimates regarding matters that are by nature uncertain. Any change in the conditions forming the basis of the judgements, assumptions and estimates used could have a significant impact on subsequent results.

<b>Impairment of assets</b>	<p>Assets are impaired when events or changes in circumstances give cause to believe that the book value is not recoverable. The events which may give rise to an impairment of assets include changes in business plans, changes in market prices or reduced use of plants. The decision on whether to apply an impairment and the quantification of any such impairment depend on the Company's management assessment of complex and highly uncertain factors, such as future price trends, the impact of inflation and technological improvements on production costs, production profiles and conditions of supply and demand.</p> <p>The impairment is determined by comparing the book value with the related recoverable value, represented by the greater of the fair value, net of disposal costs, and the value in use, determined by discounting the expected cash flows deriving from the use of the asset. The expected cash flows are quantified in the light of the information available at the time of the estimate, on the basis of subjective judgements regarding future trends in variables – such as prices, costs, the rate of growth of demand and production profiles – and are updated using a rate that takes account of the risk inherent to the asset concerned. More information on the impairment test carried out by the Company's management on property, plant and equipment and on intangible assets can be found in the "Impairment of non-financial fixed assets" section.</p>
<b>Business combinations</b>	<p>The reporting of business combination transactions involves the allocation to the assets and liabilities of the acquired company of the difference between the acquisition cost and the net book value. For the majority of assets and liabilities, the allocation of the difference is carried out by recognising the assets and liabilities at their fair value. The unallocated portion, if positive, is recognised as goodwill; if negative, it is allocated to the income statement. In the allocation process, the Italgas Group draws on the available information and, for the most significant business combinations, on external valuations.</p>
<b>Environmental liabilities</b>	<p>The Italgas Group is subject, in relation to its activities, to numerous laws and regulations on environmental protection at European, national, regional and local level, including the laws which implement international conventions and protocols relating to the activities carried out. With reference to this legislation, when it is probable that the existence and amount of a large liability can be reliably estimated, provisions are made for the associated costs.</p> <p>The group currently does not believe there will be particularly negative impacts on the financial statements due to failure to comply with environmental regulations, also taking into account the measures already undertaken. However, it cannot be definitely ruled out that further costs or responsibilities may be incurred, including quite significant ones because, as far as we are currently aware, it is impossible to predict the effects of future developments also taking into account, among other things, the following aspects: (i) the possible emergence of contamination; (ii) the results of current and future refurbishment and the other possible effects arising from the application of the laws in force; (iii) the possible effects of new laws and regulations for environmental protection; (iv) the effects of any technological innovations for environmental cleansing; and (v) the possibility of disputes and the difficulty of determining the possible consequences, including in relation to the liability of other parties and to possible compensation payments.</p>

### Provisions for employee benefits

Defined-benefit plans are valued on the basis of uncertain events and actuarial assumptions which include, inter alia, the discount rates, the expected returns on the assets servicing the plans (where they exist), the level of future remuneration, mortality rates, the retirement age and future trends in the healthcare expenses covered. The main assumptions used to quantify defined-benefit plans are determined as follows: (i) the discount and inflation rates representing the base rates at which the obligation to employees might actually be fulfilled are based on the rates which mature on high-quality bonds and on inflation expectations; (ii) the level of future remuneration is determined on the basis of elements such as inflation expectations, productivity, career advancement and seniority; (iii) the future cost of healthcare services is determined on the basis of elements such as present and past trends in healthcare costs, including assumptions regarding the inflationary growth of costs, and changes in the health of the participating employees; and (iv) the demographic assumptions reflect the best estimates of trends in variables such as mortality, turnover, invalidity and others in relation to the population of the participating employees.

Differences in the value of net liabilities (assets) in employee benefit plans, arising due to changes in the actuarial assumptions used and the difference between the actuarial assumptions previously adopted and actual events, occur routinely and are called actuarial gains and losses. Actuarial gains and losses relating to defined-benefit plans are recognised in the statement of comprehensive income. Actuarial assumptions are also used to determine obligations relating to other long-term benefits; to this end, the effects arising from changes to the actuarial assumptions or the characteristics of the benefit are fully recognised in the income statement.

### Provisions for risks and charges

In addition to recognising environmental liabilities and obligations to remove property, plant and equipment and restore sites, and liabilities relating to employee benefits, Italgas makes provisions relating mainly to legal and tax disputes and to the expenses related to reaching the Energy Efficiency Certificates targets indicated by the Authority (TEE). The estimate of the provisions for these purposes is the result of a complex process involving subjective judgements on the part of the Company's management.

## 6. RECENTLY ISSUED ACCOUNTING STANDARDS

### ACCOUNTING STANDARDS AND INTERPRETATIONS ISSUED BY THE IASB/IFRIC AND APPROVED BY THE EUROPEAN COMMISSION, BUT NOT YET IN FORCE

With respect to the accounting standards issued by the IASB and endorsed by the European Commission, IFRS 9 "Financial instruments" and IFRS 15 "Revenue from Contracts with Customers", which will enter into force as of 1 January 2018, in addition to what is already described in the 2016 Annual Report, to which reference is made, the Italgas Group is carrying out further analyses of the impacts of the application of the new accounting standards on the consolidated financial statements and on the separate financial statements of the subsidiaries.

The provisions set forth in IFRS 9 "Financial instruments" were adopted with regulation no. 2016/2067, issued by the European Commission on 22 November 2016. The provisions

in IFRS 9, replacing those contained in IAS 39, are effective from the financial years after 1 January 2018. In relation to IFRS 9, an assessment is currently being completed on the impacts on recurring transactions of the main areas concerned by the new elements of the standard, described below: (i) new impairment model on “forward looking” receivables: in evaluating the risk of future losses to which these assets could be subject, it is first necessary to note that Italgas works in a regulated sector in which it generates more than 98% of its revenues and that over 93% of its receivables refer to highly reliable customers such as Eni (28%) and Enel; in general, the rules for user access to the gas distribution service are established by ARERA and are set forth in the Network Codes, i.e., documents which establish, for each type of service, the rules governing the rights and obligations of the parties involved in the provision of those services, and dictate contractual clauses reducing the risk of breach by customers; lastly, based on the so-called Network Code (or the set of conditions governing relationships between sales companies and distributors), to access the gas distribution service the gas sales companies are required to issue dedicated guarantees in the form of bank sureties or insurance or security deposits; considering that the majority of the receivables relate to regulated activities for which forms of guarantee are provided in favour of Italgas and/or the intervention of the Energy and Environmental Services Fund is provided in the cases set forth in the regulatory codes, from the analyses conducted it is not believed that the change in the model will be capable of generating significant effects; (ii) hedge accounting: the Italgas group held no hedging instruments at 31 December 2017; (iii) classification of financial instruments: as Italgas holds primarily financial assets and liabilities measured with the amortised cost method, the classification of financial instruments pursuant to IFRS 9 on the basis of the business model and the

characteristics of the instrument will not produce significant modifications in the measurement of existing instruments.

As at 1 January 2018, the impact is basically minimum (less than €1 million) and regards the impairment of loans.

On 12 September 2016 the IASB issued the document *“Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts-Amendments to IFRS 4”*, aimed at solving the problems resulting from the application of IFRS 9 before the implementation of the standard which will replace IFRS 4, which is being developed by the IASB. The changes introduced involve the adoption of two alternatives: (i) the possibility of reclassifying costs and revenues from certain financial assets in the comprehensive income statement; (ii) the possibility of not temporarily applying IFRS 9 for entities where the main activity is to issue insurance contracts coming under the scope of the application of IFRS 4. As at 1 January 2018, the impact is basically minimum (less than €1 million) and regards the provision for impairment losses.

On 28 May 2014, the IASB published the IFRS 15 - Revenue from contracts with customers standard, which introduced a single model for recognising all revenue coming from contracts with customers and replaces the previous revenue standards/interpretations (IAS 18, IAS 11, IFRIC 13, IFRIC 15, IFRIC 18, SIC 31).

In 2016 Italgas launched an analysis of the impacts of IFRS 15, continuing with these activities in 2017. In this regard, it should be noted that:

- Italgas operates in the regulated gas distribution sector.
- The document underlying relationships between gas distribution network users (gas sales companies) and the distributors is the Network Code.

- The Network Code describes the services that users are able to request from the distribution companies.
- The overall regulatory framework governs all contractual aspects connected to the provision of services (timing, execution and invoicing methods, penalties, bonuses, etc.)
- In summary, almost all Group revenues (around 97%) are subject to regulation and include those connected to the gas distribution service, ancillary services included in the network code and refunds paid by the regulator following the attainment of technical and commercial standards, while the remainder substantially regards real estate income and third-party services.

Contracts covering the unregulated activities the Group carries on, which mainly concern contracts for the supply to subsidiaries or associates of services that Italgas manages centrally, were also analysed.

On the basis of this preliminary analysis, it is deemed that the essential points laid out by the standard (identification of the contract, identification of the individual performance obligations, determination of the price, allocation of the transaction price to each performance obligation, recognition of revenue allocated based on control by customers) will not generate significant impacts compared with the current presentation, except for a reclassification regarding the contributions for connection from fixed assets to accruals and deferrals (€436.8 million as at 1 January 2018).

On 12 April 2016 the IASB issued “Clarifications to IFRS 15 Revenue from Contracts with Customers”. The changes to the principle introduce clarifications as well as new examples in order to facilitate the application of the principle and specifically with regard to: (i) the identification of individual contract obligations; (ii) the qualification of the entity as principal or agent; (iii) when to measure revenue from the concession to a customer of the use of or access to intellectual property. The changes also introduce additional practical devices which can make the transition to the new principle less onerous and specifically with regard to: (i) contracts concluded prior to the start of the first comparison period presented, also under the scope of the full retrospective approach; (ii) the aggregate representation of the contractual changes that took place before the start of the comparison period (full retrospective approach) or the first application period (modified retrospective approach).

On 13 January 2016, the IASB issued the “IFRS 16 Leases” standard. It is based on fundamental criteria, i.e. the right of use of an asset necessary for distinguishing between the lease agreements and the service contracts on the basis of probative elements such as: identification of the asset, the right to replace it, the right to basically get all the financial benefits arising from use of the asset and the right to govern use of the asset underlying the lease agreement. Conversely, payment of an amount along the contractual term of use of the asset entails that the entity is implicitly obtaining a loan. In short, IFRS 16 eliminates the distinction between finance leases and operating leases, and introduces, for lessees, a single accounting model for recognising leases. By applying this model the entity recognises: (i) assets and liabilities for all leases longer than 12 months; (ii) separately in the income statement, the amortisation of the asset recognised and the interest on the payable entered. The Group is investigating application of the new standard with particular reference to assets such as property, computer equipment and motor vehicles/lorries. As at 1 January

2018, the impact was determined in greater Fixed assets (Right of use) and Lease debts amounting to €31 million.

#### ACCOUNTING STANDARDS, AMENDMENTS AND INTERPRETATIONS NOT YET APPROVED BY THE EUROPEAN UNION AS AT THE DATE OF REFERENCE OF THE FINANCIAL STATEMENTS AS AT 31 DECEMBER 2017

Several accounting standards, interpretations and amendments have been issued by the IASB but not yet approved by the European Union as at the date this document is drawn up, including those described below.

The IFRS 17 “Insurance Contracts” standard, issued by the IASB on 18 May 2017, regards all insurance contracts and defines their “recognition, measurement, presentation and disclosure” principles. It replaces the previous IFRS 4. With the new standard an accounting model is introduced, the “Building Block Approach” (BBA), based on discounting the expected cash flows, on clarifying a risk adjustment and a contractual service margin (CSM) representing the expected profit of an insurance contract. The contractual margin is posted to the income statement along the period of insurance coverage. Two approaches alternative to the BBA were also introduced: the Variable Fee Approach (VFA) and the Premium Allocation Approach (PAA). The standard also sets out a new method for booking insurance revenues, insurance service expenses and insurance finance income or expenses to the income statement. The measures contained in IFRS 17 will take effect from financial years starting on or after 1 January 2021, notwithstanding any subsequent deferrals established upon adoption by the European Commission.

“IFRIC 22 Foreign Currency Transaction and Advance Consideration”, issued by the IASB on 8 December 2016, establishes that when there are foreign currency transactions whereby payment is made or received in advance, the exchange rate to apply for

the initial recording of the asset, costs or revenue generated from the transaction for which advance payment/collection took place, corresponds to the exchange rate in force on the advance payment date. These measures will take effect from financial years starting on or after 1 January 2018, notwithstanding any subsequent deferrals established upon approval by the European Commission.

IFRIC 23 “Uncertainty over Income Tax Treatments”, published by the IASB on 7 June 2017, provides information on how to calculate current and deferred taxes if there are uncertainties on tax treatments concerning income taxes that the entity has adopted. In calculating the income taxes to record in the financial statements, the entity must consider the probability that the tax authority accepts the tax treatment it has adopted. If this acceptance is deemed improbable, the entity must reflect the uncertainties in the calculation of the current and deferred taxes by using one of the following methods: the most likely amount and the expected value; otherwise, the income taxes recorded in the financial statements will be consistent with the tax treatment adopted in the income tax return. The entity must review the estimates of the uncertainties if new information becomes available or if there are changes in the circumstances. These measures will take effect from financial years starting on or after 1 January 2019, notwithstanding any subsequent deferrals established upon approval by the European Commission.

With the document “Sale or Contribution of Assets between an Investor and its Associate or Joint Venture - Amendments to IFRS 10 and IAS 28” of 11 September 2014, the IASB introduced amendments whose objective is to define the accounting treatment concerning gains or losses coming from transactions with joint ventures or associates valued using the



equity method more in detail, particularly with reference to: (i) the loss of control of a subsidiary (regulated by IFRS 10), (ii) downstream transactions (regulated by IAS 28). The accounting treatment used in the investor's financial statements depends on whether or not the object of the transaction is a business as defined by IFRS 3. In fact, the amendments specify that: (i) the gains (or losses) arising from remeasurement at fair value of the investment kept in a previously controlled company that is not a business, that qualifies as a joint venture or associate (valued with the equity method), are recognised in the financial statements of the investor only for the amount held by minority investors in the joint venture or associate; (ii) the gains (or losses) arising from downstream transactions regarding the assets not forming business between an entity and its joint ventures or associates must be recognised in full in the entity's financial statements (IAS 28).

With "Classification and Measurement of Share-based Payment Transactions - Amendments to IFRS 2" of 20 June 2016, the IASB: (i) clarifies the effects of the vesting and non-vesting conditions on the measurement of transactions with cash-settled share-based payment; (ii) specifies that the changes in transactions with cash-settled to equity-settled share-based payment eliminate the original liability, recognition of the payment based on share-based payment with instruments representing capital at the fair value of the date of change to shareholders' equity to the extent for which, as at the same date, the services were provided and the immediate accounting of any difference to the income statement; (iii) with reference to the transactions with share-based payment with net settlement arising from withholding at the source made by the employer in compliance with tax laws or regulations, it introduces an exception so that these transactions are classified

as equity-settled in full if they should be identified as such if there is not net settlement imposed by application of the tax legislation. These measures, in effect from financial years starting on or after 1 January 2018, are awaiting approval by the European Commission.

With "Transfers of Investment property - Amendments to IAS 40" of 8 December 2016, the IASB clarifies that an entity should reclassify a property to, or from, the category of property investments if and only if there is a change in use of the property; a change in management's intended use with regard to the property does not, in itself, constitute evidence of a change in use. These measures, in effect from financial years starting on or after 1 January 2018, are awaiting approval by the European Commission.

The IASB issued "Annual Improvements to IFRS 2012-2014 Cycle" on 25 September 2014 with which: (i) with reference to IFRS 5, it clarifies that any different classification of an asset (or discontinued operation) from held for sale to held for sale to shareholders (or vice versa) must not be considered a new discontinued operation plan but rather a continuation of the original plan; (ii) with reference to IFRS 7 "Financial instruments: disclosures", it provides an additional guide to determining whether or not residual involvement in a transferred financial asset exists if a service contract pertaining to it exists, such as to determine the level of information required; again with reference to the same standard, it also clarifies applicability of the disclosures required concerning the offsetting of financial assets and liabilities in interim financial statements; (iii) with reference to IAS 19, it clarifies that the discount rate to use for discounting bonds must be determined with reference to the market yields of securities of primary companies denominated in the same currency instead of that of the country of reference; (iv) with reference to IAS 34, it

clarifies the meaning of the reference to the information contained in other sections of the interim financial statements and specifies that they must be available with the same time frame.

On 12 October 2017, the International Accounting Standards Board (IASB) published an amendment to IFRS 9, Financial statements, in order to allow some financial instruments having advance payments with negative offsetting (the borrower is authorised to pay back the financial instrument at an amount that might be less than the capital and unpaid interest) to be measured at amortised cost or at fair value reported in other comprehensive income (FVOCI) instead of at the fair value through profit or loss (FVTPL).

The changes are effective for the years that begin on 1 January 2019 or at a later date, with the possibility of early application starting from actual application of IFRS 9 in its current formulation (1 January 2018).

The International Accounting Standards Board (IASB) published “Long-term interests in associates and joint ventures (Amendments to IAS 28)” on 12 October 2017, in order to clarify that an entity applies IFRS 9 Financial instruments to the long-term interests falling under the net investment in associates or joint ventures to which measurement by the equity method is not applied.

The changes are effective for the years that begin on 1 January 2019 or at a later date, with the possibility of early application starting from actual application of IFRS 9 in its current formulation (1 January 2018).

## 7. BUSINESS COMBINATION TRANSACTIONS

On 6 December 2017, the subsidiary Italgas Reti S.p.A. finalised acquisition of 100% of Enerco Distribuzione S.p.A., holder of 27 concessions in the provinces of Padua and Vicenza, and of 100% of the company S.G.S. S.r.l.

The price of €35,918 thousand was paid at the time of acquisition; an earn-out mechanism<sup>26</sup> based on the higher RAB value, if any, is also included and will be recognised by the Authority on the acquired concessions.

The transaction led to an increase in revenue and a reduction of Group profit of €253 thousand and €56 thousand, respectively, for the period falling between the acquisition date and 31 December 2017. If the transaction had been carried out on 1 January 2017, the contribution to the revenue and profit of the year would have been about €8,410 thousand and €994 thousand, respectively.

<sup>26</sup> The values recorded following the aggregation are subject to the assessment period pursuant to paragraph 45 of IFRS 3, which allows temporary amounts to be recognised in the closing financial statements while waiting to acquire additional information that might come from potential adjustments pertaining to the acquired assets and liabilities.

The fair value of the acquired net assets, shown in the table below, was €35,918 thousand; so no goodwill was posted in connection with the acquisition.

(€ thousands)	
Cash and cash equivalents	1,092
Trade and other receivables	2,591
Inventories	135
Tax assets	132
Other current assets	173
<b>Current assets</b>	<b>4,123</b>
Property, plant and equipment	54
Intangible assets	59,991
Other non-current assets	89
<b>Non-current assets</b>	<b>60,134</b>
<b>TOTAL ASSETS</b>	<b>64,257</b>
Short-term financial liabilities	6,117
Trade and other payables	5,169
Tax liabilities	954
<b>Current liabilities</b>	<b>12,240</b>
Long-term financial liabilities	5,548
Provisions for risks and charges	1,939
Provisions for employee benefits	241
Deferred tax liabilities	8,198
Other non-current liabilities	173
<b>Non-current liabilities</b>	<b>16,099</b>
<b>TOTAL LIABILITIES</b>	<b>28,339</b>
<b>NET VALUE OF ACQUIRED ASSETS</b>	<b>35,918</b>

The costs incurred for the transactions were not significant.

