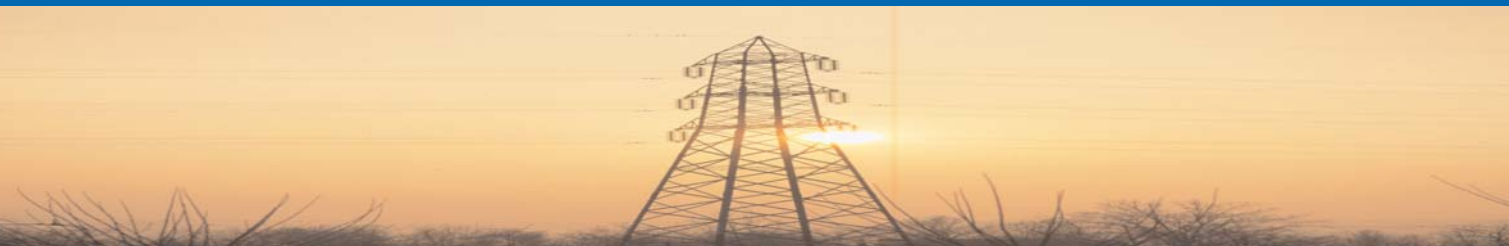




ANNUAL REPORT 2005

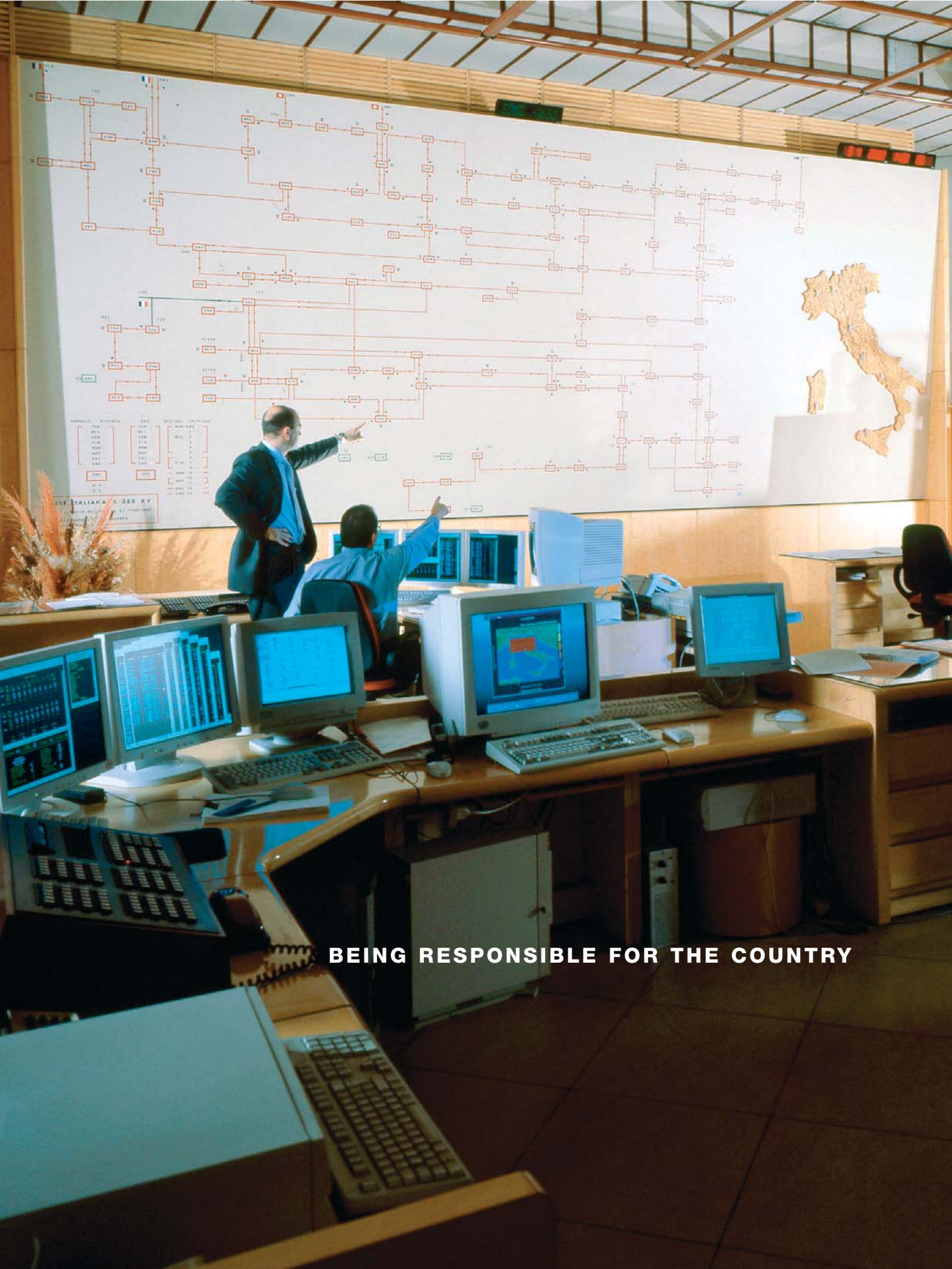
OUR PRESENT



SAFELY GUARANTEEING ENERGY TRANSMISSION TO THE COUNTRY
GUARANTEEING QUALITY SERVICE AND ACCESS TO THE NATIONAL TRANSMISSION GRID
TO ALL SECTOR OPERATORS
PROVIDING THE GRID'S MAINTENANCE AND DEVELOPMENT WHILE RESPECTING THE ENVIRONMENT
CREATING VALUE FOR SHAREHOLDERS, COLLABORATORS AND THE COUNTRY