## 8. CASH AND CASH EQUIVALENTS

*Cash and cash equivalents*, equal to €2,831 thousand (€1,544 thousand as at 31 December 2016), refer to current account deposits held at banks.

Cash and cash equivalents are not subject to any usage restrictions.

A comprehensive analysis of the financial situation and major cash commitments during the year can be found in the Statement of Cash Flows.

## 9. OTHER FINANCIAL ASSETS HELD FOR TRADING OR AVAILABLE FOR SALE

The *other financial assets held for trading or available for sale*, amounting to €119 thousand, unchanged compared to 31 December 2016, pertain to the remaining portion of the shareholding of Italgas Reti S.p.A. in Acqua Campania S.p.A.

## 10. TRADE RECEIVABLES AND OTHER CURRENT AND NON-CURRENT RECEIVABLES

*Trade receivables and other current and non-current receivables*, amounting to €619,358 thousand (€579,246 thousand as at 31 December 2016) break down as follows:

(€ thousands)	31.12.2016			31.12.2017		
	Current	Non-current	Total	Current	Non-current	Total
Trade receivables	417,631		<b>417,631</b>	406,479		<b>406,479</b>
Financial receivables		156	<b>156</b>		156	<b>156</b>
- held for operations		156	<b>156</b>		156	<b>156</b>
Receivables from investment/ divestment activities	5,791		<b>5,791</b>	5,279		<b>5,279</b>
Other receivables	155,668		<b>155,668</b>	207,444		<b>207,444</b>
	<b>579,090</b>	<b>156</b>	<b>579,246</b>	<b>619,202</b>	<b>156</b>	<b>619,358</b>

Trade receivables (€406,479 thousand as at 31 December 2017 and €417,631 thousand as at 31 December 2016), which mainly relate to the gas distribution service and ancillary services, mainly involve receivables from sales companies (€285,899 thousand), of which from Eni S.p.A. (€170,239 thousand) and the Cassa per i Servizi Energetici e Ambientali (CSEA) relating to the equalisation<sup>27</sup> (€45,856 thousand) and other refunds (€35,654 thousand).

<sup>27</sup> The mechanism based on which the differences between what is invoiced to sales companies and the revenue restrictions defined by the Authority are recorded as debits/credits from the CSEA.

These are reported net of the provision for impairment losses (€20,702 thousand at 31 December 2017 and €20,578 thousand at 31 December 2016). Changes in the provision for impairment losses on receivables during the year are shown below:

(€ thousands)

	Provision for impairment at 31.12.2016	Change scope of consolidation	Provision	Uses	Other changes	Provision for impairment at 31.12.2017
Trade receivables	19,725	457	609	(1,777)		<b>19,014</b>
Other receivables	853		800		35	<b>1,688</b>
	<b>20,578</b>	<b>457</b>	<b>1,409</b>	<b>(1,777)</b>	<b>35</b>	<b>20,702</b>

Receivables for investment/disinvestment activities (€5,279 thousand as at 31 December 2017 and €5,791 thousand as at 31 December 2016) involve receivables for sales of property, plant and equipment and intangible assets.

Other receivables (€207,444 thousand as at 31 December 2017 and €155,668 thousand as at 31 December 2016) break down as follows:

(€ thousands)

	31.12.2016	31.12.2017
IRES receivables for the national tax consolidation scheme	15,558	<b>15,452</b>
Other receivables:	140,110	<b>191,992</b>
- Cassa per i Servizi Energetici e Ambientali (CSEA)	82,221	<b>137,901</b>
- Public administration	27,488	<b>28,874</b>
- Advances to suppliers	13,666	<b>15,715</b>
- from staff	4,886	<b>4,493</b>
- Other	11,849	<b>5,009</b>
	<b>155,668</b>	<b>207,444</b>

IRES receivables for the national tax consolidation scheme (€15,452 thousand at 31 December 2017) concern receivables with the former parent company, Eni, relating to the IRES refund request resulting from the partial IRAP deduction relating to tax years 2004 to 2007 (pursuant to Article 6 of Decree-Law 185 of 28 November 2008, converted into Law 2 of 28 January 2009) and tax years 2007 to 2011 (pursuant to Decree-Law 201/2011).

Receivables from the CSEA (€137,901 thousand as at 31 December 2017) relate to the additional components of gas distribution tariffs for €39,279 thousand (UG2<sup>28</sup> and Gas Bonus<sup>29</sup>) and for €98,622 thousand to Energy Efficiency Certificates.

Receivables from public administrations (€28,874 thousand) relate to receivables from Municipalities.

The item "Others" (€5,009 thousand as at 31 December 2017) mainly relates to receivables from Snam S.p.A. following the transfer of personnel to Italgas S.p.A. and Italgas Reti S.p.A.

The market value of trade and other receivables is analysed in the Note "Guarantees, commitments and risks - Other information about financial instruments". All receivables are in Euros.

The fair value measurement of trade and other receivables has no material impact considering the short period of time from when the receivable arises and its due date and contractual conditions.

The seniority of trade and other receivables is shown below:

(€ thousands)	31.12.2016			31.12.2017		
	Trade receivables	Other receivables (*)	Total	Trade receivables	Other receivables (*)	Total
Non-overdue and non-impaired receivables	389,048	161,410	<b>550,458</b>	393,802	212,723	<b>606,525</b>
Overdue and non-impaired receivables:	28,583	49	<b>28,632</b>	12,677		<b>12,677</b>
- from 0 to 3 months	9,092		<b>9,092</b>	5,075		<b>5,075</b>
- from 3 to 6 months	1,216		<b>1,216</b>	3,885		<b>3,885</b>
- from 6 to 12 months	3,737		<b>3,737</b>	1,262		<b>1,262</b>
- beyond 12 months	14,538	49	<b>14,587</b>	2,455		<b>2,455</b>
	<b>417,631</b>	<b>161,459</b>	<b>579,090</b>	<b>406,479</b>	<b>212,723</b>	<b>619,202</b>

(\*) They include the Receivables for investment/divestment activities and Other receivables.

Overdue and non-impaired receivables equal to €12,677 thousand and mainly involve relations with gas marketing companies for the distribution service, covered by guarantee policies, and other receivables from public administrations.

28 Additional component of the distribution tariff for the purpose of containing the cost of the gas service for low consumption end users.

29 Component relating to requests for subsidies for natural gas provision by economically disadvantaged customers.



Non-recourse, non-notification sale transactions of trade receivables and other receivables, also not overdue, were carried out in 2017 for a nominal amount of €93,520 and €160,583 thousand with the relevant increase of cash and cash equivalents.

Due to the contractual provisions set out, collection of the sold receivables is managed and, within their limits, the amounts received at the factoring are transferred.

Receivables from related parties are described in the note "Related-party transactions".

Specific information on credit risk is provided in the note "Guarantees, commitments and risks - Financial risk management - Credit risk".

## 11. INVENTORIES

*Inventories*, which amount to €22,410 thousand, are analysed in the table below:

(€ thousands)	31.12.2016			31.12.2017		
	Gross value	Provision for impairment losses	Net value	Gross value	Provision for impairment losses	Net value
<b>Inventories</b>	<b>32,865</b>	<b>(284)</b>	<b>32,581</b>	<b>22,695</b>	<b>(285)</b>	<b>22,410</b>
- Raw materials, consumables and supplies	32,865	(284)	<b>32,581</b>	22,695	(285)	<b>22,410</b>
- Finished goods and goods for resale						
	<b>32,865</b>	<b>(284)</b>	<b>32,581</b>	<b>22,695</b>	<b>(285)</b>	<b>22,410</b>

Inventories of raw materials, consumables and supplies (€22,410 thousand at 31 December 2017) mainly consisted of gas meters in connection with the replacement plan. The provision for impairment is €285 thousand.

Inventories are not collateralised. Inventories do not secure liabilities, nor are they recognised at net realisation value.

The €-10,171 thousand change in inventories includes the effect of the change in the scope of consolidation.

## 12. CURRENT INCOME TAX ASSETS/LIABILITIES AND OTHER CURRENT TAX ASSETS/LIABILITIES

*Current income tax assets/liabilities and other current tax assets/liabilities break down as follows:*

(€ thousands)	31.12.2016	31.12.2017
<b>Current income tax assets</b>	<b>34,607</b>	<b>8,571</b>
- IRES	33,215	8,229
- IRAP	475	342
- Other assets	917	
<b>Other current tax assets</b>	<b>3,318</b>	<b>21,139</b>
- VAT	814	18,837
- Other taxes	2,504	2,302
<b>Current income tax liabilities</b>	<b>945</b>	<b>4,489</b>
- IRES	933	3,150
- IRAP	12	1,339
<b>Other current tax liabilities</b>	<b>12,515</b>	<b>11,424</b>
- VAT	3,990	2,587
- IRPEF withholdings for employees	7,560	8,144
- Other taxes	965	693
	<b>24,465</b>	<b>13,797</b>

*Current income tax assets* of €8,571 thousand mainly relate to IRES receivables involving the Group tax consolidation scheme.

*Other current income tax assets* of €21,139 thousand mainly relate to VAT receivables (€18,837 thousand).

Non-recourse, non-notification sale transactions of VAT receivables were carried out in 2017 for the amount of €24,563 thousand, with a corresponding increase of cash and cash equivalents.

Due to the contractual provisions set out, collection of the sold receivables is managed and, within their limits, the amounts received at the factoring are transferred.

*Current income tax liabilities* of €4,489 thousand refer to payables to the tax authorities for IRES (€3,150 thousand).

*Other current tax liabilities* of €11,424 thousand mainly refer to payables to the tax authorities for IRPEF withholdings for employees (€8,144 thousand).

Taxes pertaining to the year under review are shown in the note "Income taxes".

### 13. OTHER CURRENT AND NON-CURRENT ASSETS

*Other current assets*, amounting to €5,944 thousand, and *other non-current assets*, amounting to €77,891 thousand, break down as follows:

(€ thousands)	31.12.2016			31.12.2017		
	Current	Non-current	Total	Current	Non-current	Total
Other regulated assets	2,264	31,004	<b>33,268</b>	3,236	75,310	<b>78,546</b>
Other assets	2,146	6,870	<b>9,016</b>	2,708	2,581	<b>5,289</b>
- Prepayments	2,146	5,519	<b>7,665</b>	2,708	1,148	<b>3,856</b>
- Security deposits		1,351	<b>1,351</b>		1,433	<b>1,433</b>
	<b>4,410</b>	<b>37,874</b>	<b>42,284</b>	<b>5,944</b>	<b>77,891</b>	<b>83,835</b>

Other regulated assets (78,546 thousand as at 31 December 2017) essentially relate to the tariff recognition, by the Authority, following the plan to replace traditional meters with electronic meters.

The remaining item, equal to €5,289 thousand, mainly concerns the prepayments related to costs incurred when undersigning revolving credit lines (€1,496 thousand, of which €548 thousand short-term), long-term security deposits (€1,433 thousand) and prepayments on insurance premiums and rentals (€511 thousand, of which €466 thousand short-term).

## 14. PROPERTY, PLANT AND EQUIPMENT

*Property, plant and equipment*, which amounts to €224,651 thousand as at 31 December 2017 (€227,476 thousand at 31 December 2016), breaks down as follows:

(€ thousands)		31.12.2016					
	Land	Buildings	Plant and equipment	Industrial and commercial equipment	Other assets	Work in progress and payments on account	Total
<b>Cost at 1.6.2016</b>							
Investments						4,761	<b>4,761</b>
Divestments				(864)			<b>(864)</b>
Change in scope of consolidation	11,197	349,737	11,721	179,475		5,699	<b>557,829</b>
Other changes		1,258	15	6,253		(7,510)	<b>16</b>
<b>Cost at 31.12.2016</b>	<b>11,197</b>	<b>350,995</b>	<b>11,736</b>	<b>184,864</b>		<b>2,950</b>	<b>561,742</b>
<b>Accumulated depreciation at 1.6.2016</b>							
Total amortisation and depreciation		(683)	(47)	(1,419)			<b>(2,149)</b>
Divestments				844			<b>844</b>
Change in scope of consolidation		(172,110)	(5,253)	(151,400)			<b>(328,763)</b>
Other changes		(341)	341	1			<b>1</b>
<b>Accumulated depreciation at 31.12.2016</b>		<b>(173,134)</b>	<b>(4,959)</b>	<b>(151,974)</b>			<b>(330,067)</b>
<b>Provision for impairment losses at 1.6.2016</b>							
Change in scope of consolidation			(4,199)				<b>(4,199)</b>
<b>Provision for impairment losses at 31.12.2016</b>			<b>(4,199)</b>				<b>(4,199)</b>
<b>Net balance at 1.6.2016</b>							
<b>Net balance at 31.12.2016</b>	<b>11,197</b>	<b>177,861</b>	<b>2,578</b>	<b>32,890</b>		<b>2,950</b>	<b>227,476</b>

(€ thousands)

31.12.2017

	Land	Buildings	Plant and equipment	Industrial and commercial equipment	Other assets	Work in progress and payments on account	Total
<b>Cost at 31.12.2016</b>	<b>11.197</b>	<b>350.995</b>	<b>11.736</b>	<b>184.864</b>		<b>2.950</b>	<b>561.742</b>
Investments		8		2.287	45	8.527	<b>10.867</b>
Divestments	(2)			(44.587)	(1)		<b>(44.590)</b>
Change in scope of consolidation					158		<b>158</b>
Other changes	40	1.645	66	7.653	704	(7.185)	<b>2.923</b>
<b>Cost at 31.12.2017</b>	<b>11.235</b>	<b>352.648</b>	<b>11.802</b>	<b>150.217</b>	<b>906</b>	<b>4.292</b>	<b>531.100</b>
<b>Accumulated depreciation at 31.12.2016</b>		<b>(173.134)</b>	<b>(4.959)</b>	<b>(151.974)</b>			<b>(330.067)</b>
Total amortisation and depreciation		(5.776)	(302)	(10.112)	(71)		<b>(16.261)</b>
Divestments				44.153			<b>44.153</b>
Change in scope of consolidation					(104)		<b>(104)</b>
Other changes		479	(2)	(218)	(199)		<b>60</b>
<b>Accumulated depreciation at 31.12.2017</b>		<b>(178.431)</b>	<b>(5.263)</b>	<b>(118.151)</b>	<b>(374)</b>		<b>(302.219)</b>
<b>Provision for impairment losses at 31.12.2016</b>			<b>(4.199)</b>				<b>(4.199)</b>
(Write-down)/Value restorations						(31)	<b>(31)</b>
<b>Provision for impairment losses at 31.12.2017</b>			<b>(4.199)</b>			<b>(31)</b>	<b>(4.230)</b>
<b>Net balance at 31.12.2016</b>	<b>11.197</b>	<b>177.861</b>	<b>2.578</b>	<b>32.890</b>		<b>2.950</b>	<b>227.476</b>
<b>Net balance at 31.12.2017</b>	<b>11.235</b>	<b>174.217</b>	<b>2.340</b>	<b>32.066</b>	<b>532</b>	<b>4.261</b>	<b>224.651</b>

Investments (€10,867 thousand) mainly refer to fixed assets under construction. Depreciation (€16,261 thousand) refers to economic and technical depreciation determined on the basis of the useful life of the assets or their remaining possible use by the Company.

During the year, there were no changes in the estimated useful life of assets or in the depreciation rates applied and explained by category in the Note - "Measurement criteria - Property, plant and equipment".

The provision for impairment of €4,230 thousand mostly relates to the district heating plant and equipment of the municipality of Cologno Monzese (MB).

Property, plant and equipment of the Company are not collateralised and there are no restrictions on the ownership of property, plant and equipment.

Contractual commitments to purchase property, plant and equipment, and to provide services related to the construction thereof, are reported in the Note "Guarantees, commitments and risks".

## 15. INTANGIBLE ASSETS

Intangible assets, which amount to €4,676,561 thousand as at 31 December (€4,486,511 at 31 December 2016) break down as follows:

(€ thousands)		31.12.2016				
		Definite useful life			Indefinite useful life	
	Service concession agreements	Industrial patent rights and intellectual property rights	Work in progress and payments on account	Other Intangible Assets	Goodwill	Total
<b>Cost at 1.6.2016</b>						
Investments	59,440	531	14,419	692		<b>75,082</b>
Change in the scope of consolidation	7,444,433	332,138	27,153	36,881	9,738	<b>7,850,343</b>
Divestments	(8,697)		(650)			<b>(9,347)</b>
Other changes	20,080	21,211	(20,056)	482		<b>21,717</b>
<b>Cost at 31.12.2016</b>	<b>7,515,256</b>	<b>353,880</b>	<b>20,866</b>	<b>38,055</b>	<b>9,738</b>	<b>7,937,795</b>
<b>Accumulated depreciation at 1.6.2016</b>						
Total amortisation and depreciation	(69,449)	(4,722)		(1,669)		<b>(75,840)</b>
Change in the scope of consolidation	(3,067,745)	(268,380)		(25,453)		<b>(3,361,578)</b>
Divestments	9,402					<b>9,402</b>
Other changes	(22,172)	36				<b>(22,136)</b>
<b>Accumulated depreciation at 31.12.2016</b>	<b>(3,149,964)</b>	<b>(273,066)</b>		<b>(27,122)</b>		<b>(3,450,152)</b>
<b>Provision for impairment losses at 1.6.2016</b>						
Change in the scope of consolidation	(1,132)					<b>(1,132)</b>
<b>Provision for impairment losses at 31.12.2016</b>	<b>(1,132)</b>					<b>(1,132)</b>
<b>Net balance at 1.6.2016</b>						
<b>Net balance at 31.12.2016</b>	<b>4,364,160</b>	<b>80,814</b>	<b>20,866</b>	<b>10,933</b>	<b>9,738</b>	<b>4,486,511</b>



(€ thousands)

31.12.2017

	Definite useful life				Indefinite useful life	Total
	Service concession agreements	Industrial patent rights and intellectual property rights	Work in progress and payments on account	Other Intangible Assets	Goodwill	
<b>Cost at 31.12.2016</b>	<b>7.515.256</b>	<b>353.880</b>	<b>20.866</b>	<b>38.055</b>	<b>9.738</b>	<b>7.937.795</b>
Investments	451.048	178	27.943	3.267		<b>482.436</b>
Change in the scope of consolidation	76.705	628	3	20		<b>77.356</b>
Divestments	(119.434)	(79)				<b>(119.513)</b>
Other changes	445	37.735	(36.191)	(4.962)		<b>(2.973)</b>
<b>Cost at 31.12.2017</b>	<b>7.924.020</b>	<b>392.342</b>	<b>12.621</b>	<b>36.380</b>	<b>9.738</b>	<b>8.375.101</b>
<b>Accumulated depreciation at 31.12.2016</b>	<b>(3.149.964)</b>	<b>(273.066)</b>		<b>(27.122)</b>		<b>(3.450.152)</b>
Total amortisation and depreciation	(295.185)	(31.662)		(8.893)		<b>(335.740)</b>
Change in the scope of consolidation	(16.720)	(626)		(19)		<b>(17.365)</b>
Divestments	111.723	6				<b>111.729</b>
Other changes	430	(8.066)		8.066		<b>430</b>
<b>Accumulated depreciation at 31.12.2017</b>	<b>(3.349.716)</b>	<b>(313.414)</b>		<b>(27.968)</b>		<b>(3.691.098)</b>
<b>Provision for impairment losses at 31.12.2016</b>	<b>(1.132)</b>					<b>(1.132)</b>
(Write-down)/Value restorations	(4.214)			(2.096)		<b>(6.310)</b>
Change in the scope of consolidation						
<b>Provision for impairment losses at 31.12.2017</b>	<b>(5.346)</b>			<b>(2.096)</b>		<b>(7.442)</b>
<b>Net balance at 31.12.2016</b>	<b>4.364.160</b>	<b>80.814</b>	<b>20.866</b>	<b>10.933</b>	<b>9.738</b>	<b>4.486.511</b>
<b>Net balance at 31.12.2017</b>	<b>4.568.958</b>	<b>78.928</b>	<b>12.621</b>	<b>6.316</b>	<b>9.738</b>	<b>9.738</b>

Service concession agreements (€4,568,958 thousand as at 31 December 2017) refer to agreements between the public and private sectors on the development, financing, management and maintenance of infrastructure under concession by a contracting party. The provisions relating to the service concession agreements are applicable for Italgas in its role as a public service natural gas distributor, i.e. they are applicable to the agreements

under which the operator is committed to providing the public natural gas distribution service at the tariff established by the Authority, holding the right to use the infrastructure, which is controlled by the grantor, for the purposes of providing the public service.