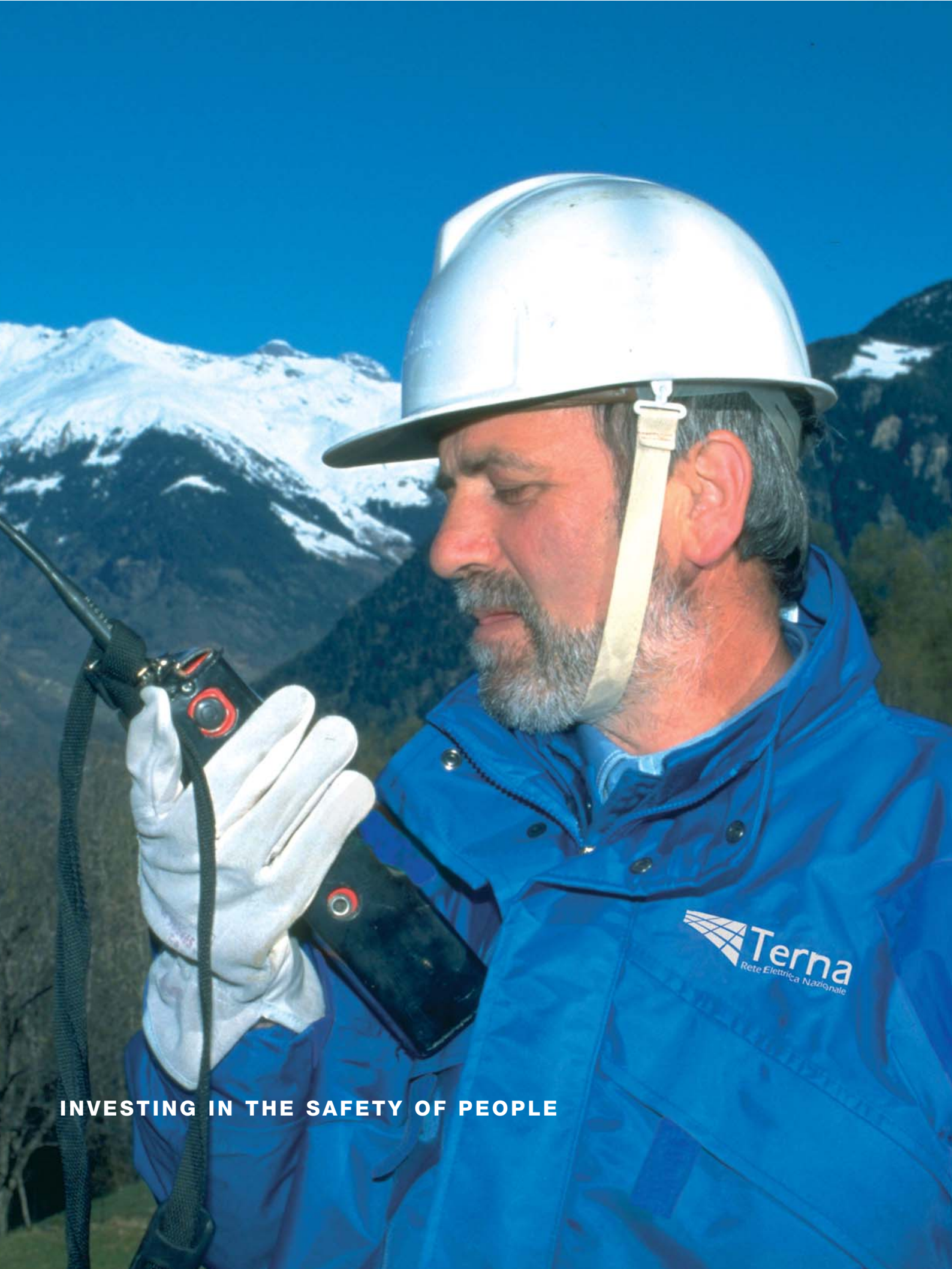
CONSOLIDATED FINANCIAL STATEMENTS 2005



BEING RESPONSIBLE FOR THE COUNTRY

FEELING RESPONSIBLE FOR THE ENVIRONMENT



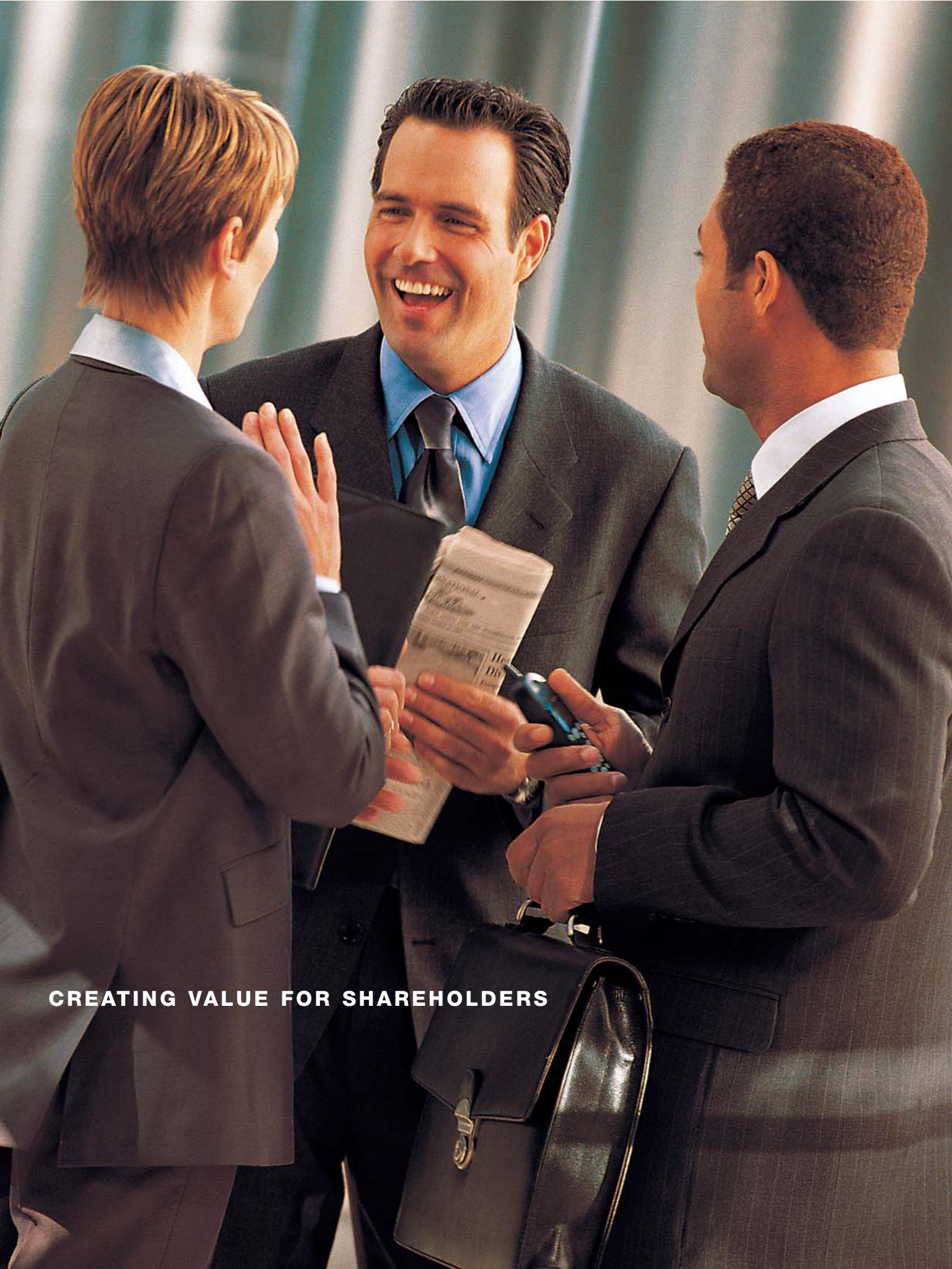


 **Terna**
Rete Elettrica Nazionale

INVESTING IN THE SAFETY OF PEOPLE



INVESTING IN TECHNOLOGICAL INNOVATION

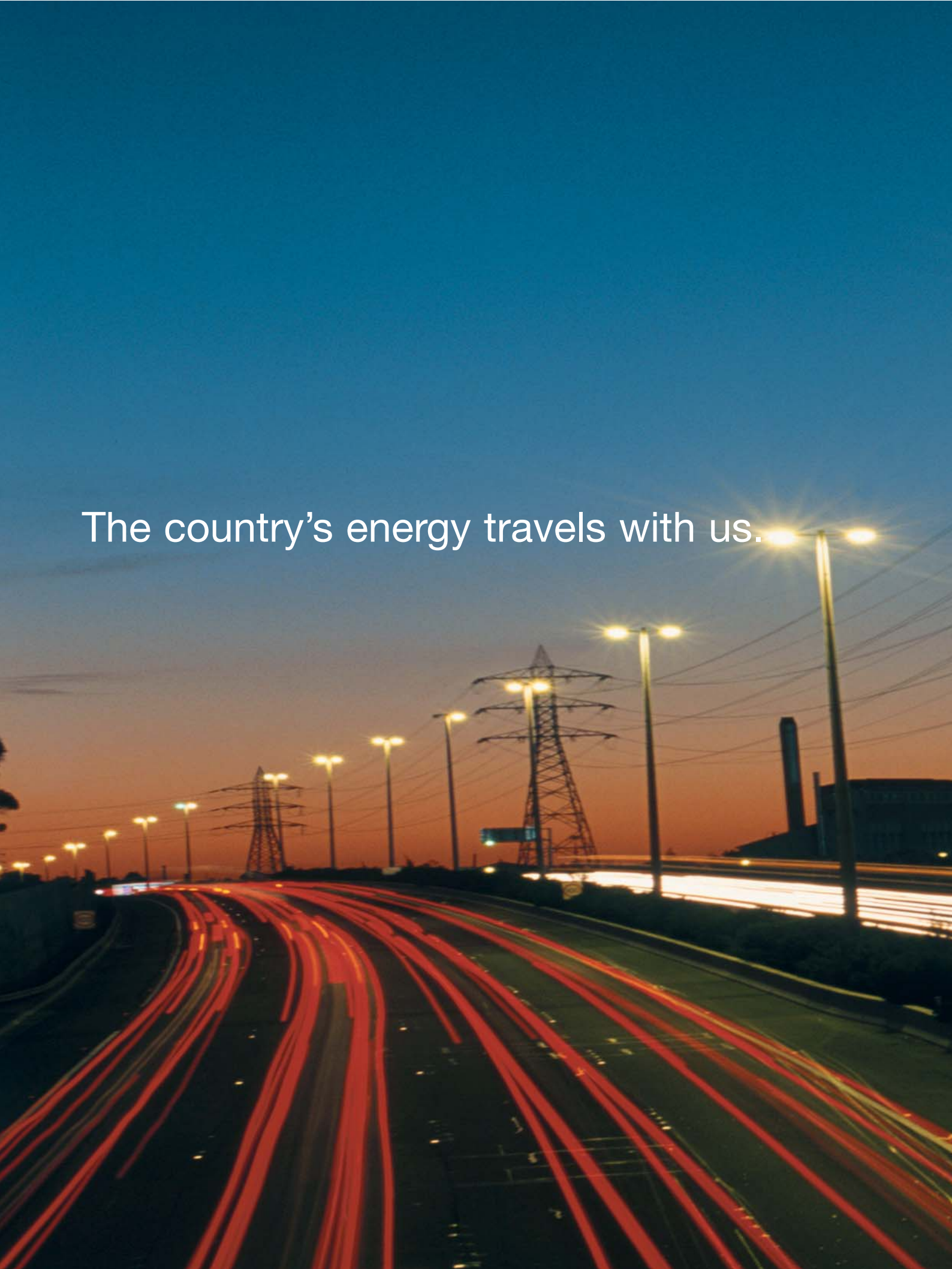


CREATING VALUE FOR SHAREHOLDERS

GIVING VALUE TO THE INTERNATIONAL PRESENCE



The country's energy travels with us.