Industrial patent rights and intellectual property rights (€78,928 thousand as at 31 December 2017) mainly concern information systems and applications in support of operating activities.

Intangible assets with an indefinite useful life (€9,738 thousand as at 31 December 2017) consist mainly of the goodwill recognised in 2008 following the acquisition by Italgas of 100% of the shares of Siciliana Gas. Goodwill was subjected to an impairment test which did not reveal losses in value compared with the recoverable amount and the carrying amount.

Although there are no impairment indicators, the Group decided to submit the entire value of the intangible assets to an impairment test in view of their significance. Based on their recoverable value, no impairment losses emerged.

Investments for the year, equal to €482,436 thousand, mainly relate to service agreements awarded for the maintenance and development of the remote reading network (€451,048 thousand) and fixed assets under construction (€27,943 thousand).

Capital contributions from government authorities and other entities, €28,573 thousand, are recorded as a deduction in the net value of service concession agreements.

Changes in the scope of consolidation (€59,991 thousand, net of the related provisions for depreciation, amortisation and impairment losses) relate to the acquisition of the stakeholding in Enerco Distribuzione S.p.A. by Italgas Rete S.p.A.

Amortisation refers to economic and technical amortisation determined on the basis of the finite useful life of the intangible assets or their remaining possible use by the Company. The amount of €335,740 thousand includes greater amortisation as a result of the reduction in the useful life of traditional meters<sup>30</sup>, subject to the plan to replace them with electronic meters, required by AEEGSI resolutions under the scope of the implementation of the remote metering reading plan (€50,153 thousand).

Research and development expenses of the period are not of a considerable amount.

Contractual commitments to purchase intangible assets, and to provide services related to the development thereof, are reported in the Note - "Guarantees, commitments and risks".

<sup>30</sup> The useful life of the meters included in the project pursuant to ARERA resolutions 631/13 and 554/15 was adjusted, in order to complete the amortisation process in line with the meter replacement plan, scheduled for completion by 2018.

## 16. INVESTMENTS VALUED USING THE EQUITY METHOD AND OTHER INVESTMENTS

The *investments valued using the equity method*, which amounts to €184,829 thousand (€175,707 thousand as at 31 December 2016) and the *other investments*, which total €54 thousand) (unchanged compared to 31 December 2016), breaks down as follows:

(€ thousands)			
	Investments in joint ventures	other	Total
<b>Opening balance at 31.12.2016</b>	<b>175,707</b>	<b>54</b>	<b>175,761</b>
Income (charges) from measurement using the equity method	22,927		22,927
Decrease for dividends	(13,805)		(13,805)
<b>Closing balance at 31.12.2017</b>	<b>184,829</b>	<b>54</b>	<b>184,883</b>

Income from measurement using the equity method (€22,927 thousand) mostly refers to Toscana Energia S.p.A. (€22,753 thousand).

Equity investments are not collateralised.

With regard to the recoverable value of equity investments, for companies operating exclusively in regulated businesses, recoverable value is calculated using the adjusted RAB value of the net financial position.

In the light of the positive performance of those companies, the value estimated in this way is higher for all equity investments than the value recorded in the financial statements, and therefore there are no losses in value.

### OTHER INFORMATION ON EQUITY INVESTMENTS

In accordance with the provisions of IFRS 12 - "Disclosure of interests in other entities", the economic and financial data for joint ventures and associates are provided below.

### INVESTMENTS IN JOINT VENTURES

The IFRS-compliant economic and financial data for each significant joint venture<sup>31</sup>, are reported below:

(€ thousands)	31.12.2017		
	Toscana Energia S.p.A.	Umbria Distribuzione Gas S.p.A.	Sant'Angelo Lodigiano S.p.A.
Current assets	96,916	2,348	814
- of which cash and cash equivalents	4,771		
Non-current assets	820,461	7,169	3,108
<b>Total assets</b>	<b>917,377</b>	<b>9,517</b>	<b>3,922</b>
Current liabilities	264,084	6,500	1,489
- of which current financial liabilities	152,453	3,044	580
Non-current liabilities	248,023	64	171
- of which non-current financial liabilities non-current	225,109		
<b>Total liabilities</b>	<b>512,107</b>	<b>6,564</b>	<b>1,660</b>
<b>Shareholders' Equity</b>	<b>405,270</b>	<b>2,953</b>	<b>2,262</b>
Equity investment held by the group %	48.08%	45.00%	50.00%
Group interest	194,854	1,329	1,131
Other adjustments	(12,485)		
<b>Book value of the equity investment</b>	<b>182,369</b>	<b>1,329</b>	<b>1,131</b>
Revenue	139,850	6,473	1,674
Operating costs	(40,991)	(5,789)	(1,001)
Amortisation, depreciation and impairment	(41,902)	(457)	(169)
<b>EBIT</b>	<b>56,957</b>	<b>227</b>	<b>504</b>
Financial income (expense)	(3,165)	(101)	(13)
Income (expense) from equity investments	994		
Income taxes	(15,826)	(35)	(137)
<b>Net profit</b>	<b>38,960</b>	<b>91</b>	<b>354</b>
Other components of comprehensive income			
<b>Total comprehensive income</b>	<b>38,960</b>	<b>91</b>	<b>354</b>

31 Unless otherwise indicated, the financial statement figures for joint ventures, reported in full, have been updated to include adjustments made by the Parent Company pursuant to the equity-accounting method.

## Information on Investments in joint ventures

### ***Toscana Energia S.p.A.***

Toscana Energia S.p.A. operates in the natural gas distribution segment in Tuscany.

The share capital of Toscana Energia S.p.A. is owned by Italgas Reti S.p.A. (48.08%), the Municipality of Florence (20.61%), Publiservizi S.p.A. (10.38%)<sup>32</sup>, other Local Authorities<sup>33</sup> (20.26%) and banking institutions (0.67%).

The corporate governance rules stipulate that decisions on significant activities must be taken with the unanimous consent of the private (Italgas Reti S.p.A.) and public (municipalities) shareholders.

Toscana Energia S.p.A.'s consolidated financial statements include Toscana Energia S.p.A. and Toscana Energia Green S.p.A.

### ***Umbria Distribuzione Gas S.p.A.***

Umbria Distribuzione Gas S.p.A. operates in the natural gas distribution segment in Umbria.

The share capital of Umbria Distribuzione S.p.A. is owned by Italgas Reti S.p.A. (45%), by A.S.M. Terni S.p.A. (40%) and by Acea S.p.A. (15%).

Umbria Distribuzione Gas, as the holder of an 11-year mandate, manages the natural gas distribution service in the Terni municipality, making use of an integrated system of infrastructures, owned by Terni Reti S.r.l., a wholly-owned subsidiary of the Terni municipality, comprising stations for withdrawing gas from the transportation network, pressure reduction plants, the local transportation and distribution network, user derivation plants and redelivery points comprising technical equipment featuring meters at the end users.

### ***Metano Sant'Angelo Lodigiano S.p.A.***

Metano Sant'Angelo Lodigiano S.p.A. operates in the natural gas distribution sector in the municipalities of Sant'Angelo Lodigiano (LO), Villanova del Sillaro, Bargano (LO), Castiraga Vidardo (LO), Marudo (LO) and Villanterio (PV).

The corporate governance rules stipulate that decisions on significant activities must be taken with the unanimous consent of the private (Italgas Reti S.p.A.) and public (municipalities) shareholders.

<sup>32</sup> A fully public, pure holding company. The company's shareholders are 35 Tuscan municipalities in the provinces of Florence, Pisa, Pistoia and Siena.

<sup>33</sup> Data taken from the financial statements of Toscana Energia S.p.A. for the year ended 31 December 2017.

## 17. ASSETS HELD FOR SALE AND ASSOCIATED LIABILITIES

*Assets held for sale and associated liabilities*, of respectively €11 thousand (€18,979 thousand as at 31 December 2016) dropped by €18,968 thousand following finalisation of the contract of sale of the property in Via Ostiense in Rome to Eni S.p.A. for the amount of €21,972 thousand.

The table below summarises the breakdown of Assets and Liabilities classified as available for sale:

(€ thousands)	31.12.2016	31.12.2017
<b>Non-current assets held for sale</b>	<b>24,949</b>	<b>11</b>
Buildings	24,949	11
<b>Associated liabilities</b>	<b>5,970</b>	
Provisions for environmental risks and charges	5,970	
	<b>18,979</b>	<b>11</b>

The residual amount at 31 December 2017 totals €11 thousand and again refers to the property in Via Ostiense in Rome, not yet finalised as per the contract of sale.





## 18. SHORT-TERM FINANCIAL LIABILITIES, LONG-TERM FINANCIAL LIABILITIES AND SHORT-TERM PORTIONS OF LONG-TERM FINANCIAL LIABILITIES

Short-term financial liabilities, amounting to €81,133 thousand (€2,695,603 thousand as at 31 December 2016) and long-term financial liabilities, including short-term portions of long-term liabilities totalling €3,642,087 thousand (€923,440 thousand as at 31 December 2016), break down as follows:

(€ thousands)

31.12.2016					
	Short-term liabilities	Long-term liabilities			Total long-term liabilities
		Short-term portion	Long-term portion due within 5 years	Long-term portion due beyond 5 years	
Bank loans	2,695,603	435	293,005	630,000	923,440
Bonds					
	<b>2,695,603</b>	<b>435</b>	<b>293,005</b>	<b>630,000</b>	<b>923,440</b>

31.12.2017					
	Short-term liabilities	Long-term liabilities			Total long-term liabilities
		Short-term portion	Long-term portion due within 5 years	Long-term portion due beyond 5 years	
Bank loans	81,133	1,770	271,671	716,714	990,155
Bonds		23,273	743,080	1,885,579	2,651,932
	<b>81,133</b>	<b>25,043</b>	<b>1,014,751</b>	<b>2,602,293</b>	<b>3,642,087</b>

### SHORT-TERM FINANCIAL LIABILITIES

Short-term financial liabilities, amounting to €81,133 thousand, mainly relate to utilisations of uncommitted bank credit lines.

There are no short-term financial liabilities denominated in currencies other than the Euro.

The weighted average interest rate on short-term financial liabilities was 0.00%.

### LONG-TERM FINANCIAL LIABILITIES AND SHORT-TERM PORTIONS OF LONG-TERM FINANCIAL LIABILITIES

Long-term financial liabilities, including short-term portions of long-term liabilities, amounted to €3,642,087 thousand, net of accruals and amortised cost (€1,932 thousand as at 31 December 2017).

Bonds, amounting to €2,651,932 thousand as at 31 December 2017, relate to the bonds issued for a face value of €2,650,000 thousand and €1,932 thousand relating to the accruals and adjustments of amortised cost, and break down as follows:

(€ thousands)

Issuing company	Emission (year)	Currency	Nominal Value	Adjustments (a)	Balance as at 31.12.2017	Rate (%)	Due date (year)
<b>Euro Medium Term Notes</b>							
ITALGAS S.p.A.	2017	€	750,000	(3,365)	746,635	0.5	2022
ITALGAS S.p.A.	2017	€	650,000	2,335	652,335	1.125	2024
ITALGAS S.p.A.	2017	€	750,000	3,758	753,758	1.625	2027
ITALGAS S.p.A.	2017	€	500,000	(796)	499,204	1.625	2029
		€	<b>2,650,000</b>	<b>1,932</b>	<b>2,651,932</b>		

(a) Includes issue premium/discount and accrual of interest.

Debts due to bank loans (€990,115 thousand as at 31 December 2017; €923,440 thousand at 31 December 2016) mainly refer to the following loans undersigned with:

- European Investment Bank (EIB):
  - novation agreement, stipulated on 26 October 2016, between Snam and Italgas, for two loans amounting to a nominal value of €424 million, previously stipulated between Snam and the EIB and expiring on 30 October 2033 and 22 October 2017; on 27 December 2017 the €300 million EIB loan was repaid in light of the granting of a new loan on 28 December 2017;
  - on 12 December 2016, of a loan of €300 million, expiring on 30 November 2032;
  - on 28 December 2017, of a new loan of €360 million, expiring on 15 December 2037;
- Banca Nazionale del Lavoro (BNL) for a nominal value of €200 million, expiring on 28 October 2019.

There are no other long-term bank loans denominated in currencies other than the euro.

There were no breaches of loan agreements as at the reporting date.

The weighted average interest rate on debts due to bank loans used was 0.50%.

The market value of short- and long-term financial liabilities is reported in the note, "Other information about financial instruments", which is hereby referred to.

The Company had unused committed lines of credit worth €1.1 billion.

#### FINANCIAL COVENANTS AND NEGATIVE PLEDGE COMMITMENTS

As at 31 December 2017, there were no financial covenants and unsecured bilateral and syndicated loan agreements in place with banks and other financial institutions. Some of these contracts provide, inter alia, for the following: (i) negative pledge commitments pursuant to which Italgas and its subsidiaries are subject to limitations on pledging real property rights or other restrictions on all or part of the respective assets, shares or merchandise; (ii) pari passu and change-of-control clauses; and (iii) limitations on certain extraordinary transactions that the Company and its subsidiaries may carry out.

As at 31 December 2017, Italgas also had medium/long-term loans taken out with the European Investment Bank (EIB), the contractual clauses of which are broadly in line with those described above. Exclusively for the EIB loans, the lender has the option

to request additional guarantees if Italgas' credit rating is downgraded to BBB- (Standard & Poor's/Fitch Ratings Limited) or Baa3 (Moody's) for at least two of the three ratings agencies.

As at 31 December 2017, the banking financial liabilities subject to these restrictive clauses amounted to approximately €0.99 billion.

Failure to comply with the commitments established for these loans - in some cases only when this non-compliance is not remedied within a set time period - and the occurrence of other events, such as cross-default events, some of which are subject to specific threshold values, may result in Italgas' failure to comply and could trigger the early repayment of the relative loan.

As at 31 December 2017, there were no identified events resulting in failure to comply with the aforementioned commitments.

### BREAKDOWN OF NET FINANCIAL DEBT

The breakdown of net financial debt, showing related-party transactions, is provided in the following table:

(€ thousands)	31.12.2016			31.12.2017		
	Current	Non-current	Total	Current	Non-current	Total
A. Cash and cash equivalents	1,544		1,544	2,831		2,831
B. Securities held for sale and to be held to maturity	119		119	119		119
<b>C. Liquidity (A+B)</b>	<b>1,663</b>		<b>1,663</b>	<b>2,950</b>		<b>2,950</b>
D. Financial receivables not held for operations						
E. Short-term financial liabilities to banks (*)	2,696,038		2,696,038	82,903		82,903
F. Long-term financial liabilities to banks		923,005	923,005		988,385	988,385
G. Bonds				23,273	2,628,659	2,651,932
H. Short-term financial liabilities to related entities						
I. Long-term financial liabilities to related entities						
L. Other short-term financial liabilities						
M. Other long-term financial liabilities						
<b>N. Gross financial debt (E+F+G+H+I+L+M)</b>	<b>2,696,038</b>	<b>923,005</b>	<b>3,619,043</b>	<b>106,176</b>	<b>3,617,044</b>	<b>3,723,220</b>
<b>O. Net financial debt (N-C-D)</b>	<b>2,694,375</b>	<b>923,005</b>	<b>3,617,380</b>	<b>103,226</b>	<b>3,617,044</b>	<b>3,720,270</b>

(\*) This amount includes the short-term portion of long-term financial liabilities.

### 19. TRADE AND OTHER PAYABLES

Trade payables and other payables, which amount to €498,174 thousand as at 31 December 2017 (€443,112 thousand as at 31 December 2016) comprise the following:

(€ thousands)	31.12.2016	31.12.2017
Trade payables	174,534	184,050
Payables for investment activities	102,855	140,618
Other payables	165,723	173,506
	<b>443,112</b>	<b>498,174</b>

Trade payables (€184,050 thousand as at 31 December 2017; €174,534 thousand as at 31 December 2016) relate mainly to payables to suppliers.

Payables for investment activities equal to €140,618 thousand as at 31 December 2017 relate to payables to suppliers.

Other payables (€173,506 thousand) break down as follows:

(€ thousands)	31.12.2016	31.12.2017
Payables to the public administration	48,937	42,743
Payables to the Cassa per i Servizi Energetici e Ambientali (CSEA)	47,632	57,442
Payables to personnel	39,347	39,548
Payables to social security institutions	19,327	19,157
Payables to consultants and professionals	4,265	5,923
Other payables	6,215	8,693
	<b>165,723</b>	<b>173,506</b>

Payables to the public administration (€42,743 thousand) primarily involve payables to municipalities for concession fees for the distribution business.

Payables to the CSEA (€57,442 thousand) relate to several ancillary components of tariffs for the gas distribution service to be paid to this Fund (RE, RS, UG1 and GS)<sup>34</sup>.

Payables to personnel (€39,548 thousand) involve payables mainly for holidays accrued and not taken, the fourteenth months' pay and performance-related pay.

Payables to related parties are described in the note "Related-party transactions".

The book value of trade payables and other payables, considering the limited time interval between the occurrence of the payable and its maturity, is an approximation of the fair value. The market value of trade and other payables is provided in the Note - "Guarantees, commitments and risks - Other information on financial instruments".

34 These components refer to: (i) RE - Variable portion to cover the expenses for calculating and implementing energy savings and the development of renewable energy sources in the natural gas sector; (ii) RS - Variable portion as coverage for expenses for gas services quality; (iii) UG1 - Variable portion to cover any imbalances in the equalisation system and to cover any adjustments; and (iv) GS - Variable portion to cover the tariff compensation system for economically disadvantaged customers.

## 20. OTHER CURRENT AND NON-CURRENT LIABILITIES

*Other current liabilities and other non-current liabilities are broken down below:*

(€ thousands)	31.12.2016			31.12.2017		
	Current	Non-current	Total	Current	Non-current	Total
Other liabilities from regulated activities						
Other liabilities	193	4,876	5,069	182	2,055	2,237
- Liabilities for security deposits		4,839	4,839		1,849	1,849
- Other	193	37	230	182	206	388
	193	4,876	5,069	182	2,055	2,237

Other liabilities, totalling €2,237 thousand, mainly regard long-term security deposits (€1,849 thousand).

## 21. PROVISIONS FOR RISKS AND CHARGES

*Provisions for risks and charges, which amount to €208,246 thousand as at 31 December 2017 (€230,524 thousand as at 31 December 2016) comprise the following:*

(€ thousands)	31.12.2016							
	Uses							
	Opening balance	Change in scope of consolidation	Provisions	Increase for the passing of time	against charges	due to surplus	Other changes	Closing balance
Provision for environmental risks and charges		135,913	2,698	(682)	(2,039)	(310)		135,580
Provision for litigation		22,576	393		(861)	(656)		21,452
Provisions for other risks - energy efficiency certificates		9,622	3,906		(202)	(124)		13,202
Provision for plant upgrade risks		19,707			(167)			19,540
Provisions for retirement risks		5,070	14,873		(1)		(2,991)	16,951
Other personnel risk provisions		804	2,672		(69)	512	3,603	7,522
Risk provision for tax disputes		1,722	1,827		(49)	(4)		3,496
Other provisions		13,274	106		(87)	(512)		12,781
		208,688	26,475	(682)	(3,475)	(1,094)	612	230,524



(€ thousands)

31.12.2017

	Opening balance	Change in scope of consolidation	Provisions	Increase for the passing of time	Uses			Closing balance
					against charges	due to surplus	Other changes	
Provision for environmental risks and charges	135,580		242	486	(6,130)			<b>130,178</b>
Provision for litigation	21,452	802	1,589		(5,788)	(3,067)	25	<b>15,013</b>
Provisions for other risks - energy efficiency certificates	13,202		8,190		(7,505)			<b>13,887</b>
Provision for plant upgrade risks	19,540				(126)	(19,414)		
Provisions for retirement risks	16,951		5,345		(10,106)			<b>12,190</b>
Provision for op. restoration of metering			16,000					<b>16,000</b>
Risk provision for ICT Snam contract			8,419					<b>8,419</b>
Other personnel risk provisions	7,522		900		(895)	(2,909)	12	<b>4,630</b>
Risk provision for tax disputes	3,496		1,051		(1,674)	(1,107)		<b>1,766</b>
Other provisions	12,781	1,137	2,179		(1,243)	(8,666)	(25)	<b>6,163</b>
	<b>230,524</b>	<b>1,939</b>	<b>43,915</b>	<b>486</b>	<b>(33,467)</b>	<b>(35,163)</b>		<b>12 208,246</b>

The provision for environmental risks and charges (€130,178 thousand as at 31 December 2017; €135,580 thousand as at 31 December 2016) mainly included costs for environmental soil reclamation, pursuant to Law 471/1999, as subsequently amended, primarily for the disposal of solid waste, in relation to the distribution business.

The provision for litigation (€15,013 thousand) included costs which the Company has estimated it will incur for existing lawsuits.

The Energy Efficiency Certificates risk provision (€13,887 thousand) is connected with reaching the Energy Efficiency Certificates targets (TEE) set by the Authority.

The adjustments to facilities risk provision is totally released against completion of the adjustment interventions required by the inspections carried out by the judicial administration in 2014 that showed no need for further checks.

The provision for operational restoration of metering, totalling €16,000, comprises the costs estimated for replacing/restoring operations of the G4 and G6 smart meters having operational problems.

The risk provision for early retirement (€12,190 thousand) involves personnel incentive and mobility schemes.

In accordance with ESMA Recommendation 2015/1608 of 27 October 2015, the effects on provisions of risks and charges arising from a reasonably possible change to the discount rate used at year-end are shown below.

The sensitivity<sup>35</sup> of the discount rate represents the change in the value of the actuarial liability obtained using the end-of-year valuation data, changing the discount rate without any change in the other assumptions.

(€ thousands)		Change in discount rate	
Effect on net obligation as at 31.12.2017	Reduction of 10%	Increase of 10%	
Provision for environmental risks and charges	742	(791)	

## 22. PROVISIONS FOR EMPLOYEE BENEFITS

*Provisions for employee benefits*, which amount to €116,149 thousand as at 31 December 2017 (€120,648 thousand as at 31 December 2016) comprise the following:

(€ thousands)	31.12.2016	31.12.2017
Employment severance pay (TFR)	72,438	69,317
Supplemental healthcare provision for company executives of Eni (FISDE)	6,021	6,082
Gas Fund	35,039	33,292
Other provisions for employee benefits	7,150	7,458
	<b>120,648</b>	<b>116,149</b>

The provision for employee severance pay (TFR), governed by Article 2120 of the Italian Civil Code, represents the estimated liability determined on the basis of actuarial procedures for the amount to be paid to employees at the time that the employment is terminated. The principal amount of the benefit is equal to the sum of portions of the allocation calculated on compensation items paid during the employment and revalued until the time that such relationship is terminated. Due to the legislative changes introduced from 1 January 2007 for companies with more than 50 employees, a significant part of severance pay to be accrued is classified as a defined-contribution plan since the company's only obligation is to pay the contributions to the pension funds or to INPS. Liabilities related to severance pay pre-dating 1 January 2007 remain a defined-benefit plan to be valued using actuarial methods (€69,317 thousand as at 31 December 2017).

<sup>35</sup> For the purposes of sensitivity, only provisions for risks and charges showing a significant accretion discount were taken into account.

The supplementary healthcare provision (€6,082 thousand as at 31 December 2017) includes the estimate of costs (determined on an actuarial basis) related to contributions benefiting current<sup>36</sup> and retired executives.

FISDE provides financial supplementary healthcare benefits to Eni Group<sup>37</sup> executives and retired executives whose most recent contract of employment was as an executive with the Eni Group. FISDE is funded through the payment of: (i) contributions from member companies; (ii) contributions from individual members for themselves and their immediate family; and (iii) ad hoc contributions for specific benefits. The amount of the liability and the healthcare cost are determined on the basis, as an approximation of the estimated healthcare expenses paid by the fund, of the contributions paid by the company in favour of pensioners.

The Gas Fund (€33,292 thousand as at 31 December 2017) relates to the estimate, made on an actuarial basis, of the charges sustained by the employer due to the elimination, as of 1 December 2015, of the fund pursuant to Law 125 of 6 August 2015. In particular, Articles 9-decies and 9-undecies of the Law stipulate that the employer must cover: (i) an extraordinary contribution to cover expenses related to supplementary pension benefits in place at the time of the elimination of the Gas Fund for the years 2015 to 2020<sup>38</sup>; and (ii) a contribution in favour of those registered or in voluntary continuation of the contribution, that as at 30 November 2015 were not entitled to supplementary pension benefits from the eliminated Gas Fund, of 1% for each year of registration in the supplementary fund, multiplied by the social security tax base relating to the same supplementary fund for 2014, to be allocated through the employer or the supplementary pension scheme.

At present, the criteria, procedures and time periods for payment of the extraordinary contribution have not yet been announced. Employee selection of where the amounts would be allocated (supplementary pension scheme or to the employer) were concluded, pursuant to the law, on 14 February 2016.

The other employee benefit provisions (€7,458 thousand as at 31 December 2017) relate to seniority bonuses and the deferred cash incentive plan (IMD).

Deferred cash incentive plans are allocated to executives who have met the goals set out in the year preceding the allocation year, and allocate a basic incentive that is disbursed after three years and varies according to the performance achieved by the Company during the course of the three-year period following the time of the allocation. The benefit is provisioned when Italgas' commitment to the employee arises. The estimate is subject to revision in future periods, based on the final accounting and updates to profit forecasts (above or below target).

36 For executives in service, contributions are calculated from the year in which the employee retires and refer to the years of service provided.

37 The fund provides the same benefits for Italgas Group executives.

38 Article 9-*quinquiesdecies* also stipulates that "... If monitoring shows that the extraordinary contribution pursuant to Article 9-decies is insufficient to cover the relative expenses, a decree issued by the Ministry of Labour and Social Policy, in concert with the Ministry of Economic Development and the Ministry of Economy and Finance, provides for the redetermination of the extraordinary contribution, the criteria for redistribution of the contribution between employers and the time periods and procedures for payment of the extraordinary INPS contribution".

The long-term incentive plans, which replaced the preceding stock option allocations, involve the payment, three years after allocation, of a variable cash bonus tied to a measure of company performance. Obtaining the benefit depends on the achievement of certain future performance levels and is conditional on the beneficiary remaining with the Company for the three-year period following the allocation (the “vesting period”). This benefit is allocated pro rata over the three-year period depending on the final performance parameters.

Seniority bonuses are benefits paid upon reaching a minimum service period at the Company and are paid in kind.

Deferred cash incentive plans, long-term cash incentive plans and seniority bonuses are classified as other long-term benefits pursuant to IAS 19.

The composition of and changes in employee benefit provisions, determined by applying actuarial methods, are as follows<sup>39</sup>:

(€ thousands)	31.12.2016					31.12.2017				
	Employee severance pay	FISDE	Gas Fund (* )	Other provisions	Total	Employee severance pay	FISDE	Gas Fund (* )	Other provisions	Total
<b>Current value of the obligation at the start of the year</b>						<b>72,438</b>	<b>6,021</b>	<b>35,039</b>	<b>7,150</b>	<b>120,648</b>
Change in scope of consolidation	70,526	6,043	33,353	5,811	<b>115,733</b>	244				<b>244</b>
Current cost		71		1,532	<b>1,603</b>		129		2,722	<b>2,851</b>
Cost for past services			(623)		<b>(623)</b>					
Cost for interest		112	583	62	<b>757</b>	859	71	422	24	<b>1,376</b>
Revaluations / (Impairment):	1,810	(788)	1,113	7	<b>2,142</b>	(256)	97	794	268	<b>903</b>
- Actuarial (Gains) / Losses resulting from changes in the financial assumptions	2,378	275	1,145	296	<b>4,094</b>	(149)	86	(369)	(23)	<b>(455)</b>
- Effect of past experience	(568)	(1,063)	(32)	(289)	<b>(1,952)</b>	(107)	11	1,163	291	<b>1,358</b>
Paid benefits	(1,881)	(240)	(1,145)	(998)	<b>(4,264)</b>	(3,967)	(236)	(3,143)	(2,783)	<b>(10,129)</b>
Effect of transfers	1,983	823	1,758	736	<b>5,300</b>	(1)		180	77	<b>256</b>
<b>Current value of the obligation at the end of the year</b>	<b>72,438</b>	<b>6,021</b>	<b>35,039</b>	<b>7,150</b>	<b>120,648</b>	<b>69,317</b>	<b>6,082</b>	<b>33,292</b>	<b>7,458</b>	<b>116,149</b>

(\*) Concerns the measurement of the liabilities arising from: (i) the contribution in favour of those registered or in voluntary continuation of the contribution, equal to 1% for each year of registration in the Gas Fund multiplied by the social security tax base for 2014, (ii) the extraordinary contribution for expenses related to supplementary pension benefits in place at the time of the elimination of the Gas Fund for the years 2015 to 2020.

39 The table also provides a reconciliation of liabilities recorded for employee benefit provisions.

Costs for defined-benefit plans recognised under other components of comprehensive income are broken down in the following table:

(€ thousands)	31.12.2016					31.12.2017				
	Employee severance pay	FISDE	Gas Fund provisions	Other provisions	Total	Employee severance pay	FISDE	Gas Fund provisions	Other provisions	Total
Revaluations / (Impairment):										
- Actuarial (Gains) / Losses resulting from changes in the financial assumptions	2,378	275	1,145	296	<b>4,094</b>	(149)	86	(369)	(23)	<b>(455)</b>
- Effect of past experience	(568)	(1,063)	(32)	(289)	<b>(1,952)</b>	(107)	11	1,163	291	<b>1,358</b>
	<b>1,810</b>	<b>(788)</b>	<b>1,113</b>	<b>7</b>	<b>2,142</b>	<b>(256)</b>	<b>97</b>	<b>794</b>	<b>268</b>	<b>903</b>

The main actuarial assumptions used to determine liabilities at the end of the year and to calculate the cost for the following year are indicated in the table below:

	2016					2017				
	Employee severance pay	FISDE	Gas Fund	Other Employee provisions	Employee severance pay	FISDE	Gas Fund	Other provisions		
Discount rate (%)	1.20	1.20	1.20	N/A	1.40	1.40	1.40	N/A		
Inflation rate (%) (*)	1.20	1.20	N/A	N/A	1.50	1.50	N/A	N/A		

(\*) With reference to the other provisions, the rate refers only to the seniority bonuses.

The discount rate adopted was determined by considering the yields on corporate bonds issued by Eurozone companies with AA ratings.

The employee benefit plans recognised by Italgas are subject, in particular, to interest rate risk, in the sense that a change in the discount rate could result in a significant change in the liability.

The table below illustrates the effects of a reasonably possible<sup>40</sup> change in the discount rate at the end of the year.

The sensitivity of the discount rate represents the change in the value of the actuarial liability obtained using the end-of-year valuation data, changing the discount rate by a certain number of basis points, without any change in the other assumptions.

40 With regard to FISDE, any changes relating to mortality do not have a significant effect on the liability.

(€ thousands)	Discount rate	
Effect on net obligation as at 31.12.2017	0.5% reduction	0.5% increase
Employment severance pay	3,147	(3,421)
FISDE	473	(420)
Gas Fund (*)	937	(894)
Other provisions for employee benefits	68	(129)
	<b>4,625</b>	<b>(4,864)</b>

(\*) The amount includes the estimate of the 10% INPS solidarity contribution applied to the amounts to allocate to the supplementary pension.

The maturity profile of the obligations for employee benefit plans is shown in the following table:

(€ thousands)	31.12.2016					31.12.2017				
	Employee severance pay	FISDE	Gas Fund provisions (*)	Other provisions	Total Employee severance pay	Employee severance pay	FISDE	Gas Fund provisions (*)	Other provisions	Total
Within the next year	1,545	254	3,824	2,747	<b>8,370</b>	1,361	255	2,798	3,110	<b>7,524</b>
Within five years	9,505	932	14,502	4,037	<b>28,976</b>	12,316	932	11,900	3,890	<b>29,038</b>
Beyond five and up to ten years	28,182	954	13,265	366	<b>42,767</b>	27,743	949	12,467	330	<b>41,489</b>
Beyond ten years	33,206	3,881	3,448		<b>40,535</b>	27,897	3,946	6,127	128	<b>38,098</b>
	<b>72,438</b>	<b>6,021</b>	<b>35,039</b>	<b>7,150</b>	<b>20,648</b>	<b>69,317</b>	<b>6,082</b>	<b>33,292</b>	<b>7,458</b>	<b>116,149</b>

(\*) The amount includes the estimate of the 10% INPS solidarity contribution applied to the amounts to allocate to the supplementary pension.

The weighted average maturity of obligations for employee benefit plans is shown below:

2017				
	Employee severance indemnity	FISDE	Gas Fund	Other provisions
Weighted average maturity (years)	10	15	5	2



## 23. DEFERRED TAX LIABILITIES

Deferred tax liabilities of €94,790 thousand are stated net of offsettable prepaid tax assets of €206,062 thousand.

(€ thousands)

	1.6.2016	Change in scope of consolidation	Provisions	Uses	Other changes	31.12.2016
Deferred tax liabilities		329,731	311	(2,973)		<b>327,069</b>
Prepaid tax assets		(212,846)	(11,545)	3,598		<b>(220,793)</b>
		<b>116,885</b>	<b>(11,234)</b>	<b>625</b>		<b>106,276</b>

(€ thousands)

	31.12.2016	Change in scope of consolidation	Provisions	Uses	Other changes	31.12.2017
Deferred tax liabilities	327,069	8,198	712	(35,127)		<b>300,852</b>
Prepaid tax assets	(220,793)		(30,712)	45,443		<b>(206,062)</b>
	<b>106,276</b>	<b>8,198</b>	<b>(30,000)</b>	<b>10,316</b>		<b>94,790</b>

There are no prepaid tax assets which cannot be offset.

Deferred tax liabilities and prepaid tax assets break down as follows, based on the most significant temporary differences:

(€ thousands)	31.12.2016								
	Opening balance	Changes in scope of consolidation	Provisions	Uses	Impacts recorded in share-holders' equity	Other changes	Closing balance	of which: IRES	of which: IRAP
Deferred tax liabilities		329,731	311	(2,973)			327,069	297,589	29,480
Amortisation and depreciation exclusively for tax purposes		153,862	243	(3,832)			150,273	143,856	6,417
Revaluation of property, plant and equipment		122,065		9,491			131,556	111,962	19,594
Capital gains subject to deferred taxation		16,548		(15,793)			755	755	
Employee benefits		3,101		(175)			2,926	2,419	507
Capitalisation of financial expenses		3,342		(144)			3,198	2,722	476
Impairment losses on receivables in excess of tax deductibility		534		183			717	717	
Other temporary differences		30,279	68	7,297			37,644	35,158	2,486
Prepaid tax assets		(212,846)	(11,545)	3,598			(220,793)	(188,562)	(32,231)
Provision for risks and charges and other non-deductible provisions		(69,484)	(1,031)				(70,515)	(60,013)	(10,502)
Non-repayable and contractual grants		(72,521)	(4,547)				(77,068)	(65,590)	(11,478)
Non-deductible amortisation and depreciation		(56,576)		3,598			(52,978)	(45,076)	(7,902)
Employee benefits		(12,356)	(3,416)				(15,772)	(13,423)	(2,349)
Other temporary differences		(1,909)	(2,551)				(4,460)	(4,460)	
Net deferred tax liabilities		116,885	(11,234)	625			106,276	109,027	(2,751)

(€ thousands)

31.12.2017

	Opening balance	Changes in scope of consolidation	Provisions	Uses	Impacts recorded in share- holders' equity	Other changes	Closing balance	of which: IRES	of which: IRAP
<b>Deferred tax liabilities</b>	<b>327,069</b>	<b>8,198</b>	<b>712</b>	<b>(35,127)</b>			<b>300,852</b>	<b>256,216</b>	<b>44,636</b>
Amortisation and depreciation exclusively for tax purposes	150,273	8,198	115	(4,160)			154,426	131,427	22,999
Revaluation of property, plant and equipment	131,556			(7,232)			124,324	105,808	18,516
Capital gains subject to deferred taxation	755		597	(791)			561	561	
Employee benefits	2,926			(550)			2,376	2,022	354
Capitalisation of financial expense	3,198			(338)			2,860	2,434	426
Impairment losses on receivables in excess of tax deductibility	717			(130)			587	587	
Other temporary differences	37,644			(21,926)			15,718	13,377	2,341
<b>Prepaid tax assets</b>	<b>(220,793)</b>	<b>.</b>	<b>(30,712)</b>	<b>45,443</b>			<b>(206,062)</b>	<b>(175,373)</b>	<b>(30,689)</b>
Provision for risks and charges and other non-deductible provisions	(70,515)		(5,700)	27,204			(49,011)	(41,712)	(7,299)
Non-repayable and contractual grants	(77,068)			8,359			(68,709)	(58,476)	(10,233)
Non-deductible amortisation and depreciation	(52,978)		(18,113)	7,802			(63,289)	(53,851)	(9,438)
Employee benefits	(15,772)		(6,101)	577			(21,296)	(18,124)	(3,172)
Other temporary differences	(4,460)		(798)	1,501			(3,757)	(3,210)	(547)
<b>Net deferred tax liabilities</b>	<b>106,276</b>	<b>8,198</b>	<b>(30,000)</b>	<b>10,316</b>			<b>94,790</b>	<b>80,843</b>	<b>13,947</b>

Prepaid tax assets and deferred tax liabilities are considered to be long term.

The note "Income taxes" provides information about taxes for the year.