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CHAIRMAN'S MESSAGE

Dear Terna Shareholders and Stakeholders,

by means of this Annual Report, for the first time the Group has presented results which include the functions of the grid operator, acquired as from November 2005. Terna looks out over 2006 with a new aspect: within a context of attention towards the financial markets and the creation of value, the Company has enhanced its connotation of concession holder of a public service, whilst at the same time confirming the commitments towards the search for business opportunities within non-regulated spheres.

The transmission of electricity is a service of primary importance for the community: its continual and safe supply and the constant search for improvements, also in relation to costs, represents a central responsibility for the Group. This is valid in Italy, where our activities extend to nearly all the transmission grid, but it is also true for the areas of foreign countries where our subsidiary companies operate: Terna is aware of the importance of the service which it provides, of its repercussions on the economic system and on the quality of life of the individuals, and is highly committed to guaranteeing a high level of quality of said service, improving management processes which however are already efficient

The investments in infrastructures envisaged by the Development Plan for the national transmission grid, which Terna annually submits for the approval of the Public Authorities, play a significant role in accompanying the country's economic growth. It is our responsibility that the definition of the Plan reflects the best possible choices for the community, reconciling the technical needs of the electricity system, the economic requirements and respect for the environment; for such a purpose, besides adopting independence and tertiary nature as our guidelines, we have decided to streamline the system for monitoring and handling the environmental impact of our activities and to subsequently submit it for certification. It is also our responsibility that the investments are accomplished within the timescales envisaged by the Plan, so as to guarantee the efficiency and inexpensiveness of the corporate operations. At the same time, attention towards the needs of the communities settled in the areas affected by our projects, will not be neglected; the study of solutions for improving the visual impact of the power stations will represent a tangible example of our approach.

The experience gained over the last few years is a requirement which reassures with regards to Terna's success prospects. The men and women who work for Terna are bearers of advanced specialist technical skills, and share attitudes and values which make it possible to look to the challenges posed by the Group's strategic objectives with confidence. The pride in providing a public utility service is already a factor for the aggregation of Terna's staff, as is the value of the technical training and the professional updating. Our schedule includes training measures which reinforce this precious gift of skills and values, and we have started along a route of constant reference to the ethical dimension of our activities, launching the review of the Ethical Code, a founding element of the corporate identity. In fact, we intend to accompany the Group's growth with regards to the business with the consolidation of its strong points: the human resources, the use of the best technologies available, the correctness of conduct.



We believe that the emphasis on responsibility which Terna is vested with, and which has been accounting for up to this point, must not be and is not in contrast with the aim of remunerating the shareholders. By contrast, in the future we intend to transparently provide account of our social and environmental performances: in fact we are convinced that awareness of the implications beyond our activities can provide us with important indications so as to render the growth process which the Group successfully started in 2005, and which has been set as the schedule for the coming years, sustainable in the future as well. It is with this conviction that we work every day.

The Chairman
LUIGI ROTH

A handwritten signature in black ink, reading "Luigi Roth". The signature is stylized and cursive, with the first name "Luigi" and the last name "Roth" clearly distinguishable.

LETTER TO THE SHAREHOLDERS AND STAKEHOLDERS

Dear Terna Shareholders and Stakeholders,

2005 was a year of positive results, on the up for Terna, which allows us to face 2006 with determination for growth and improvement. For Terna, 2005 was characterized by extremely significant corporate events which increase the Management responsibilities. On the one hand, the acquisition of the TSO business activities and the obligations deriving from the concessionary holder status mean that we have to pursue objectives of safety, reliability, efficiency and lower cost of the transmission and dispatch service envisaged by the Grid Code, operating on a neutral and impartial basis with respect to the other parties in the electricity sector. On the other hand, Cassa Depositi e Prestiti SpA's acquisition of 29.99% of Terna's share capital led to the loss of the Enel Group's control over the Company, completing the course towards full operating autonomy commenced by means of stockmarket listing.

Once again this year, Terna has demonstrated that it is in a position to achieve extremely significant results, continuing to apply the strategy targeted at operating excellency by means of increasing efficiency, optimizing investments and the quality of the service, operating levers which, together with the activities acquired under the TSO business segment, will provide a considerable contribution to the growth of the Group's value over the next few years.

During 2005, results considerably higher than in 2004 were achieved and the service quality and grid reliability objectives were attained.

Group revenues came to € 1.087 million, disclosing growth of 6.6% on 2004; the consolidated EBITDA amounted to € 722 million, disclosing an increase of 11%. The EBIT rose to € 547 million, registering a rise of 10.6%. Net earnings totaled € 297.9 million, up by 28.9%. These results, obtained partly thanks to the important contribution of the Brazilian companies, permits us to propose an accrued distribution of dividends amounting to Euro 0.13 with a yield of around 6%, up by 13% on last year and one of the highest levels of the sector.

The maintenance of an elevated return by means of an attractive dividend policy, supported by the steady generation of cash flows, represents the most important commitment made with the market by the Company's new management team, made even more interesting by the continuity of the commitment which the Company has already made to distribute dividends twice a year.



The equity soundness and the limited level of risk which characterize the Group continue to be confirmed by the assessments expressed by the rating agencies Standard & Poor's and Moody's.

Terna will pursue the stockmarket listing of the Brazilian subsidiaries during 2006, with the aim of fully expressing the value of the same, permitting access to the local capital market, extending the possibilities of future growth in the country, at the same time reducing the direct exposure to risk by Terna SpA. The operations will continue to be targeted at greater reliability and efficiency and the quality and safety of the services. The Company will continue to constantly compete with the costs and the quality of the best energy market operators in the world and has established ambitious operating, financial and strategic objectives for each of the following years with the aim of maintaining an elevated level of profitability which ensures on-going growth of the Group's value.

The Chief Executive Officer
FLAVIO CATTANEO

A handwritten signature in black ink, reading 'Flavio Cattaneo'. The signature is stylized, with a large, looped 'F' and a long horizontal line extending to the right.

NOTICE OF THE SHAREHOLDERS' MEETING

The Shareholders' Meeting is called in ordinary session at the "ROMA EVENTI - Piazza di Spagna" Congress Center, Via Alibert 5/a, Rome, on April 26, 2006 at 11.00 a.m. in first calling and, if necessary, on April 27, 2006, at the same time and place, in second calling in order to discuss and vote on the following

AGENDA

- Financial statements as of December 31, 2005. Reports of the Board of Directors, the Board of Statutory Auditors and the Independent Auditors. Related resolutions. Presentation of the consolidated financial statements as of December 31, 2005.
- Allocation of the net earnings for the year.

The Chairman of the Board of Directors
LUIGI ROTH

THE NOTICE OF CONVOCAION OF THE ORDINARY SHAREHOLDERS' MEETING IS PUBLISHED
IN THE OFFICIAL GAZETTE OF THE ITALIAN REPUBLIC, PART II°, NO. 70 DATED MARCH 24, 2006

SUMMARY OF THE RESOLUTIONS OF THE ORDINARY SHAREHOLDERS' MEETING

The ordinary session of the Shareholders' Meeting of Terna SpA held in second calling on April 27, 2006 at the "ROMA EVENTI - Piazza di Spagna" Congress Center in Via Alibert 5/a, Rome,:

- Approved the statutory financial statements of Terna SpA as of December 31, 2005;
- Acknowledged the figures of the consolidated financial statements of the Terna Group, likewise relating to December 31, 2005, which closed with net earnings of € 297,922.760.34;
- Passed a resolution to allocate Terna SpA's net earnings for 2005, equal to € 268,044,434.32 in the following manner:
 - To the extent of € 100,000,000.00 to cover the interim dividend available for payment as from November 24, 2005;
 - To the extent of € 160,000,000.00 as payment of the dividend to be distributed equal to € 0.080 - gross of any withholdings required by law - for each of the 2,000,000,000 ordinary shares, available for payment as from June 22, 2006 with "detachment date" of coupon No. 4 set for June 19, 2006;
 - To the extent of € 8,044,434.32 as "retained earnings".

BOARD OF DIRECTORS, BOARD OF STATUTORY AUDITORS AND INDEPENDENT AUDITORS

Board of Directors

President

Luigi Roth

Chief Executive Officer

Flavio Cattaneo

Directors

Luigi De Paoli

Mario Garraffo

Salvatore Machì

Carmine Macrì

Piero Giuseppe Maranesi

Massimo Ponzellini

Massimo Romano

Franco Smurro

Secretary to the Board

Ernesto Calaprice

Board of Statutory Auditors

Chairman

Giovanni Ferreri

Acting Auditors

Giancarlo Russo Corvace

Roberto Tasca

Alternate Auditors

Vito Di Battista

Bruno Franceschetti

Independent Auditors

KPMG SpA

STRUCTURE OF POWERS

Board of Directors

The Board of Directors is vested by the By-laws with the widest powers for the ordinary and extraordinary business of the Company and, specifically, it has the authority to carry out all the acts which it deems expedient for the fulfillment and achievement of the corporate purpose, excluding only those acts which the law and the By-laws reserve for the shareholders in general meeting.

Chairman of the Board of Directors

Pursuant to the By-laws, the Chairman is empowered to legally represent the Company and sign on its behalf, chair the general meetings, call and chair the Board of Directors and verify the implementation of the resolutions adopted by said Board. On the basis of the Board resolution dated November 2, 2005, the Chairman is also acknowledged certain powers of a non-operational nature.

Chief Executive Officer

The Chief Executive Officer is also empowered to legally represent the Company and sign on its behalf as a result of the By-laws, and is also vested, on the basis of the Board resolution dated November 2, 2005, with all the powers for the administration of the Company, with the exception of those otherwise assigned by the law, by the By-laws or reserved for the Board of Directors in accordance with the same resolution.

TERNA MANAGEMENT



Terna has endowed itself with a new organizational structure so as to seize as fully as possible all the opportunities and synergies of a genuine integrated operator deriving from the integration with the activities of the national transmission grid operator. The managers are required to pursue objectives of safety, reliability and efficiency of the transmission and dispatch service, operating on the basis of neutrality and impartiality with respect to the other operators in the electricity sector and at the same time creating value for the shareholders and the communities within which Terna operates.



From left to right:

1. FRANCESCO DEL PIZZO *Systems and Technologies Director*, **2.** LUIGI DE FRANCISCI *Regulatory Affairs Director*, **3.** STEFANO CONTI *Institutional Affairs Director*, **4.** ELISABETTA COLACCHIA *Investor Relations Manager*, **5.** LUCA D'AGNESE *Italy Operations Director*, **6.** MASSIMO CIOFFI *Human Resource and Organization Director*, **7.** FILOMENA PASSEGGIO *Corporate Secretary and Legal Department Director*, **8.** GIACOMO DONNINI *Settlement Manager*, **9.** ALESSANDRO FIOCCO *Business Development and International Director*, **10.** FLAVIO CATTANEO *Chief Executive Officer*, **11.** LUIGI CELANI *Procurement Director*, **12.** LUIGI ROTH *Chairman*, **13.** GIANNI ARMANI *Grid Planning and Development Director*, **14.** GIOVANNI BUTTITTA *External Relation and Communication Director*, **15.** UMBERTO COLONNA *Plant Maintenance Director*, **16.** EVARISTO DI BARTOLOMEO *Engineering Director*, **17.** FABIO TODESCHINI *Chief Financial Officer*, **18.** LUCIANO DI BACCO *Administration and Fiscal Manager*, **19.** FULVIO DE LUCA *Internal Audit Manager*, **20.** CARLO SABELLI *Dispatching Manager*.

TERNA - THE COMPANY

Terna - the business

In Italian, the name Terna (Circuit) indicates the main element which makes up an electricity line, in other words the series of three conductors or wires. The Company logo also represents the flows of electricity which intersect on the transmission grid. Terna is the company responsible for the transmission and dispatch of electricity on the high and extra high voltage grid in Italy. By means of the ownership and management of the National Transmission Grid, Terna guarantees the quality of the services, the safety of and access to the grid, all conditions being equal, by the sector operators. It takes steps to develop and maintain the grid respecting the environment, combining skills and technologies for improving quality and efficiency.

The Terna story

Terna – Rete Elettrica Nazionale SpA has for years been an industrial and service entity for the country. The changes within the energy scenario over the last year, including the process for the deregulation of the electricity market, the privatization of its grid, the appearance of a variety of market competitors in Italy and abroad, once again see Terna among the leading players within the national energy scenario. The unification between ownership and management of the National Transmission Grid, which became operative as of November 1, and the appointment of the new Board of Directors and Luigi Roth and Flavio Cattaneo, respectively Chairman and Chief Executive Officer, signal the launch of the new route of an entity which comes from afar.

The main stages of its recent history are briefly mentioned:

May 31, 1999: the company Terna is established within the Enel Group, by way of implementation of Italian Legislative Decree No. 79/99 ("Bersani Decree") which within the context of the process for the deregulation of the Italian electricity sector, sanctioned the separation between ownership and management of the national transmission grid. Terna's activities, operative as from October 1, of the same year, concern the running and maintenance of the Enel Group installations belonging to the national transmission grid, and the development of the grid itself in accordance with the directives imparted by GRTN (National Transmission Grid operator).

October 27, 2003: Italian Law No. 290 is issued, which provides for the unification of the ownership and the management of the national transmission grid.

May 11, 2004: the Prime Minister's Decree is issued which establishes the criteria, formalities and conditions relating to the unification between the ownership and the management of the national transmission grid, and the corporate governance system.

June 23, 2004: 50% of Terna's share capital is listed on the Borsa Italiana screen-based stockmarket.

February 28, 2005: the Terna-GRTN agreement is entered into for the transfer of the GRTN business segment concerning the electricity transmission and dispatch activities.

March 31, 2005: Enel transfers a 13.86% interest in Terna's share capital to institutional investors.

April 20, 2005: the Ministry for Production Activities issues new Concessions for the performance of electricity transmission and dispatch activities throughout Italy.

May 24, 2005: the grid transmission, dispatch, development and safety code (so-called "Grid Code"), envisaged by the Prime Minister's Decree dated May 11, 2004, enters into force.

September 15, 2005: Enel transfers 29.99% of Terna's share capital to Cassa Depositi e Prestiti: the shareholding structure of the Company adopts the current structure.

October 1, 2005: efficacy of the transfer to Terna of Acea Trasmissione (re-named Rete di Trasmissione Locale SpA - (R.T.L. SpA).

November 1, 2005: the unification between the ownership and management of the transmission grid becomes operative: Terna - Rete Elettrica Nazionale SpA is formed.

November 2, 2005: the shareholders' meeting appoints the new Terna Board of Directors for the three-year period 2005-2007; Luigi Roth and Flavio Cattaneo are respectively appointed as Chairman and Chief Executive Officer.

December 21, 2005: Terna's Board of Directors approves the new organizational structure and launches the NTG Development Plan for the period 2006-2015.