## 24. SHAREHOLDERS' EQUITY

*Shareholders' equity*, which amounts to €1,185,640 thousand as at 31 December 2017 (€1,064,294 thousand as at 31 December 2016) breaks down as follows:

(€ thousands)	31.12.2016	31.12.2017
<b>Shareholders' equity attributable to Italgas</b>	<b>1,063,406</b>	<b>1,185,640</b>
Share capital	1,001,232	1,001,232
Legal reserve	192,236	200,246
Share premium reserve	620,130	620,130
Consolidation reserve	(316,385)	(323,907)
Reserve for business combinations under common control	(349,854)	(349,854)
Other reserves		(169,413)
Retained earnings		(72,209)
Reserve for recalculation of defined-benefit plans for employees	(11,744)	(13,351)
Net profit (loss)	(72,209)	292,766
<i>to be deducted</i>		
- Treasury shares		
<b>Shareholders' equity attributable to minority interests</b>	<b>888</b>	
Napoletanagas	888	
	<b>1,064,294</b>	<b>1,185,640</b>

### SHARE CAPITAL

The share capital as at 31 December 2017 consisted of 809,135,502 shares with no indication of par value, with a total value of €1,001,231,518.

### LEGAL RESERVE

The legal reserve stood at €200,246 thousand as at 31 December 2017. The €8,010 thousand increase compared to 31 December 2016 came about after allocating the 2016 profit of Italgas S.p.A. resolved by the Shareholders' Meeting on 28 April 2017.

### SHARE PREMIUM RESERVE

The share premium reserve stood at €620,130 thousand as at 31 December 2017 (unchanged compared to 31 December 2016).

### CONSOLIDATION RESERVE

The consolidation reserve (-€323,907 thousand) compared to 31 December 2016 shows a €7,522 thousand change following a price adjustment of the value of the equity investment in Italgas Reti. This adjustment is due to the fact that as part of the Snam separation in 2016,

Italgas Reti S.p.A. retained rights and obligations relating to the Rome Ostiense real estate complex deriving from specific contractual agreements within the context of the transfer of the entire share capital of Italgas Reti S.p.A. from Eni to Snam in 2009. The rights and obligations regarding the price adjustment of the equity investment in Italgas Reti were transferred from Snam S.p.A. to Italgas S.p.A.

#### OTHER RESERVES

Other reserves mainly relate to the reserve for business combination under common control, amounting to -€349,838 thousand, recorded following the acquisition by Snam S.p.A. of 38.87% of the stake in Italgas Reti S.p.A.

#### RESERVE FOR RECALCULATION OF DEFINED-BENEFIT PLANS FOR EMPLOYEES

As at 31 December 2017, the reserve for recalculation of employee benefit plans (-€13,351 thousand) included actuarial losses, net of the relative tax effect, recognised under other components of comprehensive income pursuant to IAS 19.

The changes in the reserve during the course of the year are shown below:

(€ thousands)

	Gross reserve	Tax effect	Net reserve
<b>Reserve as at 1 January 2016</b>			
Changes in scope of consolidation	(20,834)	5,875	(14,959)
Changes of the year 2016	3,696	(1,042)	2,654
<b>Reserve as at 31 December 2016</b>	<b>(17,138)</b>	<b>4,833</b>	<b>(12,305)</b>
Changes of the year 2017	(1,457)	411	(1,046)
<b>Reserve as at 31 December 2017</b>	<b>(18,595)</b>	<b>5,244</b>	<b>(13,351)</b>

#### TREASURY SHARES

As at 31 December 2017 Italgas did not have any treasury shares in its portfolio.

#### DIVIDENDS

In its meeting of 12 March 2018, the Board of Directors proposed to the Shareholders' Meeting convened for 19 April 2018 the distribution of an ordinary dividend of €0.208 per share. The dividend will be paid out as of 23 May 2018, with an ex-coupon date of 21 May 2018 and a record date of 22 May 2018.

**MINORITY INTERESTS**

Net profit and shareholders' equity attributable to minority interests relate to the following consolidated entities:

(€ thousands)

	Shareholders' equity attributable to minority interests 31.12.2016	Shareholders' equity attributable to minority interests 31.12.2017	Net income attributable to minority interests 31.12.2016	Net income attributable to minority interests 31.12.2017
Napoletanagas	888		90	

**Comparison of net income and shareholders' equity between Italgas S.p.A. and those consolidated**

(€ thousands)

	Profit for the Shareholders' year equity	
<b>Financial Statements of Italgas S.p.A.</b>	<b>174,152</b>	<b>1,653,160</b>
Profit for the year of the Companies included in the scope of consolidation	316,375	
Difference between carrying amount of the equity investments in the consolidated companies and shareholders' equity of the financial statements, including net income		(502,826)
<b>Adjustments made during consolidation for:</b>		
Dividends net of tax effect	(195,047)	
Income from valuation of equity investments using equity method and other income from investments	9,153	30,036
Other consolidation adjustments net of tax effect	(11,867)	5,270
	<b>118,614</b>	<b>(467,520)</b>
<b>Consolidated Financial Statements</b>	<b>292,766</b>	<b>1,185,640</b>

## 25. GUARANTEES, COMMITMENTS AND RISKS

*Guarantees, commitments and risks*, amounting to €823,306 thousand as at 31 December 2017 comprise:

(€ thousands)	31.12.2016	31.12.2017
<b>Guarantees given in the interest:</b>	<b>96,475</b>	<b>105,455</b>
- of subsidiaries	96,475	105,455
<b>Financial commitments and risks:</b>	<b>545,263</b>	<b>717,851</b>
<b>Commitments</b>	<b>503,546</b>	<b>676,163</b>
Commitments for the purchase of goods and services	494,601	583,601
Other	8,945	92,562
<b>Risks</b>	<b>41,717</b>	<b>41,688</b>
- for compensation and litigation	41,717	41,688
	<b>641,738</b>	<b>823,306</b>

### GUARANTEES

Guarantees of €105,455 thousand refer mainly to guarantees issued, holding harmless Snam S.p.A. (€86,088 thousand), holding harmless Italgas S.p.A. (€16,111 thousand) with regard to sureties and other guarantees issued in the favour of subsidiaries.

### COMMITMENTS

At 31 December 2017, commitments with suppliers to purchase property, plant and equipment and provide services relating to investments in property, plant and equipment and intangible assets under construction totalled €583,601 thousand.

The other commitments regard mainly commitments for acquisitions of investments, concessions and business units, and are explained in the following table:

(€ million)	
AEnergia Reti (municipality of Portopalo di Capo Passero - Siracusa)	2.2
Hera (acquisition of the company Medea)	24.1
CPL Concordia (acquisition of Ichnusa Gas)	26.2
CPL Concordia (7 concessions in Southern Italy)	13.0
Amalfitana Gas (gas distribution business unit)	18.5
	<b>84.0</b>



Furthermore, purchase of the equity investment of Enerco Distribuzione from the subsidiary Italgas Reti during the year is subject to an ownership price adjustment (earn-out) clause.

The purchase of 51% of the share capital of ACAM Gas S.p.A. from the subsidiary Italgas Reti in 2015 comprise mutual commitments of the parties with regard to the first public tender for the concession of Atem of La Spezia.

Other commitments also include minimum future payments concerning non-voidable operating lease transactions (€8,562 thousand, of which €1,823 thousand falling due within the next year and €6,739 thousand between one and five years).

### RISKS

Risks concerning compensation and litigation (€41,688 thousand) relate to possible (but not probable) claims for compensation arising from ongoing litigation, with a low probability that the pertinent economic risk will arise.

## FINANCIAL RISK MANAGEMENT

### INTRODUCTION

Italgas has established the Enterprise Risk Management (ERM) unit, which reports directly to the General Manager of Finance and Services and oversees the integrated process of managing corporate risk for all Group companies. The main objectives of the ERM are to define a homogeneous and transversal risk assessment model, to identify priority risks and to guarantee the consolidation of mitigation actions and the development of a reporting system.

The ERM methodology adopted by the Italgas Group is in line with the reference models and existing international best practices (COSO Framework and ISO 31000).

The ERM unit operates as part of the wider Internal Control and Risk Management System of Italgas.

The main corporate financial risks identified, monitored and, where specified below, managed by Italgas are as follows:

- risk arising from exposure to fluctuations in interest rates;
- credit risk arising from the possibility of counterparty default;
- liquidity risk arising from not having sufficient funds to meet short-term financial commitments;
- rating risk;
- debt covenant and default risk.

There follows a description of Italgas' policies and principles for the management and control of the risks arising from the financial instruments listed above. In accordance with IFRS 7 - "Financial instruments: Additional information", there are also descriptions of the nature and size of the risks resulting from such instruments.

Information on other risks affecting the business (operational risk and risks specific to the segment in which Italgas operates) can be found in the "Elements of risk management

and uncertainty” section of the Directors’ Report.

## INTEREST RATE RISK

Fluctuations in interest rates affect the market value of Italgas’ financial assets and liabilities and its net financial expense. The Italgas Group has adopted a centralised organisational model. In accordance with this model, Italgas’ various departments access the financial markets and use funds to cover financial requirements, in compliance with approved objectives, ensuring that the risk profile stays within the defined limits.

As at 31 December 2017 the financial debt at floating rate was 28.8% and at fixed rate was 71.2%.

As at the same date the Italgas Group used external financial resources in the following forms: Bonds subscribed by institutional investors, bilateral and syndicated loans with banks and other financial institutions, in the form of medium-to-long-term loans and bank credit lines at interest rates indexed to benchmark market rates, in particular the Europe Interbank Offered Rate (Euribor).

Therefore, an increase in interest rates, not implemented – in full or in part – in the regulatory WACC, could have negative effects on the assets and on the economic and financial situation of the Italgas Group.

At full performance, Italgas aims to maintain a debt ratio between a fixed rate and variable rate to minimise the risk of rising interest rates, with a goal being a fixed-rate and variable-rate debt composition of approximately 2/3 for fixed-rate and 1/3 for variable-rate. To this regard, in 2017 the Company issued bond loans for a total of €2,650 million with the following characteristics: (i) €1,500 million, issued

on 19 January 2017 and divided into two tranches, the first with a term of 5 years and the second of 10 years, both at a fixed rate, amounting to €750 million each and an annual coupon of 0.50% and 1.625%, respectively; (ii) €650 million issued on 14 March 2017, maturing on 14 March 2024 with a fixed rate annual coupon of 1.125%; (iii) €500 million issued on 18 September 2017, maturing on 18 January 2029 with a fixed rate annual coupon of 1.625%.

## CREDIT RISK

Credit risk is the Company’s exposure to potential losses arising from counterparties failing to fulfil their obligations. Default or delayed payment of amounts owed may have a negative impact on the financial results and financial situation of Italgas.

For the risk of non-compliance by the counterparty concerning contracts of a commercial nature, the credit management for credit recovery and any possible disputes is handled by the business units and the centralised Italgas departments.

The rules for customer access to the gas distribution service are established by the Authority and set out in the Network Codes, namely, in documents that establish, for each type of service, the rules regulating the rights and obligations of the parties involved in the process of providing said services and contain contractual conditions that reduce the risk of non-compliance by customers, such as the provision of bank or insurance guarantees on first request.

As previously analysed under the section “Trade receivables and other receivables”, to which the reader is referred for detailed information, the receivables past due and not impaired as at 31 December 2017 amount to €12,677 thousand (€28,632 thousand as at 31 December 2016).

As at 31 December 2017 there were no significant credit risks. It should be noted, however, that around 96% of trade receivables refer to extremely reliable clients, including Eni, which represents 42% of the total trade receivables.

It cannot be ruled out, however, that the Company could incur liabilities and/or losses due to its customers' failure to fulfil their payment obligations.

## **LIQUIDITY RISK**

Liquidity risk is the risk that new financial resources may not be available (funding liquidity risk) or that the company may be unable to convert assets into cash on the market (asset liquidity risk), meaning that it cannot meet its payment commitments. This may affect profit or loss should the company incur extra costs to meet its commitments or, in extreme cases, lead to insolvency and threaten the company's future as a going concern.

In order to mitigate this risk and to maintain a level of liquidity consistent with maintaining the requirements of its rating, Italgas signed finance agreements unused as at 31 December 2017. These credit lines (€ 1.1 billion) may be used to address possible liquidity needs, where necessary, if the actual borrowing requirement is higher than estimated. Also note that at the same date, in addition to the funding from the banking system, the Euro Medium Term Notes (EMTN) programme, approved by the Italgas Board of Directors on 23 October 2017, has allowed issue of the remaining bonds worth €850 million to be placed with institutional investors.

Italgas aims, in financial terms, at establishing a financial structure that, in line with its business objectives, ensures a level adequate for the group in terms of the duration and composition of the debt. The achievement of this financial structure will take place through the monitoring of certain key parameters, such as the ratio between debt and the RAB, the ratio between short-term and medium-/long-term debt, the ratio between fixed rate and floating rate debt and the ratio between bank credit granted and bank credit used.

## **RATING RISK**

With reference to the long-term debt of Italgas, respectively on 4 August and 12 October 2017, Fitch and Moody's assigned Italgas S.p.A. confirmed the rating assigned to Italgas S.p.A. (BBB+ with stable outlook stabile and Baa1 with negative outlook).

Based on the methodologies adopted by the rating agencies, a downgrade of one notch in the Italian Republic's current rating could trigger a downward adjustment in Italgas' current rating.

## **DEBT COVENANT AND DEFAULT RISK**

As at 31 December 2017, there were no financial covenants and unsecured bilateral and syndicated loan agreements in place with banks and other financial institutions. Some

of these contracts provide, inter alia, for the following: (i) negative pledge commitments pursuant to which Italgas and its subsidiaries are subject to limitations on pledging real property rights or other restrictions on all or part of the respective assets, shares or merchandise; (ii) pari passu and change-of-control clauses; and (iii) limitations on certain extraordinary transactions that the Company and its subsidiaries may carry out.

The bonds issued by Italgas as at 31 December 2017 as part of the Euro Medium Term Notes programme provide for compliance with covenants that reflect international market practices regarding, inter alia, negative pledge and pari passu clauses.

Failure to comply with the commitments established for these loans - in some cases only when this non-compliance is not remedied within a set time period - and the occurrence of other events, such as cross-default events, some of which are subject to specific threshold values, may result in Italgas' failure to comply and could trigger the early repayment of the relative loan.

With reference to the EIB, the relative contracts contain a clause whereby, in the event of a significant reduction in EBITDA resulting from the loss of concessions, there is a disclosure obligation to the EIB and a subsequent consultation period, after which the early repayment of the loan may be required.

## ENVIRONMENTAL REGULATIONS

With respect to environmental risk, while the Company believes that it operates in substantial compliance with the laws and regulations and considering the adjustments to environmental regulations and actions already taken, it cannot be ruled out that the Company may incur costs or liabilities, which could be significant.

It is difficult to foresee the repercussions of any environmental damage, partly due to new laws or regulations that may be introduced for environmental protection, the impact of any new technologies for environmental clean-ups, possible litigation and the difficulty in determining the possible consequences, also with respect to other parties' liability and any possible insurance compensation.

## FUTURE PAYMENTS FOR FINANCIAL LIABILITIES, TRADE AND OTHER PAYABLES

The table below shows the repayment plan contractually established in relation to the financial payables, including interest payments not discounted:

(€ thousands)		Due date							
	Balance as at 31.12.2016	Balance as at 31.12.2017	Portion with due date within 12 months	Portion with due date beyond 12 months	2019	2020	2021	2022	Beyond
<b>Financial liabilities</b>									
Bank loans	3,619,043	989,138		989,138	200,000		33,267	33,267	722,604
Bonds		2,650,000		2,650,000				750,000	1,900,000
Short-term liabilities		81,133	81,133						
Interest on loans			33,751	296,293	34,226	35,330	34,571	37,255	154,911
	<b>3,619,043</b>	<b>3,720,271</b>	<b>114,884</b>	<b>3,935,431</b>	<b>234,226</b>	<b>35,330</b>	<b>67,838</b>	<b>70,522</b>	<b>2,777,515</b>

With reference to the payment times with regard to trade and other payables, refer to the note "Short-term financial liabilities, long-term financial liabilities and short-term portions of long-term liabilities" in the consolidated financial statements.

## OTHER INFORMATION ON FINANCIAL INSTRUMENTS

With reference to the categories provided for by IAS 39 "Financial Instruments: recording and assessment", note that the financial assets and liabilities of Italgas fall entirely into the financial instruments category, assessed using the amortised cost method.

The book value of financial instruments and their relative effects on results and on equity can be analysed as follows:

(€ thousands)		Book value		Income / expense recognised to income Statement		Income / expense recognised to shareholders' equity (a)	
		Balance as at 31.12.2016	Balance as at 31.12.2017	Balance as at 31.12.2016	Balance as at 31.12.2017	Balance as at 31.12.2016	Balance as at 31.12.2017
<b>Financial instruments measured at amortised cost</b>							
- Long-term financial payables (b)		923,005	3,617,044	123,974	36,089		

(a) Net of tax effect.

(b) The effect in the income statement are recognised in the item "Financial income (expense)"

The table below provides a comparison between the book value of financial assets and liabilities and their respective fair value.

(€ thousands)

	Balance as at 31.12.2016		Balance as at 31.12.2017	
Financial instruments measured at amortised cost	Book value	Market value	Book value	Market value
- Long-term financial payables	923,005	923,005	3,617,044	3,689,670

The book value of trade, other receivables and financial payables is close to the related fair value measurement, given the short period of time between when the receivable or the financial payable arises and its due date.

## MARKET VALUE OF FINANCIAL INSTRUMENTS

Below is the classification of financial assets and liabilities measured at fair value in the Statement of Financial Position in accordance with the fair value hierarchy defined on the basis of the significance of the inputs used in the measurement process. More specifically, in accordance with the characteristics of the inputs used for measurement, the fair value hierarchy comprises the following levels:

- a) level 1: listed prices (unadjusted) on active markets for identical financial assets or liabilities;
- b) level 2: measurements made on the basis of inputs differing from the quoted prices referred to in the previous point, which, for the assets/liabilities submitted for measurement, are directly (prices) or indirectly (price derivatives) observable;
- c) level 3: inputs not based on observable market data.

The company does not hold financial instruments measured at fair value as at 31 December 2017.

## DISPUTES AND OTHER MEASURES

Italgas is involved in civil, administrative and criminal cases and legal actions related to its normal business activities. According to the information currently available and considering the existing risks, Italgas believes that these proceedings and actions will not have material adverse effects on its consolidated financial statements.

The following is a summary of the most significant proceedings; unless indicated otherwise, no allocation has been made for the litigation described below because the Company believes it improbable that these proceedings will have an unfavourable outcome or because the amount of the allocation cannot be reliably estimated.

## CRIMINAL CASES

### **Italgas Reti S.p.A. - Barletta event**

On 25 April 2015, an explosion occurred due to a gas leak. The event, which happened during an operation following the report of damage to the gas network, killed one Italgas Reti worker and injured others. The local Public Prosecutor's office closed the preliminary investigations and the press reported that two employees of the third-party companies involved in the accident allegedly requested plea bargaining, while another two were allegedly committed for trial.

### **Italgas Reti S.p.A. - Rome/Via Parlatore event**

The public prosecutor at the Court of Rome opened an investigation in relation to the incident that took place on 7 September 2015 during an ordinary intervention in the gas distribution network in the municipality of Rome.

The incident, which took place due to causes that are still being investigated, caused a fire that involved three people. Two of them, workers for an Italgas Reti contractor, suffered mild injuries. The third person – an Italgas Reti employee – died after a few weeks despite medical treatment.

The Public Prosecutor's office of Rome requested that all persons under investigation be dismissed. The trial bundle has not yet been assigned to the examining judge for the ruling.

### **Italgas Reti S.p.A. - Cerro Maggiore/Via Risorgimento event**

The public prosecutor at the Court of Busto Arsizio opened criminal proceedings against Italgas Reti executives, technicians and manual workers in relation to an incident that took place on 11 November 2015 during an emergency intervention. The incident was caused by a gas leak due to remote

controlled horizontal drilling work for the placement of fibre-optic cables performed by a third party.

The explosion occurred while interception activities were being completed on the section involved in the damage, causing the collapse of a house at No. 39 and the death of the woman who lived there, a serious injury to an Italgas Reti employee and to two other people who suffered mild injuries. The area was closed off. On 15 November 2015, the Busto Arsizio public prosecutor served a one-time notice of technical investigation, and the public prosecutor appointed its own technical consultants, who filed their report on 22 April 2016.

Italgas Reti also appointed its own technical consultants.

A notice was served on 24 April 2017 advising of the conclusion of the preliminary investigations pursuant to Article 415-bis of the Code of Criminal Procedure of the persons under investigation and Italgas Reti, with regard to which it was alleged the occupational safety prevention measures had failed to be adopted. The company will organise the most appropriate defence to ensure it is extricated from this situation.

### **Italgas Reti S.p.A. - Rome/Via Magnaghi event**

On 25 October 2016, while a meter was being replaced by employees of an Italgas Reti contractor, there was a fire which involved two workers as well as the owner of the property. The three people suffered injuries of varying degrees.

The Public Prosecutor launched investigations with regard to unknown persons and the Company is actively cooperating.

### **Actions promoted by Italgas Reti following the Judicial Administration phase**

Following the appeal brought by Italgas



Reti, on 25 July 2016 the Palermo Court of Appeal issued a Decree revoking the Judicial Control measure with regard to Italgas Reti, declaring the implementation of the consequent provisions terminated. The Public Prosecutor did not propose an appeal under the terms of the law at the Court of Cassation; therefore, the ruling became definitive.

Italgas Reti, through an appeal filed on 24 October 2016, opposed the settlement order of the expert witnesses of the Court of Palermo, challenging its non-involvement and, alternatively, the excess compensation paid.

On 16 January 2017 Italgas Reti filed at the Court of Palermo:

- a note challenging the statement submitted by the Judicial Administrators, highlighting the irregularities and incompleteness of the documentation;
- a motion requesting the repayment of all costs incurred for payments and refunds with regard to the Judicial Administrators and their assistants and consultants.

In the proceedings concerning the contesting of the report of the Judicial Administrators, following the hearing for discussion on 28 September 2017, the Court set aside the ruling.

***Autorità di Regolazione per Energia Reti e Ambiente (ARERA), formerly Autorità per l'Energia Elettrica, il Gas e il Sistema Idrico (AEEGSI).***

#### **Italgas Reti S.p.A. - Gas distribution service quality violations**

Through resolution 33/2012/S/gas of 9 February 2012, ARERA arranged the launch of four disciplinary proceedings for the issuance of monetary fines with regard to gas distribution service quality to establish the violation of Articles 2, paragraphs 1 and 12, paragraph 7, letter b) of the ARG/

gas 120/08 resolution by four natural gas distribution companies including Italgas Reti.

In particular, ARERA claims that, with regard to its Venice plant, the company failed to comply with the obligation to recondition or replace, by 31 December 2010, at least 50% of the cast-iron pipes with hemp- and lead-sealed joints in operation as at 31 December 2003, set out in the aforementioned Article 12, paragraph 7, letter b).

On 25 March 2016, ARERA announced the findings of the preliminary investigation. After the proceeding, with Resolution no. 195/2017/S/Gas of 30 March 2017, as adjusted by Resolution no. 232/2017/S/Gas of 6 April 2017, ARERA imposed an administrative fine of €204,000.00 on Italgas Reti for the violation of Article 12, paragraph 7, letter b) of the Gas Distribution and Metering Service Quality Regulation ("RQDG"). Irrespective of all considerations concerning the Company's actual liability with regard to the alleged conduct, it seems that the extent of the penalty can be challenged on the grounds that it is disproportionate with respect to the actual conduct of Italgas Reti, also in light of a penalty, of a significantly lower amount, imposed in different proceedings regarding the same circumstances relating to the year 2008. The Company decided to challenge the above-mentioned rulings before the Lombardy Regional Administrative Court and the relative appeal was served on 29 May 2017. The date of the hearing is still to be set.

#### **Italgas Reti S.p.A. - Gas distribution service violations relating to the billing of the "municipal fees" tariff component**

By means of Resolution 104/2015/S/gas of 12 March 2015, ARERA began enforcement proceedings for violations relating to the billing of the "COLci" component.

The Authority specifically alleges that the

billing procedures for this component stipulated under current regulations have not been complied with.

The duration of the investigation has been set at 180 days, while the deadline for the adoption of the provision is 90 days from the closing date of the investigation.

On 23 April 2015, ARERA requested the transmission of billing data for the COLci tariff component for the years 2009-2013, which the company provided on 7 May 2015. To date, the preliminary investigation has not been concluded.

#### **Italgas Reti S.p.A. - Violations relating to Energy Efficiency Certificates**

With decision DSAI/13/2018/EFR of 7 February 2018, the Authority opened enforcement proceedings against Italgas Reti S.p.A. to ascertain violation of Art. 13, paragraph 3 of Italian Ministerial Decree of 28 December 2012 on the subject of Energy Efficiency Certificates for 2016.

More specifically, Art. 13 of Italian Ministerial Decree of 28 December 2012 establishes that:

- starting from 2014, the obligated entities send GSE the white certificates regarding the previous year by 31 May of each year;
- GSE checks that each obligated entity has certificates corresponding to the annual obligation assigned to them;
- for the years 2015 and 2016, if the obligated entity attains an obligated quota of its responsibility lower than 100%, but however equal to or higher than the minimum quota of 60%, it may offset the remaining quota during the following two years without incurring penalties;
- the Authority applies penalties for each missing certificate to the obligated entities that attain percentages lower than the target assigned to them.

The note of GSE dated 17 August 2017 that was sent to the Authority states that Italgas Reti sent 453,030 Energy Efficiency Certificates (out of a total of 1,083,345), equal to about 41.82% of its specific target for the year 2016, therefore being partially in default (by 18.18% of the 2016 target, equal to 196,977 EECs) compared to the minimum required quota of 60% for that year.

In initiating the proceedings, the Authority also established that:

- the deadline of the preliminary investigation is 120 days starting from notification of the resolution;
- the deadline for adopting the final measure is 100 days starting from the deadline of the preliminary investigation;
- the entities that are entitled to take part in the proceedings may submit a request to access the documents.

The potential liability connected with these proceedings was considered in setting up the provisions for risks and charges.

## ADMINISTRATIVE DISPUTE

### **Italgas Reti S.p.A. - Municipality of Venice - Council of State (Gen. Reg. 8060/2017)**

Italgas Reti appealed against the acts through which the Municipality of Venice had deducted from the refund due to Italgas Reti as the outgoing operator, the value (for Italgas amounting to €31,000,000) of a portion of the distribution network (Block A), over which the Municipality of Venice claims that it acquired - through a free transfer - ownership at the end of the original concession deed (2010). However, according to Italgas Reti, the expiry of the concession and therefore the accrual of entitlement to the free transfer was postponed to 2025 on the basis of subsequent amendments to the original concession deed, signed by the parties in 1995. With its Ruling no. 654/2017, the Veneto Regional Administrative Court rejected the Company's appeal on the grounds that entitlement to the free transfer of part of the distribution network was accrued when the concession relationship originally expired (2010). Italgas Reti appealed against the ruling before the Council of State, which set the hearing for oral arguments for 29 March 2018. As a result of Ruling no. 654/2017, the Municipality of Venice asked Italgas Reti to pay a fee, whose amount is still to be determined, in connection with use of the plants freely transferred with its letter dated 2 February 2018. Italgas Reti challenged this request with appeal before the Veneto Regional Administrative Court. The date of the hearing is still to be set.

### **Italian Antitrust Authority (AGCM)**

With its ruling of 5 December 2017, the Italian Antitrust Authority resolved to start proceedings IP 288 against Eni gas e luce S.p.A. due to failure to comply with the Italian Antitrust Authority measure of 11 May 2016 for assessment of unfair trade practices initiated at least from March 2014, consisted of inadequate management of end customer claims regarding the invoicing and delayed repayment of amounts due to the end customers for various reasons. As part of proceedings IP 288, on 14 and 15 December 2017 the Italian Antitrust Authority inspected the premises of Italgas Reti to collect documents helpful in the preliminary investigations of Eni gas e luce S.p.A., taking into account that Italgas Reti is one of the major companies operating in the distribution of gas and carries on metering and self-reading validation activities. Italgas Reti is therefore unrelated to proceedings IP 288.

## TAX CASES

### **Italgas Reti S.p.A. - Direct taxes**

The 2009 general tax audit performed by the Revenue Agency, which ended on 7 December 2012 with the release of the official audit report, resulted in around €1 million of additional IRES, IRAP and VAT, plus penalties and interest.

The Company, as regards the assessment notice concerning IRES, on 28 May 2015 appealed to the Provincial Tax Commission of Turin, challenging only the findings relating to the undue deduction of taxes on foreign regularisations and other unrelated taxes; this appeal was accepted with the ruling of 23 June 2016. The Revenue Agency appealed against the ruling. The Company is waiting for convocation of the hearing at the Regional Tax Commission of Turin.

As for the other findings, not challenged by the Company, in July 2017 it agreed to the facilitated settlement of the pending charges that allowed it to settle the debt by paying a total of €558,131 without paying the inflicted penalties. The risk fund was used to make this payment.

On 12 December 2016, a notice of investigation was served relating to greater IRES and IRAP, plus penalties and interest, totalling €240,600 as a result of the findings of the Audit Report of 17 November 2014 ending the general tax inspection that the Revenue Agency had conducted into the incorporated company AES Torino S.p.A., for the 2011 tax period. With regard to the risks associated with the proceedings in question, an allocation of €90,251 has been set aside.

On 10 May 2017, the settlement of the notice of investigation was concluded, with the signing of the report, followed on 25 May 2017 by payment of the sums in question, €43,968. At the same time the risk fund was also used for the part of the excess resulting provision equal to €46,283, as a result of the payment by Iren S.p.A. of the share pertaining to the stake held by it in AES Torino in the 2011 tax period.

The case in question is therefore settled.

An assessment notice was served by the Turin Guardia di Finanza on 3 May 2017, which, with regard to the 2014 tax period, challenged the wrongful deduction of €704,000 in VAT.

In light of the challenge, an amount equivalent to the VAT and related penalties to the risk provision calculated was allocated, in the event of a tax settlement plus interest due, at a total of €1,050,966.

The Revenue Agency has not yet issued its findings, but served an order to file an appearance and official debate began for facilitated settlement of the dispute.

#### **Italgas Reti S.p.A. - Local duties**

On 29 December 2016 Italgas Reti was notified by AMA, on behalf of the Municipality of Rome, of waste tariff assessment notices for the period from

1 January 2011 to 31 December 2013 and waste tax assessment notices for the period from 1 January 2014 to 30 June 2016 in relation to the properties owned by the Company at 47/53 Via Giuseppe Guicciardi. An allocation to the risk provision, equal to €1,572,117, corresponding to the Tariff/Tax calculation, the reduced penalties (if there is a settlement concession) and the relevant interest, was made due to this assessment. If there is no response soon from the tax authorities surrounding the request submitted by the Company to re-examine the notices, an appeal will be submitted to the Rome Provincial Tax Commission

In September 2017, the Company submitted a request to settle the tax dispute (pursuant to Italian Decree Law no. 51/2017 and Resolution no. 45/2017 of the Municipality of Rome) by paying the total sum of €791,117 with concomitant use of the risk fund and reversal of the excess amount of €781,000.

#### **Italgas Reti S.p.A. (formerly Napoletanagas S.p.A incorporated) - Local duties**

The tax risk provision involves:

- 14 assessment notices, relating to waste disposal tax in the Municipality of Caserta, served in 2013 to 2016 and being challenged by the Company at the competent tax commissions. Following the favourable rulings accepting repeals, in 2017 reversals for €226,757 regarding the portion of the surplus provision were made;
- the amount of €72,405, referring to the assessment notice received in 2016 in relation to the recovery of waste disposal tax for the years 2010, 2011 and 2012 for the premises at 66/f Via Galileo Ferraris in Naples. The notice was challenged before the Naples Provincial Tax Commission and the appeal was declared inadmissible on 11 May 2017. In September 2017, the Company submitted a request to settle the tax dispute (pursuant to Italian Decree Law

no. 51/2017 and Resolution no. 67/2017 of the Municipality of Naples) by paying the total sum of €42,340 with concomitant use of the risk fund and reversal of the excess amount of €30,065;

- the amount of €185,464 relates to two notices received in 2016 for assessment of the waste disposal tax for the years 2010, 2011 and 2012, relating to the premises in Naples at Via Brin and Via Leopardi. After the facilitated settlement, €162,738 was paid in 2017 with consequent use of the provision and reversal of the €22,726 surplus.

The accounting items of the 2017 Consolidated Income Statement are compared with the figures of the consolidated financial statements as at 31 December 2016 represented by Italgas S.p.A. starting from the date of incorporation (1 June 2016) and its subsidiaries from the date of acquiring control over them (7 November 2016). The data are therefore not comparable.

## 26. REVENUE

The breakdown of revenue for the period, which totalled €1,621,041 thousand, is shown in the following table:

(€ thousands)	Jun-Dec 2016	2017
Core business revenue	247,672	1,570,929
Other revenue and income	26,050	50,112
	<b>273,722</b>	<b>1,621,041</b>

Group revenue is earned exclusively in Italy. The details are provided below.

### CORE BUSINESS REVENUE

Core business revenue, which amounts to €1,570,929 thousand, is analysed in the table below:

(€ thousands)	Jun-Dec 2016	2017
Natural gas distribution	177,049	1,044,966
Revenue for infrastructure construction and improvements (IFRIC 12)	61,712	479,651
Technical assistance, engineering, IT and other services	5,159	39,779
Water distribution and sale	3,752	6,533
	<b>247,672</b>	<b>1,570,929</b>

Core business revenue refers primarily to the consideration for the natural gas transmission service (€1,044,966 thousand) and revenue deriving from the construction and upgrading of natural gas distribution infrastructure connected with concession agreements pursuant to IFRIC 12 (€479,651 thousand).

Core business revenue is reported net of the following items, involving tariff components, in addition to the tariff, applied to cover gas system expenses of a general nature. Amounts received from Italgas are paid in full to the Cassa per i Servizi Energetici e Ambientali (CSEA).

(€ thousands)	Jun-Dec 2016	2017
RE-RS-UG1 fees	26,583	98,921
UG3 fees	12,805	42,263
Gas Bonus and GS fees	(1,482)	(10,221)
UG2 fees	4,808	(56,777)
	<b>42,714</b>	<b>74,186</b>

The fees in addition to the distribution service (€74,186 thousand) mainly relate to the following fees: (i) RE, to cover the expenses for calculating and implementing energy savings and the development of renewable energy sources in the gas sector; (ii) RS, as coverage for gas services quality; (iii) UG1, to cover any imbalances in and adjustments to the equalisation system; (iv) UG2, to cover the costs of retail sales marketing; (v) UG3int, to cover expenses connected to the interruption of services; (vi) UG3ui, to cover expenses connected to any imbalances in specific equalisation mechanism balances for the Default Distribution Service Provider (FDD) as well as the expenses for payment delays incurred by Suppliers of Last Instance (FUI), limited to end customers for which the supply cannot be suspended; (vii) UG3ft, to fund the expense account for the service of temporary providers on the transport network; (viii) GS, to cover the tariff compensation system for economically disadvantaged customers.

Gas distribution revenue (€1,044,966 thousand) refers to natural gas transport on behalf of all commercial operators requesting access to the networks of the distribution companies based on the Network Code; the most significant annual transport volumes were those relating to activities carried out for Eni S.p.A. This revenue was calculated based on Authority resolutions no. 220/2017/R/gas and 367/2014/R/gas.

They include €47,911 thousand relating to the contribution pursuant to Article 57 of the Authority Resolution 367/14 which relates to the investment plan to replace traditional meters with electronic smart meters, as set out in the remote reading project pursuant to Authority resolutions 631/13 and 554/15.

Revenue from the sale of water (€6,533 thousand) relates to the water distributed by Napoletanagas until 30 September 2017 and by Italgas Reti from 1 October 2017 to 31 December 2017 for Napoletanagas' incorporation in Italgas Reti.

## OTHER REVENUE AND INCOME

*Other revenue and income*, which amounted to €50,112 thousand, can be broken down as follows:

(€ thousands)	Jun-Dec 2016	2017
Income from gas distribution service safety recovery incentives	24,289	12,129
Income from property investments	983	4,291
Contractual penalties receivable	489	728
Net income from Energy Efficiency Certificates (*)		8,055
Capital gains from sale of assets		2,551
Plant safety assessment pursuant to Law Decree 40/04		2,766
Revenue from regulated activities		12,479
Management refunds and chargebacks (**)		1,685
other revenue	289	5,428
	<b>26,050</b>	<b>50,112</b>

(\*) Net of costs incurred for purchase of certificates

(\*\*) The value includes revenue relating to inventories, totalling €1,090 thousand.

Income from safety recovery incentives, equal to €12,129 thousand, relates to refunds paid by the Authority connected to achieving quality and technical standards relating to the natural gas distribution service.

## 27. OPERATING COSTS

The breakdown of operating costs for the period, which totalled €844,797 thousand, is shown in the following table:

(€ thousands)	Jun-Dec 2016	2017
Purchases, services and other costs	110,497	613,112
Personnel cost	57,269	231,685
	<b>167,766</b>	<b>844,797</b>



Operating costs relating to the construction and upgrading of natural gas distribution infrastructure connected with concession agreements pursuant to what is set forth in IFRIC 12, amount to €479,651 thousand and are broken down as follows:

(€ thousands)	Jun-Dec 2016	2017
Purchase costs for raw materials, consumables, supplies and goods	7,825	129,820
Service costs	37,196	239,289
Costs for the use of third-party assets	712	12,438
Personnel cost	15,841	97,116
Other expense	138	988
	<b>61,712</b>	<b>479,651</b>

#### PURCHASES, SERVICES AND OTHER COSTS

Purchases, services and other costs, which amounted to €613,112 thousand, can be broken down as follows:

(€ thousands)	Jun-Dec 2016	2017
Purchase costs for raw materials, consumables, supplies and goods	14,897	135,485
Service costs	69,148	354,237
Costs for the use of third-party assets	7,971	76,064
Changes in raw materials, consumables, supplies and goods	(7,651)	10,306
Net provisions for risks and charges	5,272	3,677
Net provisions for impairment	274	684
Other expense	21,231	33,317
	<b>111,142</b>	<b>613,770</b>
<i>To be deducted:</i>		
<b>Increases for own work</b>	<b>(645)</b>	<b>(658)</b>
- of which service costs	(645)	(658)
	<b>110,497</b>	<b>613,112</b>

Purchase costs for raw materials, consumables, supplies and goods are analysed below:

(€ thousands)	Jun-Dec 2016	2017
Inventories	13,470	124,604
Purchase of water	397	2,079
Motive power	149	1,132
Purchase of fuel	580	3,836
Consumables	301	3,834
	<b>14,897</b>	<b>135,485</b>

Inventories refer in particular to the acquisition of meters and gas pipes.