Ownership and management: a sole point of reference

The independence of the grid is fundamental in the new phase for the deregulation of the electricity scenario. Just as the re-unification between ownership and management of the grid guarantees the tertiary requirements of a national operator. Italy is among the European countries which are the first to implement the action necessary for the process of creating an integrated operator, which plans and achieves investments in safety coordinating the structural requirements with the possible responses for the market. The objectives of the unification include: ensuring greater efficiency, safety and reliability of the national electricity system as well as encouraging the development of the transport capacity of the transmission grid and improving the safety and the inexpensiveness of the national electricity system. The independence and autonomy of the company are guaranteed by means of precise limits set with regards to equity investments in the same. The current Terna shareholding structure guarantees independence and autonomy in the management of the grid infrastructures, in accordance with the matters envisaged by the national and European legislator.

The benefits of unification

- **greater independence** of the owner/operator of the national transmission grid, safeguarding both the users and the investors interested in entering the sector. The recent adoption by Terna of the Grid transmission, dispatch, development and safety code is an example of such transparency, a code which indicates specific and clear rules and procedures for the operators and for all the users of the national transmission grid.
- **improved organization** with regards to the grid maintenance and development activities, making it possible to integrate the planning and achievement of the measures within a single company.
- **greater efficiency**, also by means of the reduction of the operative management costs of the national transmission grid.
- **greater safety and reliability** of the Italian electricity system.
- **greater transmission capacity** for increasingly greater safety of the supplies and service continuity, with standards as uniform as possible for all areas of the country.





More skills, more areas of intervention

The national electricity transmission grid is complex and extremely widespread: the Italian grid in fact comprises in total 44,447 km of electricity lines and 341 transforming and switching stations and includes all the **extra high voltage** grid (equalling to 21,539 km of alternated voltage lines, 1,176 km of continual voltage lines and 263 stations) and part of the **high voltage** grid (equalling to 21,373 km of alternated voltage lines and 78 stations), in addition to 18 **interconnection** lines which permit the exchange of electricity with foreign countries.

Such a structured entity therefore needs operating abilities which range over various levels. Terna responds effectively to this need, each day, operating essentially in three areas of activities:

Development of the grid

Terna decides to carry out development measures on the national transmission grid. The new 2006-2015 Development Plan envisages the creation of 3,300 km of new electricity lines and 60 new stations, involving a total investment of € 3.1 billion.

Management of the electricity system

Terna guarantees the balance between the energy requested and that produced. The safe management of the national electricity system is carried out by the National Control Center and the Territorial Operating Areas. By means of the Remote Control centers, Terna works its plants and monitors the running.

Engineering and the management of the plants

Terna ensures the maximum efficiency of the infrastructures and the excellence of the maintenance by means of a strong vocation towards technological innovation and an operating structure present throughout the entire territory.

An entity of international proportions

In Italy, Terna is the owner of more than 90% of the National Transmission Grid, in other words the high and extra high voltage network. In particular, Terna owns:

- 35.129 km of electricity lines
 - 380 kV lines: 9.538 km
 - 220 kV lines: 8.053 km
 - <150 kV lines: 17.538 km
- 302 transforming and switching stations
- 3 remote control centers

The elements making up the grid include: the EHV (extra high voltage) transformers which withdraw electricity from the national electricity power stations (or from border points for imported energy); the EHV and HV (high voltage) lines which transport the energy; and, lastly, the transforming stations which supply the energy to the distribution companies which, in turn (via trading companies), convey the electricity to homes and factories. Furthermore, Terna also operates outside Italy. Since 2003, it also controls two Brazilian companies, Novatrans Energia S.A. and TSN - Transmissora Sudeste - Nordeste S.A., operating in the energy transmission sector in Brazil. Each company holds a thirty-year concession by virtue of which it is authorized to carry out the same activities which Terna exercises in Italy. What is more, in December 2005, a contract was signed for the purchase of the Brazilian company Munirah, the concession holder of 106 Km of transmission lines in the state of Bahia.

The management of the 2,340 km of 500 kV connections under thirty-year concession is divided up as follows:

- 1.077 km managed by TSN
- 1.278 managed by Novatrans

Furthermore, the two Brazilian subsidiary companies also manage 13 electricity stations:

- 7 electricity stations run by TSN
- 6 electricity stations run by Novatrans





More energy in the environmental and social commitment

Terna has been confirmed in the FTSE4GOOD EUROPE, the prestigious stockmarket index of the Financial Times Stock Exchange in London which groups together the best European countries distinguishing themselves with regards to sustainable economic growth.

The criteria for admission assess the commitments made and the results achieved by the companies in the environmental (environmental management policies and systems) and social spheres (systems for managing the relations and collaboration activities with the stakeholders) and in terms of observance and safeguarding of human rights.

In short, these are the main commitments of Terna vis-à-vis the environment and the quality of life:

- Rationalization of works throughout the territory within a logic of sharing of the projects with the stakeholders.
- Realization of pylons with an innovative design, conceived so as to be perceived no longer as just industrial man-made items.
- Project for obtaining ISO 14001 standard certification for the stations, for the entire national transmission grid.
- Reductions in the emissions of the electromagnetic fields by means of the reconfiguration layout of the conductors (with consequent development of new types of pylons) and the addition of passive compensation circuits.
- Application of new solutions via buried cables with extruded insulation for extra high voltage (220 kV-380 kV).

Terna - the numbers

The numbers can be important for understanding the dimension and the work of a company. Therefore, here are the most representative numbers for comprehending Terna:

0,4	km: the length of the shortest 380 kV line ("Ostiglia-Ostiglia C.le", in Lombardy)
1	National Control Center
1	Central Headquarters in Rome
1	investee company in Italy
2	subsidiary companies in Brazil
2	sub-marine interconnection lines (Italy-Greece and Italy-Corsica)
3	Remote Control Centers
8	Territorial Operating Areas (AOT)
9	the percentage of women employees
16	interconnection lines on the north border
46	average age of employees
73	wire inside a conductor or electrical cable
90	and over, the percentage of ownership of the national transmission grid
91	the percentage of men employees





196	km the length of the longest 380 kV line ("Fiumesanto - Selargius", in Sardinia)
276	engineers
302	transforming and switching stations
329,4	billion kilowatt hours requested in Italy during 2005
572	transformers
1.000	megawatts: the transport capacity of the most powerful lines
1.098	blue-collar workers and technicians
3.442	employees (Italy and Brazil)
3.947	bays
8.053	km of 220 kV electricity lines
9.538	km of 380 kV electricity lines
17.538	km of 150 kV electricity lines
35.129	km of total transmission lines (around three times the land's diameters)
55.015	megawatts the national requirement on December 20 ,2005 (all-time record)
108.209	MVA (MegaVoltAmpere) of transformer capacity
600.000	tons of iron of the trestlework which make up the Terna grid (82 times greater than the quantity of iron comprising the Eiffel tower)
2.000.000.000	investments in Euro envisaged in the 2006-2010 Business Plan

TERNA HIGHLIGHTS

The National Control Center

The nerve center of the entire Italian electricity system

Located in Rome, at an high security site, it is operative 24/7 365 days a year: in the central control room one can gain an overall view of the entire high and extra high voltage electricity grid in Italy. The energy controlled over a period of a year at the National Control Center amounts to more than 330 billion KWh. The flow of energy produced in Italy and imported from abroad is controlled instant by instant here, and the transmission of energy under safe conditions is handled and guaranteed every day here, implementing action for balancing electricity supply and demand in Italy.