Purchase costs for raw materials, consumables, supplies and goods include costs relating to the construction and upgrading of gas distribution infrastructure (€129,820 thousand) recognised due to the entry into force of IFRIC 12 as of 1 January 2010.

Costs for services of €354,237 thousand relate to:

(€ thousands)	Jun-Dec 2016	2017
Project management and plant maintenance	31,923	206,547
Consultancy and professional services	12,923	46,632
Centralised service services	9,903	31,100
Costs for personnel services	2,754	13,842
IT and telecommunications services	2,257	16,324
Electricity, water and other (utility) services	733	4,775
Insurance	1,104	6,687
Cleaning, security service and guard services		3,871
Advertising and entertainment		2,447
Other services	9,873	27,614
Use of risk provision	(2,322)	(5,602)
	<b>69,148</b>	<b>354,237</b>
To be deducted:		
Increases for own work	(645)	(658)
	<b>68,503</b>	<b>353,579</b>

Costs for services include costs relating to the construction and upgrading of gas distribution infrastructure (€239,289 thousand) recognised due to the entry into force of IFRIC 12 as of 1 January 2010.

Costs for project management and plant maintenance planning (€206,547 thousand) essentially relate to the extension and maintenance of gas distribution plants.

Costs for the use of third-party assets, of €76,064 thousand, are analysed below:

(€ thousands)	Jun-Dec 2016	2017
Patent, license and concession fees	6,134	58,004
Leases and rentals	1,846	18,068
Use of risk provision	(9)	(8)
	<b>7,971</b>	<b>76,064</b>

Fees, patents and licences (€58,004 thousand) refer primarily to fees recognised to contracting parties for the running of natural gas distribution activities under concession.

Leases and rentals (€18,068 thousand) mainly relate to rent payments for office properties.

Costs for use of third-party assets include costs relating to the construction and upgrading of gas distribution infrastructure (€12,438 thousand) recognised due to the entry into force of IFRIC 12 as of 1 January 2010.

Changes in raw materials, consumables, supplies and goods (€10,306 thousand) were due mainly to the gas meter replacement plan.

Net allocations to the provision for risks and charges, amounting to €3,677 thousand net of utilisations, refer mainly to the environmental risk provision and the EEC risk provision.

For more details on the changes in provisions for risks and charges, please refer to the note "Provisions for risks and charges".

Other expenses, of €33,317 thousand, are analysed below:

(€ thousands)	Jun-Dec 2016	2017
Gas distribution service safety improvement penalties	15,904	7,920
Other penalties		3,415
Indirect taxes, local taxes	2,931	11,526
Capital losses from disposal/recovery of property, plant and equipment and intangible assets	730	6,675
Membership fees	59	1,310
Costs for transactions, compensation and penalties	847	320
Use of risk provision	(738)	(13,901)
Charges attributable to Energy Efficiency Certificates	60	7,431
Other expense	1,438	8,621
	<b>21,231</b>	<b>33,317</b>

Gas distribution service safety improvement penalties (€7,920 thousand) relate to repayments, paid to the Authority, related to awards for gas distribution safety improvements for 2017.

Charges attributable to Energy Efficiency Certificates (€7,431 thousand) are fully covered by use of the relevant risk provision.

#### PERSONNEL COST

Personnel cost, totalling €231,685 thousand, breaks down as follows:

(€ thousands)	Jun-Dec 2016	2017
Wages and salaries	28,600	168,482
Social charges	9,708	51,099
Employee benefits	2,374	14,336
Secondment	(1,387)	(6,440)
Other expense	18,921	7,328
	<b>58,216</b>	<b>234,805</b>
<i>To be deducted:</i>		
Increases for own work	(947)	(3,120)
	<b>57,269</b>	<b>231,685</b>

The item includes costs relating to the construction and upgrading of gas distribution infrastructure (€97,116 thousand) recognised due to the entry into force of IFRIC 12 as of 1 January 2010.

Employee benefits (€14,336 million) mainly regard expenses connected to the elimination of the Gas Fund, pursuant to Law no. 125 of 6 August 2015<sup>41</sup>.

More details are provided in the “Provisions for employee benefits” note.

The item other expenses (€7,328 thousand) mainly relates to provisions made in the period to the retirement benefits fund (€6,164 thousand).

#### AVERAGE NUMBER OF EMPLOYEES

The average number of payroll employees of the consolidated entities, broken down by status, is as follows:

Professional qualification	31.12.2016	2017
Executives	37	64
Managers	222	257
Office workers	1,909	1,966
Manual workers	1,392	1,363
	<b>3,560</b>	<b>3,650</b>

The average number of employees is calculated on the basis of the monthly number of employees for each category.

At 31 December 2017, there were 3,584 employees.

#### REMUNERATION DUE TO KEY MANAGEMENT PERSONNEL

The remuneration due to persons with powers and responsibilities for the planning, management and control of the Company, i.e. executive and non-executive directors, general managers and managers with strategic responsibilities (“key management personnel”), in office at 31 December 2017, amounted to €5,947 thousand and breaks down as follows:

(€ thousands)	Jun-Dec 2016	2017
Wages and salaries	1,718	4,121
Post-employment benefits	113	312
Other long-term benefits	980	1,514
	<b>2,811</b>	<b>5,947</b>

41 As of 1 December 2015, Law no. 125 of 6 August 2015 eliminated the General compulsory disability, old age and survivors’ insurance supplementary fund for employees of private gas companies (the “Gas Fund”) in which roughly 3,500 people in the Group participated, particularly in the distribution sector. The Law set a series of additional contributions that the employer must cover. These expenses, estimated on the basis of actuarial assumptions, were to date assessed at €40 million (€28 million net of the tax effect).

#### REMUNERATION DUE TO DIRECTORS AND STATUTORY AUDITORS

Remuneration due to Directors, except for the Chairman and the Chief Executive Officer who form part of the key management personnel as explained in the foregoing paragraph, amounted to €610 million and remuneration due to Statutory Auditors amounted to €287 thousand (Article 2427, no. 16 of the Italian Civil Code). This remuneration includes emoluments and any other amounts relating to pay, pensions and healthcare due for the performance of duties as a director or statutory auditor giving rise to a cost for the Company, even if not subject to personal income taxes.

## 28. AMORTISATION, DEPRECIATION AND IMPAIRMENT

*Amortisation, depreciation and impairment*, totalling €358,342 thousand, breaks down as follows:

(€ thousands)	Jun-Dec 2016	2017
<b>Amortisation and depreciation</b>	<b>76,802</b>	<b>352,001</b>
- Property, plant and equipment	2,149	16,261
- Intangible assets	74,653	335,740
<b>Impairment</b>		<b>6,341</b>
- Impairment of property, plant and equipment		31
- Impairment of intangible assets		6,310
	<b>76,802</b>	<b>358,342</b>

The amount of €335,740 thousand, relating to the amortisation of the intangible assets, includes greater amortisation as a result of the reduction in the useful life of traditional meters<sup>42</sup>, subject to the plan to replace them with electronic meters, required by AEEGSI resolutions under the scope of the implementation of the remote metering reading plan (€50,153 thousand).

42 The useful life of the meters included in the project pursuant to ARERA resolutions 631/13 and 554/15 was adjusted, in order to complete the amortisation process in line with the meter replacement plan, scheduled for completion by 2018.

## 29. FINANCIAL INCOME (EXPENSE)

Net financial expense, amounting to €36,249 thousand (€122,800 thousand as at 31 December 2016) comprises:

(€ thousands)	Jun-Dec 2016	2017
<b>Financial income (expense)</b>	<b>(123,971)</b>	<b>(36,078)</b>
Financial expense	(123,974)	(36,089)
Financial income	3	11
<b>Other financial income (expense)</b>	<b>1,171</b>	<b>(171)</b>
Other financial expense	815	(1,245)
Other financial income	356	1,074
	<b>(122,800)</b>	<b>(36,249)</b>

(€ thousands)	Jun-Dec 2016	2017
<b>Financial income (expense)</b>	<b>(123,971)</b>	<b>(36,078)</b>
<b>Borrowing costs:</b>	<b>(123,974)</b>	<b>(36,089)</b>
- Interest expense on bonds		(26,039)
- Commission expense on bank loans and credit lines	(1,451)	(5,904)
- Interest expense on credit line and loan expense due to banks and other lenders	(122,523)	(4,146)
<b>Financial expense capitalised</b>		
<b>Income on financial receivables:</b>	<b>3</b>	<b>11</b>
- Interest income and other income on financial receivables not held for operations	3	11
<b>Other financial income (expense)</b>	<b>1,171</b>	<b>(171)</b>
- Capitalised financial expense	553	139
- Financial income (expense) connected with the passing of time (accretion discount) (*)	350	(1,863)
- Uses of risk provisions and financial expense		1,314
- Other expenses	(88)	(594)
- Other income	356	833
	<b>(122,800)</b>	<b>(36,249)</b>

(\*) The item relates to the increase in the provisions for risks and charges and employee benefit funds that are specified, at a discounted value, in the notes "Provisions for risks and charges" and "Employee benefit funds".

The interest rate used for capitalising financial expenses in 2017 was 0.77%.



Expense on financial payables (€36,089 thousand) mainly concerns the expense for the coupons accruing on the bonds and other loans in place for €28,807 thousand and the amortisation of the upfront fees paid for granting of the bonds and loans for about €7,253 thousand.

### 30. INCOME (EXPENSE) FROM EQUITY INVESTMENTS

*Income (expense) from equity investments* of €22,973 thousand breaks down as follows:

(€ thousands)	Jun-Dec 2016	2017
<b>Equity method valuation effect</b>	<b>3,105</b>	<b>22,958</b>
Income from valuation using the equity method	3,105	22,958
<b>Other income (expense) from equity investments</b>		<b>15</b>
Other income from equity investments		15
	<b>3,105</b>	<b>22,973</b>

Details of capital gains and capital losses from the valuation of equity investments using the equity method can be found in the note "Investments accounted using the equity method".

### 31. INCOME TAXES

*Income taxes* for the year, amounting to €111,860 thousand (€-18,332 thousand as at 31 December 2016) comprise:

(€ thousands)	Jun-Dec 2016			2017		
	IRES	IRAP	Total	IRES	IRAP	Total
<b>Current taxes</b>	<b>9,526</b>	<b>3,788</b>	<b>(5,738)</b>	<b>111,219</b>	<b>20,233</b>	<b>131,452</b>
Current taxes for the year	(7,386)	3,788	(3,598)	108,627	20,246	128,873
Adjustments for current taxes pertaining to previous years	(2,140)		(2,140)	2,592	(13)	2,579
<b>Deferred and prepaid taxes</b>	<b>(11,778)</b>	<b>(816)</b>	<b>(12,594)</b>	<b>(16,986)</b>	<b>(2,606)</b>	<b>(19,592)</b>
Deferred taxes	(2,309)	(354)	(2,663)	(29,349)	(4,913)	(34,262)
Prepaid taxes	(9,469)	(462)	(9,931)	12,363	2,307	14,670
	<b>(21,304)</b>	<b>2,972</b>	<b>(18,332)</b>	<b>94,233</b>	<b>17,627</b>	<b>111,860</b>

Income taxes relate to current taxes amounting to €131,452 thousand (€-5,738 thousand as at 31 December 2016) and net prepaid taxes totalling €19,592 thousand (€12,594 thousand as at 31 December 2016).

The rates applied and provided for by tax regulations for current taxes are 24% for IRES and 4.2% for IRAP.

The reconciliation of the theoretical tax charge (calculated by applying the corporation tax (IRES) rate in force in Italy) with the actual tax charge for the year can be broken down as follows:

(€ thousands)	Jun-Dec 2016		2017	
	Tax rate	Balance	Tax rate	Balance
<b>IRES</b>				
Pre-tax profit		(90,541)		404,626
<b>IRES tax calculated based on the theoretical tax rate</b>	<b>27.5%</b>	<b>(24,899)</b>	<b>24.00%</b>	<b>97,110</b>
<i>Changes compared to the theoretical rate:</i>				
- Income from equity investments	(2.9%)	2,613	(0.7%)	(2,930)
- Temporary tax adjustment			(0.7%)	(2,841)
- Current taxes for previous years			0.6%	2,592
- Other permanent differences	(1.1%)	982	0.1%	302
<b>IRES taxes for the year through profit or loss</b>	<b>23.5%</b>	<b>(21,304)</b>	<b>23.3%</b>	<b>94,233</b>

(€ thousands)	Jun-Dec 2016		2017	
	Tax rate	Balance	Tax rate	Balance
<b>IRAP</b>				
EBIT for IRAP		40,305		417,643
<b>IRAP tax calculated based on the theoretical tax rate</b>	<b>4.2%</b>	<b>1,693</b>	<b>4.2%</b>	<b>17,541</b>
<i>Changes compared to the theoretical rate:</i>				
- Taxes for previous years	0.4%	163		
- Temporary tax adjustment			(0.6%)	(2,552)
- Regional IRAP adjustments	0.6%	222	0.5%	2,116
- Other permanent differences	2.2%	894	0.1%	522
<b>IRAP taxes for the year through profit or loss</b>	<b>7.4%</b>	<b>2,972</b>	<b>4.2%</b>	<b>17,627</b>

An analysis of deferred and prepaid taxes based on the nature of the significant temporary differences that generated them can be found in the note "Deferred tax liabilities".

### TAXES RELATED TO COMPONENTS OF COMPREHENSIVE INCOME

Current and deferred taxes related to other components of comprehensive income can be broken down as follows:

(€ thousands)	Jun-Dec 2016			2017		
	Pre-tax value	Tax impact	Net value	Pre-tax value	Tax impact	Net value
Remeasurement of defined-benefit plans for employees	17,138	(4,833)	12,305	18,595	(5,244)	13,351
<b>Other components of comprehensive income</b>	<b>17,138</b>	<b>(4,833)</b>	<b>12,305</b>	<b>18,595</b>	<b>(5,244)</b>	<b>13,351</b>
<b>Deferred/prepaid taxes</b>		<b>(4,833)</b>			<b>(5,244)</b>	

### 32. PROFIT (LOSS) PER SHARE

The earnings per basic share, equal to €0.36, was calculated by dividing the net profit attributable to Italgas (€292,766 thousand) by the weighted average number of Italgas shares outstanding during the year (809,135,502 shares).

The diluted earnings per share was calculated by dividing the net profit by the weighted average number of shares outstanding during the period, excluding any treasury shares, increased by the number of shares that could potentially be added to those outstanding as a result of the assignment or disposal of treasury shares in the portfolio for stock option plans. As there are no treasury shares, the basic and diluted earnings per basic share are the same.

### 33. RELATED PARTY TRANSACTIONS

Considering the “de facto” control of CDP S.p.A. over Italgas S.p.A., pursuant to the international accounting standard IFRS 10 - Consolidated Financial Statements, the related parties of Italgas, based on the current Group ownership structure, are represented by Italgas’ associates and joint ventures, as well as by the parent company, CDP S.p.A., and by its subsidiaries and associates and direct or indirect subsidiaries, associates and joint ventures of the Ministry of Economy and Finance (MEF). Members of the Board of Directors, Statutory Auditors and managers with strategic responsibilities of the Italgas Group and their families, are also regarded as related parties.

As explained in detail below, related-party transactions involve the trading of goods and the provision of regulated services in the gas sector. Transactions between Italgas and related parties are part of ordinary business operations and are generally settled at arm’s length, i.e. at the conditions that would be applied between two independent parties. All the transactions carried out were in the interest of the companies of the Italgas Group.

Pursuant to the provisions of the applicable legislation, the Company has adopted internal procedures to ensure that transactions carried out by the Company or its subsidiaries with related parties are transparent and correct in their substance and procedure.

The Directors and Statutory Auditors declare potential interests that they have in relation to the company and the group every six months, and/or when changes in said interests occur; in any case, they promptly inform the Chief Executive Officer (or the Chairman, in the case of the Chief Executive Officer's interests), who in turn informs the other directors and the Board of Statutory Auditors, of the individual transactions that the company intends to carry out and in which they have an interest.

Italgas is not subject to management and coordination activities. Italgas exerts management and coordination activities over its subsidiaries pursuant to Articles 2497 et seq. of the Civil Code.

The amounts involved in commercial, financial and other transactions with the above-mentioned related parties are shown for the 2017 financial year. The nature of the most significant transactions is also stated.

#### COMMERCIAL AND OTHER TRANSACTIONS

Commercial and other transactions are analysed below:

(€ thousands)	Jun-Dec 2016			2016				
				Costs (a)		Revenue (b)		
	Receivables	Payables	Guarantees and commitments	Assets	Services	Other	Services	Other
<b>Companies under joint control and associates</b>								
- Toscana Energia S.p.A.	1,525	155			31		518	
- Umbria Distribuzione Gas S.p.A.	413						93	
- Metano Sant'Angelo Lodigiano S.p.A.	138				(1)		5	38
	<b>2,076</b>	<b>155</b>			<b>30</b>		<b>616</b>	<b>38</b>
<b>Companies owned or controlled by the State</b>								
- Eni Group	212,710	38,820	1,141		(72)		170,853	5,007
- Snam Group	9,922	30,802	91,835		13,484	101	68	145
- Enel Group	31,667	2,537			1		30,763	453
- Anas Group	76	235				(24)		
- Ferrovie dello Stato Group	49	634				321		(87)
- Finmeccanica Group	36							
- GSE Gestore Servizi Group	44	1						
- Poste italiane Group		194			54			
	<b>254,504</b>	<b>73,223</b>	<b>91,835</b>		<b>13,467</b>	<b>398</b>	<b>201,684</b>	<b>5,518</b>
<b>Total</b>	<b>256,580</b>	<b>73,378</b>	<b>91,835</b>		<b>13,497</b>	<b>398</b>	<b>202,300</b>	<b>5,556</b>

(a) Include costs for goods and services for investment.

(b) Gross of the tariff components having contra entry in costs.

(€ thousands)

31.12.2017

2017

				Costs (a)			Revenue (b)		
	Receivables	Payables	Guaratees and commitments	Assets	Services	Other	Services	Other	
Companies under joint control and associates									
- Toscana Energia S.p.A.	2,518	155			187		3,410		
- Umbria Distribuzione Gas S.p.A.	355						536		
- Metano Sant'Angelo Lodigiano S.p.A.	203				(1)		303	(26)	
	3,076	155			186		4,249	(26)	
Companies owned or controlled by the State									
- Eni Group	186,077	43,598	725		2,089	45	630,374	21,167	
- Snam Group	6,651	24,185	85,569		34,577	498	197	1,749	
- Enel Group	30,196	3,885			8		114,566	2,147	
- Anas Group	14	304			9	227	11	29	
- Ferrovie dello Stato Group	51	400			24	212		71	
- Finmeccanica Group	10								
- GSE Gestore Servizi Group	44	23						(138)	
- Poste italiane Group		259			290				
	223,043	72,654	86,294		36,997	982	745,148	25,025	
Total	226,119	72,809	86,294		37,183	982	749,397	24,999	

(a) Include costs for goods and services for investment.

(b) Gross of the tariff components having contra entry in costs.

**COMPANIES UNDER JOINT CONTROL AND ASSOCIATES**

The main receivable commercial transactions mainly regard IT services provided to Toscana Energia S.p.A.