over

330 billion
KWh

of energy managed a year

The organization

The structure and the human resources

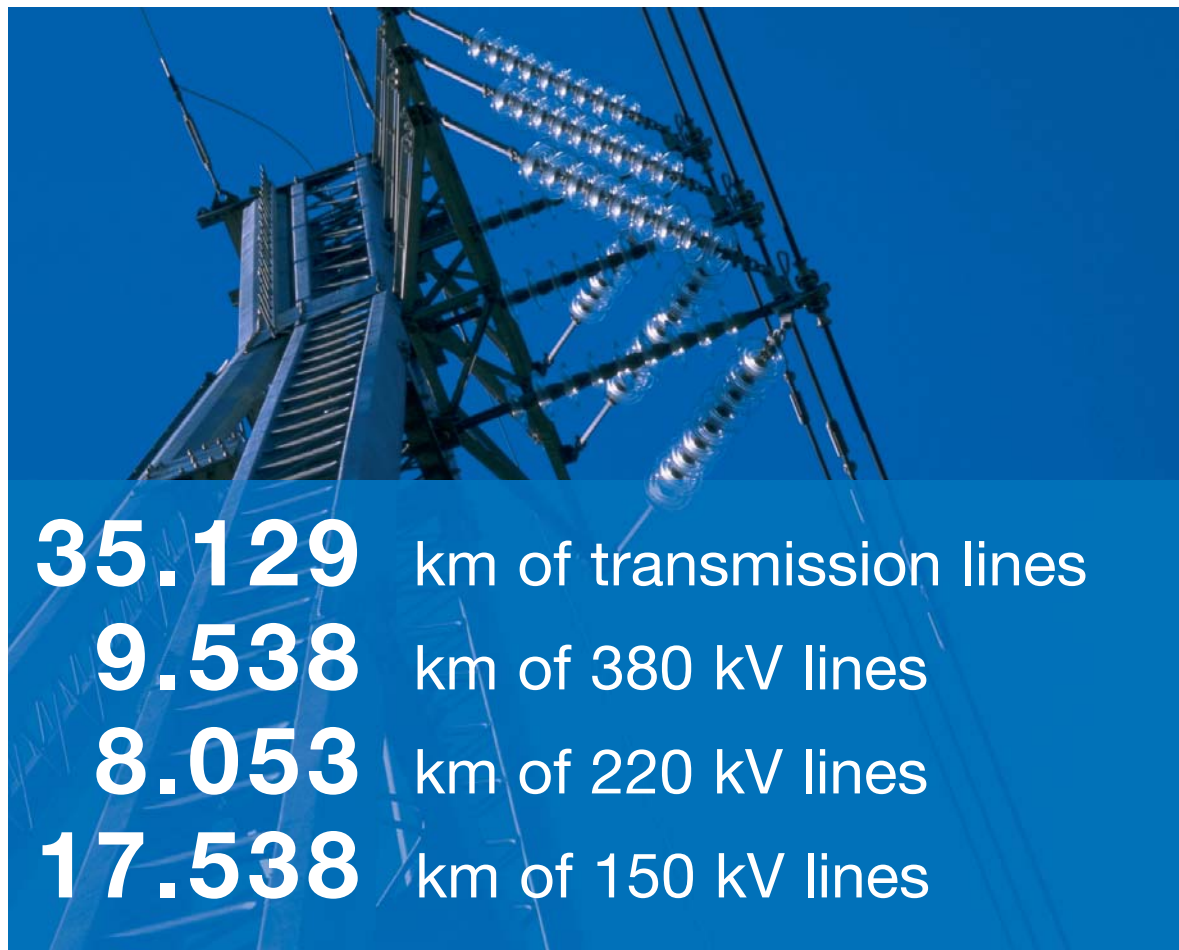
Owners of the national grid and with an international bent, the Terna Group comprises an investee Company in Italy and two important subsidiary companies, Novatrans Energia S.A. and TSN - Transmissora Sudeste - Nordeste S.A., which operate in the energy transmission sector in Brazil. Its individuals are Terna's most important capital. A great team, 3,442 employees split between Italy and Brazil, motivated by the passion and the awareness of the deep social value of their work, undergoing continual human and professional growth.



The grid

High voltage electricity lines

An electricity power line is a system which links two electricity stations, or a station and a point where electricity enters or leaves the system. It is formed of electrical conductors (three-phase alternating conductors, power lines, one or two direct current conductors, etc.), support structures (pylons, insulators, etc.) for overhead lines, protection cables and other components needed for the proper electrical and mechanical operation of the plant. A line normally carries one or more electrical power lines (single- or double-power lines). The length of a power line (linear kilometers) is expressed as the length of the projection of the power line on the ground (geographical length).



High voltage electricity stations

An electricity transport station is part of an electricity grid. Located in a specific part of the grid, it is used to dispatch electricity among the various power lines in the grid and to transfer electricity between different voltage grids. In Italy, Terna possesses 302 EHV and HV power stations. These stations are another strong point of a service which, once again in 2005, is marked by the leading quality indicators in relation to its extremely high levels. A result obtained thanks to the organization, procedures, work methods and the technological innovations which have also provided an on-going containment of the cost of the activities.



99,26% this is the result according to the **ASA** (Average System Availability) quality key which gauges the average real availability of all the grid elements in the period under review

0,681 min/year this is the result according to the **AIT** quality key (Average Interruption Time) which gauges the average time of electricity system supply interruption in the period under review

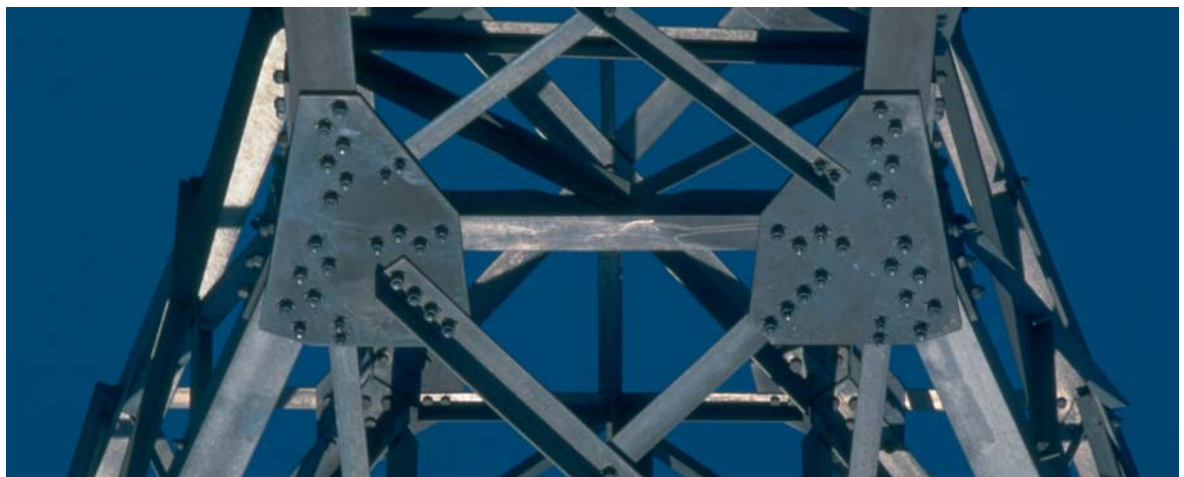
0,18 this is the result according to the **SAIFI** (System Average Interruption Frequency Index) quality key which gauges the average number of supply interruptions per consumer connected to the grid in the period under review.

The works

Interconnection electricity power line between Italy and Switzerland “S. Fiorano-Robbia

The first large infrastructural measure in the Alpine area since 1986

It is the first new interconnection electricity power line connected with abroad passing through the Alpine area, created since 1986 and entered into service in 2005. The last power line which entered into service on the northern border dates back to the “Rondissone - Albertville” power line, between Italy and France. From a technical point of view, the power line, built by Terna measures **46 km**, involving a total of 123 supports and 1,600 tons of conductors. The cost of the investment amounts to approximately € **60 million**. Work started in May 2004 and was completed in just **7 months**, compared with the 12 months usually required,, involving an average of **260** human resources a day and **5 helicopters** for transporting the structures.

**46**

Km of power lines

60

Mln € the cost of the investment

260

human resources a day

1.100

MW import capacity

In short, here are the benefits the electricity power line features:

- Increase in the import capacity of 1,100 Megawatts, taking the total to 7,150 Megawatts (+ 15%).
- Progressive reduction of the costs, due to the price differential of the electricity between Italy and the majority of the European countries, for businesses and families.
- Increase in the safety of the service.

During 2005, the following lines also entered into service

- “**Rizziconi - Laino**”, which runs through the whole of Calabria for more than 200 km.
- “**La Spezia - Acciaio**”, between Liguria and Tuscany, running 100 km.



Extend and rationalize the National Transmission Grid. This is the challenge for enhancing the infrastructures of the electricity system which create economic growth and make it possible to improve the safety of the service, reduce the energy costs, and produce benefits for businesses and Italian families.

The planning stage of an infrastructure must follow and not precede the dialogue stage. For this reason, Terna, via an innovative SEA (Strategic Environmental Assessment) instrument, launches throughout the area a phase of harmonization and sharing with all the stakeholders before proceeding with the planning and design.

TERNA AND THE FINANCIAL MARKETS

During 2005, Terna stock was essentially influenced by two factors, which occurred respectively in February and October and then affected the subsequent months' performances. After an initial appreciation of the share price, which on February 11 touched the all-time-high listing of € 2.331, from mid February the stock suffered a drop partly coinciding with the recovery of bond market prices; the stock of the companies belonging to the utilities sector in fact are often considered as alternative investment to bonds, due to their defensive nature.

At the end of September, news of the introduction of the so-called "pipe tax", subsequently cancelled and replaced by legislation which disciplines the depreciation of tangible operating assets for the exercise of

STOCK MARKET AND SHARE HIGHLIGHTS

In Euro	2005
Unit dividend ⁽¹⁾	0,13
Maximum price	2,331
Minimum price	1,951
Average price for December	2,08
Stockmarket capitalization ⁽²⁾ (in millions of Euro)	4.161
No. of shares (in millions of Euro)	2.000

⁽¹⁾ Of which Euro 0.05 distributed as an interim payment on November 24, 2005 and Euro 0.08 distributed on June 22, 2006

⁽²⁾ Calculated on the average price for December 2005

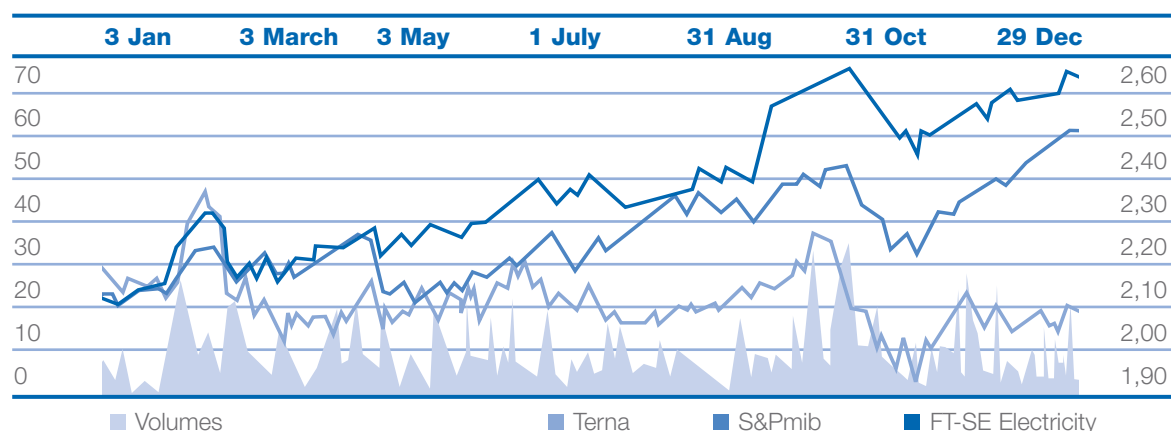
FINANCIAL RATIOS

		2005
TERNA SHARE WEIGHT ⁽³⁾		
on the MIB30 index (%)		0,87%
on the S&P/MIB index (%)		0,82%
RATING		
Standard & Poor's	Outlook	stable
	M/L term	AA-
	Short-term	A1+
Moody's ⁽⁴⁾	Outlook	stable
	M/L term	Aa3
	Short-term	Prime1

⁽³⁾ Source: Borsa Italiana. Figures at December 30, 2005

⁽⁴⁾ On January 31, 2006, Moody's placed the M/L-term rating under observation (credit watch) for a possible drop

TERNA STOCK AND S&PMIB & FT-SE ELECTRICITY INDEX PERFORMANCE



regulated activities in the electricity sector, produced a considerable retrenchment of the stock, which continued to be heavily penalized for the entire month of October. Overall, Terna closed 2005 with a performance which was down slightly (approximately - 2%), passing from a value of € 2.125 (January 3) to a value of € 2.084 per share (December 30). During the same period, the S&PMib (reference index for the Italian market) and the FT-SE Electricity index (the average of the other listed European electricity companies) reported an increase of around 15 and 20 percentage points, respectively.

The increase with respect to the placement price (€ 1.70 per share) came to 23%, which compares with a change of 28% in the S&PMib index and 33% in the FT-SE Electricity index. Average daily volumes traded during the year came to around 12 million shares, or 0.61% of the share capital, up with respect to the average daily volumes in 2004 (approximately 10 million shares).

The balance of the dividend for 2004 was paid to the shareholders on May 26, 2005, equalling to € 0.070 per share, while on November 24, 2005 the advance on the dividend relating to 2005 was paid, amounting to € 0.050 per share.

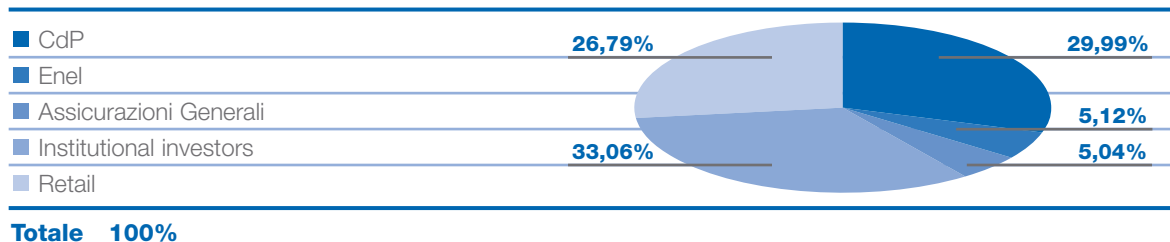
For further information, please visit the website www.terna.it in the section Investor Relations where the following can be found: economic-financial data, presentations, updates in real time on the stock performance, information relating to the composition of the corporate boards and the general shareholder, meeting regulations as well as periodic updates concerning Corporate Governance evolution. Furthermore, points of contact specifically dedicated to non-institutional investors (phone numbers: 06.8313.8136 and 06.8313.8206; e-mail address: azionisti.retail@terna.it) and institutional investors (phone number: 06.8313.8145; e-mail address: investor.relations@terna.it) have also been set up.

Shareholding structure

Terna SpA's share capital amounts to € 440 million and is represented by 2,000,000,000 ordinary shares with a par value of € 0.22 each. During 2005, Enel SpA reduced its equity investment in Terna SpA first of all by selling 277,162,000 Terna SpA ordinary shares, representing 13.86% of the share capital, by means of an accelerated bookbuilding procedure with Italian and foreign institutional investors (March 31, 2005). Subsequently, it sold 29.99% of Terna SpA's share capital to Cassa Depositi e Prestiti SpA, equalling to 599,999,999 shares (September 15, 2005). At present, Enel SpA's equity investment in Terna SpA comes to around 5.12% of the share capital.

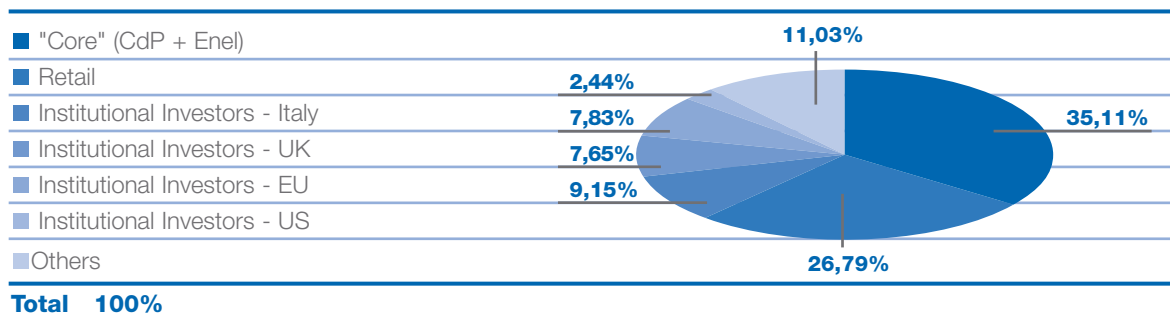
On the basis of the results of the Shareholders' Register and other information gathered as of the date of drawing up these financial statements, Terna's shareholding structure is as follows:

TERNA SHAREHOLDING STRUCTURE



In detail, the composition of the Company's institutional shareholding structure includes leading Italian and foreign investment funds with a significant presence of investors from the United Kingdom and the rest of Europe.