**COMPANIES OWNED OR CONTROLLED BY THE STATE**

The main receivable commercial transactions refer to:

- the distribution of natural gas and personnel loans to Eni S.p.A.;
- real estate management services, IT services and personnel loans to Eni S.p.A.;
- distribution of natural gas to Enel Energia S.p.A.

The main payable commercial transactions refer to:

- services provided by Snam S.p.A.;

- the supply of electricity and methane gas for internal consumption by Eni S.p.A.;
- services regarding the management and maintenance of real estate, personnel services, canteen management and other general services by Eni Servizi S.p.A..

#### FINANCIAL TRANSACTIONS

Financial transactions can be broken down as follows:

(€ thousands)	31.12.2016	2016
	Receivables Payables	Income Expense
<b>Parent company</b>		
- Cassa Depositi e Prestiti		736
		<b>736</b>
<b>Companies owned or controlled by the State</b>		
- Snam Group		120.581
		<b>120.581</b>
		<b>121.317</b>

(€ thousands)	31.12.2017	2017
	Receivables Payables	Income Expense
<b>Parent company</b>		
- Cassa Depositi e Prestiti		466
		<b>466</b>

#### RELATIONS WITH THE PARENT COMPANY CDP

The main financial transactions carried out with CDP specifically concern commissions on subscribed loans.

#### COMPANIES OWNED OR CONTROLLED BY THE STATE

Passive financial transactions with Snam S.p.A. regarding 2016 mainly relate to expenses resulting from the settlement of related loans, following the acquisition of Italgas Reti S.p.A..

Transactions with Directors, Statutory Auditors and key managers, with reference in particular to their remuneration, are described in the note "Operating costs", to which reference is made.

### IMPACT OF RELATED-PARTY TRANSACTIONS OR POSITIONS ON THE STATEMENT OF FINANCIAL POSITION, INCOME STATEMENT AND STATEMENT OF CASH FLOWS

The impact of related-party transactions or positions on the Statement of Financial Position is summarised in the following table:

(€ thousands)	Jun-Dec 2016			31.12.2017		
	Total	Related entities	Incidence %	Total	Related entities	Incidence %
Statement of financial position						
Trade and other current receivables	579,090	255,856	44.2%	619,202	225,387	36.4%
Other current assets	4,410	18	0.4%	5,944	30	0.5%
Investments valued using the equity method	175,707	175,707	100.0%	184,829	184,829	100.0%
Other investments	54	54	100.0%	54	54	100.0%
Other non-current assets	37,874	706	1.9%	77,891	702	0.9%
Short-term financial liabilities	2,695,603			81,133		
Short-term portions of long-term financial liabilities	435			25,043		
Trade and other payables	443,112	73,023	16.5%	498,174	72,469	14.5%
Other current liabilities	193	190	98.4%	182	175	96.2%
Long-term financial liabilities	923,005			3,617,044		
Other current liabilities	4,876	165	3.4%	2,055	165	8.0%

The impact of related-party transactions on the income statement is summarised in the following table:

(€ thousands)	Jun-Dec 2016			31.12.2017		
	Total	Related entities	Incidence %	Total	Related entities	Incidence %
Income Statement						
Core business revenue	247,672	202,300	81.7%	1,570,929	749,397	47.7%
Other revenue and income	26,050	5,556	21.3%	50,112	24,999	49.9%
Purchases, services and other costs	110,497	15,206	13.8%	613,112	44,623	7.3%
Personnel cost	57,269	(1,311)		231,685	(6,458)	
Financial expense	122,800	121,317	98.8%	37,334	466	1.2%
Financial income				1,085		



Related-party transactions are generally carried out at arm's length, i.e. at the conditions that would be applied between two independent parties.

The principal cash flows with related parties are shown in the following table:

(€ thousands)	Jun-Dec 2016	2017
Revenue and income	207,856	774,396
Costs and charges	(13,895)	(38,165)
Change in trade and other current receivables	(255,856)	30,469
Change in other current assets	(18)	(12)
Change in trade and other payables	73,023	569
Change in other current liabilities	190	
Interest income (paid)	(121,317)	(466)
<b>Net cash flow from operating activities</b>	<b>(110,017)</b>	<b>766,791</b>
Investments:		
Change in scope of consolidation and business units	(1,502,950)	
<b>Cash flow from investments</b>	<b>(1,502,950)</b>	
<b>Net cash flow from investment activities</b>		
Dividends distributed to Italgas shareholders		(64,003)
<b>Net cash flow from financing activities</b>		<b>(64,003)</b>
<b>Total cash flows to related entities</b>	<b>(1,612,967)</b>	<b>702,788</b>

The effect of cash flows with related parties is shown in the following table:

(€ thousands)	Jun-Dec 2016			31.12.2017		
	Total	Related entities	Incidence %	Total	Related entities	Incidence %
Cash flow from operating activities	(45,555)	(110,017)		546,712	766,791	
Cash flow from investment activities	(1,567,490)	(1,502,950)	95.9%	(476,110)		
Cash flow from financing activities	1,614,589			(69,315)	(64,003)	92.3%

### **34. SIGNIFICANT NON-RECURRING EVENTS AND TRANSACTIONS**

Pursuant to Consob Communication DEM/6064293 of 28 July 2006, it should be stated that no significant non-recurring events or transactions took place during the course of the year.

### **35. POSITIONS OR TRANSACTIONS ARISING FROM ATYPICAL AND/OR UNUSUAL TRANSACTIONS**

Pursuant to Consob Communication DEM/6064293 of 28 July 2006, it should be stated that no atypical and/or unusual positions or transactions took place during the course of the year.

### **36. SIGNIFICANT EVENTS AFTER YEAR END**

Post-balance sheet events are described in the section “Other information” contained in the Directors’ Report.

### **37. PUBLICATION OF THE FINANCIAL STATEMENTS**

The financial statements were authorised for publication by the Board of Directors of Italgas at its meeting of 12 March 2018. The Board of Directors authorised the Chairman and the Chief Executive Officer to make any changes which might be necessary or appropriate for finalising the form of the document during the period between 12 March and the date of approval by the Shareholders’ Meeting.

## Certification of the consolidated financial statements pursuant to Article 154-bis, paragraph 5 of Legislative Decree 58/1998 (Consolidated Finance Act)

1. Pursuant to article 154-bis, paragraphs 3 and 4 of Legislative Decree 58 of 24 February 1998, the undersigned Paolo Gallo and Claudio Ottaviano, as Chief Executive Officer and Chief Financial Officer of Italgas S.p.A. respectively, certify:

- the adequacy, considering the Company's characteristics, and
- the effective implementation

of the administrative and accounting procedures for the preparation of the consolidated financial statements during the course of 2017.

2. The administrative and accounting procedures for the preparation of the consolidated financial statements at 31 December 2017 were defined and their adequacy was assessed using the rules and methods in line with the Internal Control – Integrated Framework model issued by the Committee of Sponsoring Organisations of the Treadway Commission, which represents a benchmark framework for the internal control system generally accepted at international level.
3. It is also certified that:
  - 3.1 The consolidated financial statements at 31 December 2017:
    - a) were prepared in accordance with the applicable international accounting standards recognised in the European Community pursuant to Regulation (EC) no. 1606/2002 of the European Parliament and of the Council of 19 July 2002;
    - b) are consistent with the accounting books and records;
    - c) are able to provide a true and fair view of the financial position, results of operations and cash flows of the issuer and the consolidated companies.
  - 3.2 The Directors' Report includes a reliable analysis of the operating performance and results, as well as the position of the issuer and of all the companies included in the scope of consolidation, together with a description of the principal risks and uncertainties to which they are exposed.

12 March 2018

Chief Executive Officer

*Paolo Gallo*

Executive responsible

for preparing the corporate accounting documents

*Claudio Ottaviano*



## **Independent auditor's report**

*in accordance with article 14 of Legislative Decree No. 39 of 27 January 2010 and article 10 of Regulation (EU) No. 537/2014*

To the shareholders of Italgas SpA

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### **Report on the Audit of the Consolidated Financial Statements**

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#### **Opinion**

We have audited the consolidated financial statements of Italgas Group (the Group), which comprise the balance sheet as of 31 December 2017, the income statement, statement of comprehensive income, statement of changes in shareholders' equity, cash flows statement for the year then ended, and 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 Group as of 31 December 2017, 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, as well as with the regulations issued to implement article 9 of Legislative Decree No. 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 the *Auditor's Responsibilities for the Audit of the Consolidated Financial Statements* section of this report. We are independent of Italgas 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

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#### **PricewaterhouseCoopers SpA**

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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.

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### **Key Audit Matters**

### **Auditing procedures performed in response to key audit matters**

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#### **First year of the engagement**

On 28 April 2017 the shareholders of Italgas SpA in general meeting engaged PwC to perform the statutory audit of the Company's and the consolidated financial statements for the years 2017 to 2025.

The complexity of the Company and the Group, as well as the regulatory framework and environment of the gas distribution industry in which the Italgas Group operates were key audit matters requiring special attention in the course of the first year of the engagement.

In performing our audit procedures we held a number of meetings with the Group's key officials, with a special focus on understanding the regulatory framework and environment of the gas distribution industry, the associated risks, and the corporate processes and policies in place to address those risks.

We obtained a specific understanding of the key accounting policies adopted by the Italgas Group and obtained documentary evidence and the rationale for the key accounting issues in the consolidated financial statements as of 31 December 2016.

We reviewed the working papers of the predecessor auditor relating to the audit of the consolidated financial statements as of 31 December 2016 and discussed with them the audit strategy adopted, the materiality applied, the accounting policies adopted by the Italgas Group in its financial reporting for the previous year and the findings from the audit of the 2016 consolidated financial statements.

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#### **Revenue recognition**

*Note 3 "Measurement criteria" and Note 26 "Revenues" to the consolidated financial statements as of 31 December 2017.*

The recognition of revenues from distribution of natural gas is affected by regulatory schemes and is characterised by a distinction between the distributor's revenues granted by the regulator (the so-called distribution revenues cap, "Total Revenue Limit") and amounts billed to

In performing our auditing procedures we analysed, understood and evaluated the Group's system of internal control over the business process "Revenue and Receivables" which includes internal controls over revenue recognition.

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### **Key Audit Matters**

customers. The Total Revenue Limit and the tariffs to be applied for customer billing are set, and published in specific regulations, by the Italian Regulatory Authority for Energy, Networks and the Environment (Autorità di Regolazione per Energia Reti e Ambiente, ARERA). The regulation also provides for equalisation mechanisms to be applied to a distributor's revenues, based on which the difference between the Total Revenue Limit and amounts billed to customers generates an account receivable (if positive) or payable (if negative) from/to Energy and Environmental Service Fund (CSEA) - a public sector entity that manages certain tariff components paid by power, gas and water operators - which is settled in the following financial year. In consideration of the significant volume of transactions and the complexity of the regulations applicable to the quantification of distribution revenues, we identified revenue recognition as a key audit matter with reference to the correct calculation of revenues.

### **Auditing procedures performed in response to key audit matters**

We identified and validated the operation and effectiveness of the relevant (manual and automated) controls over that process, also using the support of PwC network specialists in IT systems and business process analysis.

We verified the reconciliation of sales values in the general ledger to the Total Revenue Limit identified by ARERA based on the provisional tariffs established by ARERA for FY 2017 with Regulation 220/2017.

We verified the correct quantification of the accrual for equalisation with CSEA, based on the difference between the Total Revenue Limit and amounts billed to customers during the year.

Finally, we carried out external confirmation procedures with third parties to obtain evidence supporting the trade receivables recognised.

### **Capital expenditure relating to service concession agreements (IFRIC 12) and related impairment test**

*Note 15 "Intangible assets" to the consolidated financial statements as of 31 December 2017.*

"Service concession agreements" amounted to Euro 4,569 million as of 31 December 2017, accounting for 93% of total 'Non-current assets'.

The gas distribution sector in which the Italgas Group operates is characterised by specific regulations issued by ARERA. In detail, the Group's distribution revenues are determined by ARERA based on a predefined return on capital expenditure (assets under concession), depreciation and certain operating costs.

In consideration of the significant amounts of

In performing our audit procedures we analysed, understood and evaluated the Group's system of internal control over the business processes "Tangible and intangible assets" and "Capital expenditure" which include controls over the correct capitalisation of capital expenditure and the management of tangible and intangible assets.

We identified and validated the operation and effectiveness of the relevant (manual and automated) controls over that process, also using the support of PwC network specialists in IT



### **Key Audit Matters**

capital expenditure, we identified it as a key audit matter area with reference to the correct recognition of expenditure in accordance with IFRIC 12 – Service concession agreements.

During the year the Italgas Group made capital expenditure for about Euro 482 million mainly relating to service concession agreements for maintaining and developing the remote metering networks (Euro 451 million).

Amortization for the period, equal to Euro 336 million, also includes greater amortization (Euro 50 million) as a result of the reduction in the useful life of traditional meters of that are to be replaced with electronic meters in accordance with the replacement plan issued by ARERA, to be completed within 2018 pursuant to Resolutions 631/13 and 554/15.

At the end of the period management considered it appropriate to test for impairment the intangible assets falling into the scope of IFRIC 12, regardless of the existence of possible impairment indicators, in light of the materiality of the amounts involved.

The recoverability of intangible assets was verified through a comparison between the carrying amount and the recoverable amount, this being the higher of fair value and value in use.

In detail, management estimated the recoverable amount of intangible assets included in the regulated business making reference to the net invested capital for regulatory purposes, calculated on the basis of the rules defined by ARERA for determining base revenues for regulated businesses (the Regulatory Asset Base, “RAB”), which market operators consider as the minimum measure of fair value for regulated businesses.

### **Auditing procedures performed in response to key audit matters**

systems and business process analysis.

We verified the reconciliation of the asset register to the general ledger values, recalculated amortization charges for the period, on a sample basis, and verified decreases in the period, on a sample basis.

With reference to capital expenditure in the period we selected a sample of transactions and verified that they had been recognised in accordance with the capitalisation criteria established in the applicable financial reporting standards.

With reference to the plan to replace traditional meters with smart meters, we verified the method applied by the Group to identify and determine replaced meters, and to recognise accelerated amortization in relation to the planned retirement and replacement of traditional meters. We also analysed the method of calculation used by the Group to recognise in accordance with the accrual basis of accounting the tariff contribution granted by ARERA in relation to the replaced meters.

We analysed the age of projects recognised in assets under construction and discussed with management the key items of capital expenditure and their nature, with particular reference to the oldest projects in progress, in order to identify any indicators of impairment.

We examined the method adopted by management to identify and assess possible indicators of impairment of intangible assets and, if necessary, to carry out impairment testing.

We obtained the impairment test from the Company and held meetings with management to understand the method applied. We obtained and verified the estimate of the Regulatory Asset Base as of 31 December 2017.





### **Key Audit Matters**

### **Auditing procedures performed in response to key audit matters**

We verified that the carrying amounts of tangible and intangible assets used for the impairment test matched the values in the financial statements.

We re-performed the impairment test and confirmed the Company's conclusion that fixed assets had not become impaired.

Finally, we verified the accuracy and completeness of the disclosures presented in note 15 to the consolidated financial statements as of 31 December 2017.

### **Refinancing**

*Note 18 "Short-term financial liabilities, long-term financial liabilities and short-term portion of long-term financial liabilities" to the consolidated financial statements as of 31 December 2017.*

Financial liabilities account for about 72% of the Group's "Total liabilities and equity" as of 31 December 2017.

It should also be considered that in the course of the year the Company was involved in significant refinancing transactions in the interests of the Italgas Group as a whole.

In detail, the Company issued certain medium- and long-term bonds listed on the Luxembourg stock exchange (Euro Medium Term Notes Programme), for a total of Euro 2,650 million, which enabled it to early repay the bridge loan obtained in the previous year from a pool of bank for a total of Euro 2,300 million. Moreover, the Company entered into a new loan agreement with the European Investment Bank (EIB) for Euro 360 million.

In consideration of the magnitude of the balance

In performing our audit procedures we analysed, understood and evaluated the Group's system of internal control over the business process "Finance".

We identified and validated the operation and effectiveness of the relevant (manual and automated) controls over that process, also using the support of PwC network specialists in IT systems and business process analysis.

We examined the evidence supporting the bonds issued during the year and the bank loans obtained. For the latter we performed external confirmation procedures to obtain evidence supporting the financial liabilities recognised.

We verified the correct recognition of the above-mentioned financial liabilities, and the correct measurement of financial instruments in accordance with IAS 39 and the determination of



<b><i>Key Audit Matters</i></b>	<b><i>Auditing procedures performed in response to key audit matters</i></b>
relative to 'Total liabilities and equity' and of the significant movements during the year we identified financial indebtedness as a key audit matter.	the current and non-current portions.  Finally, we verified the accuracy and completeness of the disclosures provided in note 18 to the consolidated financial statements as of 31 December 2017.

### ***Responsibilities of Management and Those Charged with Governance for the Consolidated Financial Statements***

Management is 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, as well as with the regulations issued to implement article 9 of Legislative Decree No. 38/05 and, in the terms prescribed by law, for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Management is 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, management uses the going concern basis of accounting unless management either intends to liquidate Italgas SpA or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing, in the terms prescribed by law, the Group's financial reporting process.

### ***Other matters***

The consolidated financial statements of Italgas Group for the year ended 31 December 2016 were audited by another auditor which, on 3 April 2017, issued an unqualified audit report.

### ***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 auditors' 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 judgement 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 management;
- We concluded on the appropriateness of management's 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 were of most significance in the audit of the consolidated 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) No 537/2014***

On 28 April 2017, the shareholders of Italgas SpA in general meeting engaged us to perform the statutory audit of the Company's and the consolidated financial statements for the years ending 31 December 2017 to 31 December 2025.

We declare that we did not provide any prohibited non-audit services referred to in article 5, paragraph 1, of Regulation (EU) No. 537/2014 and that we remained independent of the Company in conducting the statutory audit.

We confirm that the opinion on the consolidated financial statements expressed in this report is consistent with the additional report to those charged with governance, in their capacity as audit committee, prepared pursuant to article 11 of the aforementioned Regulation.

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***Report on Compliance with other Laws and Regulations***

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***Opinion in accordance with Article 14, paragraph 2, letter e), of Legislative Decree No. 39/10 and Article 123-bis, paragraph 4, of Legislative Decree No. 58/98***

Management of Italgas SpA is responsible for preparing a report on operations and a report on the corporate governance and ownership structure of the Italgas Group as of 31 December 2017, 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) No. 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 No. 58/98, with the consolidated financial statements of the Italgas Group as of 31 December 2017 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 Italgas SpA as of 31 December 2017 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 No. 39/10, issued on the basis of our knowledge and understanding of the Company and its environment obtained in the course of the audit, we have nothing to report.

***Statement in accordance with article 4 of Consob's Regulation implementing Legislative Decree No. 254 of 30 December 2016***

Management of Italgas SpA is responsible for the preparation of the non-financial statement pursuant to Legislative Decree No. 254 of 30 December 2016.

We have verified that management approved the non-financial statement.

Pursuant to article 3, paragraph 10, of Legislative Decree No. 254 of 30 December 2016, the non-financial statement is the subject of a separate statement of compliance issued by ourselves.

Milan, 23 March 2018

PricewaterhouseCoopers SpA

*Signed by*

Giulio Grandi  
(Partner)

*This report has been translated into English from the Italian original solely for the convenience of international readers*





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