TERNA SHAREHOLDING STRUCTURE BY TYPE AND GEOGRAPHIC AREA





HAVING VALUES CREATES VALUE





STATUTORY FINANCIAL STATEMENTS OF Terna SPA 2005

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REPORT ON OPERATIONS OF TERNA SPA

INTRODUCTION

By virtue of the options proposed by Italian Legislative Decree No. 38/2005, Terna SpA opted not to use the IFRS international accounting standards for the preparation of the statutory financial statements as of December 31, 2005. The financial statements as of December 31, 2005 of the Parent Company Terna SpA have therefore been drawn up in accordance with Italian accounting principles. The year 2005 was characterized by extremely important corporate events for Terna which effectively increase its responsibility, since it is required to pursue the objectives of safety, reliability, efficiency and lower transmission and dispatch service costs, operating neutrally and impartially with respect to the other operators in the electricity sector. Such events can be summed up in the acquisition of the TSO business segment sold off by GRTN SpA, finalized following the acquisition by Cassa Depositi e Prestiti SpA of 29.99% of Terna's share capital, which led to a loss in the Enel Group's control over the Company. On November 1, 2005, coinciding with the date of transfer of the TSO business segment's activities, Terna thus became the concession holder for the transmission and dispatch activities. The business segment transferred comprises the following:

- the dispatching activities, or rather the management of the flows introduced and withdrawn from the NTG in order to balance electricity supply and demand;
- the planning and development activities, or rather the definition of the investment programmes for enhancing the NTG.

The management of the dispatch flows determines an enormous impact in terms of costs and revenues for the purchase and sale of electricity both within and outside the scope of the Stock Exchange. It is important to emphasise that such moves do not have an impact on the result for the year since the total of the energy costs and revenues relating to dispatching are offset in full.

The income statement and balance sheet as of December 31, 2005 have been affected by the activities carried out, for the last two months of the accounting period, in the new consolidated capacity of management and ownership of the national transmission grid. However, this report contains all the information, in addition to comments, on the energy aspects pertaining to the management of dispatch activities for the whole of 2005, with particular reference to the energy budget in Italy.

As a result of the transfer of the TSO business segment, as from November 1, 2005 Terna acquired the equity investments held by the ISO (GRTN SpA) in the share capital of CESI SpA (equalling to 9.36%). Following this acquisition, Terna's entire investment in CESI's share capital rose to 24.36%.

HIGHLIGHTS

	2005	2004	Change
ENERGY DATA (GWh)			
Net electricity generated	289,655	290,022	-367
Imports	49,155	45,635	3,520
Electricity required	329,441	325,357	4,084
Maximum output required (MW)	55,015	53,606	1,409
ECONOMIC AND FINANCIAL FIGURES FROM THE STATUTORY FINANCIAL STATEMENTS (In millions of Euro)			
Revenues	908.1	905.6	2.5
Gross operating margin	604.8	600.9	3.9
Operating income	446.4	447.1	-0.7
Net income	268.0	252.9*	15.1
Fixed assets, net	4,455.5	4,157.1	298.4
Net working capital	-187.5	-200.6	13.1
Net invested capital	3,710.1	3,406.2	303.9
Employee termination indemnity, taxation, risks and charges	557.9	550.3	7.6
Shareholders' equity	1,866.0	1,838.0	28.0
Net financial position	1,844.1	1,568.2	275.9
Investments	259.4	277.8	-18.4
OTHER DATA AND RATIOS			
Average employee numbers	2,966	2,882	84
Employees as of December 31	3,388	2,871	517
Net income per share	0.134	0.126	0.008

*Net of the effects of the tax clean-up

SIGNIFICANT EVENTS IN 2005

Acquisition of the TSO business segment

On February 28, 2005 Terna SpA and Gestore della Rete di Trasmissione Nazionale SpA (GRTN), in observance of the matters laid down by the Prime Minister's Decree dated May 11, 2004, signed the agreement for the transfer to Terna of the GRTN business segment, comprising the activities, functions, assets and legal relationships as indicated by the same Prime Minister's Decree. The purpose of the agreement is to integrate the ownership and management of the NTG. The business segment being transferred includes 586 resources, and includes:

- The dispatching activities, or rather the management of the flows introduced and withdrawn from the NTG in order to balance electricity supply and demand;
- The planning and development activities, or rather the definition of the investment programmes for enhancing the NTG.

The parties have agreed a price of € 68.3 million for the transfer of the business segment, net of approximately € 112 million in trade payables due to Terna. The overall valorisation of the business segment transferred therefore amounts to € 180 million.

The date of efficacy of the unification between the ownership and management of the NTG is deferred until the occurrence of the following abeyance conditions:

- The new concession by the Ministry of Production Activities for the performance of the electricity transmission and dispatching activities within the national territory belonging to Terna;
- The approval, by the Ministry of Production Activities and the Energy Authority, of the Grid Code anticipated by the Prime Minister's Decree;
- The issuance by the Antitrust Authority of a favourable opinion on the transaction.

The first two abeyance conditions have taken place, respectively on April 20, 2005 and May 3, 2005. With regards to the third condition, as of June 22, 2005 the Antitrust Authority launched a preliminary investigation into the acquisition by Cassa Depositi e Prestiti of 29.99% of Terna's share capital, as well as into the acquisition by the latter of the GRTN business segment.

By means of Ruling No. 14542 dated August 4, 2005, communicated to the parties on August 5, 2005, the Antitrust Authority issued its authorization for the acquisition, by the company Cassa Depositi e Prestiti (CdP), of 29.99% of the share capital of Terna and of the GRTN business segment, obliging CDP to observe the following measures:

- The transfer, as from July 1, 2007 and within the subsequent 24 months, by CDP of the equity investment held in ENEL SpA, as well as

- Provisionally and until the satisfaction of the afore-mentioned condition, the undertaking of the following commitments:
 - approval by the new Terna Board of Directors of a resolution which lays down suitable procedures for enhancing the role of the Advisory Committee pursuant to Article 1 of the Prime Minister's Decree dated May 11, 2004 in relation to the adoption and implementation of the NTG development plans;
 - appointment of at least six of the seven Terna directors, due to CDP in the event of a Board of Directors comprising ten members, who are independents.

Consequently, Terna SpA's Board of Directors, which met on September 15, verified the achievement of all the conditions envisaged by the contract and the establishment of November 1, 2005 as the date of efficacy of the transfer to Terna of the Gestore della Rete di Trasmissione Nazionale SpA (GRTN) business segment, and called, for November 1 (in first calling) and for November 2 (in second calling), the Ordinary Shareholders' meeting for the renewal of the Board of Directors since its mandate was due to expire. Therefore, the shareholders' meeting held on November 2, 2005 appointed the new Board of Directors in observance of the matters envisaged by the Prime Minister's Decree and the ruling of the Antitrust Authority. Shareholders are informed that, on this occasion the Article of Association amendments required by the Prime Minister's Decree and approved by the extraordinary shareholders' meeting held on January 31, 2005, destined to be enforced in concurrence with the efficacy of the integration of the ownership and management of the NTG, were applied for the first time. The most important of these Article of Association amendments, at the time of the renewal of the Board of Directors, involves:

- The establishment to the charge of the electricity sector operators of a limit, equalling to 5% of the share capital, with regards to the exercise of the voting right when appointing the Directors;
- The foreseeing of special respectability, professionalism and independence requisites for the Directors.

Consequently, Terna amended its organizational structure; the related details are illustrated in the "Human Resources" section of this report.

EIB loan

During March 2005, the Company obtained a line of credit from the European Investment Bank (EIB) for a total of € 300 million. On March 15, the first portion of € 100 million was disbursed. The loan anticipates a period of grace of 4 years and a repayment period of 11 years, involving straight-line six-monthly instalments. The residual part can be disbursed up until December 31, 2006. The annual loan cost will be equal to a margin of 12 basis points to be added to the rate from period to period determined by the Bank which in any event cannot exceed in total the Euribor rate plus 27 basis points for the entire duration of the loan.

Acea Trasmissione

On August 8, Terna and Acea SpA (Acea) signed a contract for the purchase by Terna of the entire share capital of Acea Trasmissione SpA (Acea Trasmissione), a company wholly-owned by Acea.

Acea Trasmissione is the owner of approximately 700 km of high voltage transmission lines in Lazio, Umbria and Abruzzo and ensures the maintenance and development of the portion of the NTG it owns.

By means of this acquisition, Terna launched the process for the unification of the National Transmission Grid anticipated by Italian Law No. 290/2003 concerning the reorganization of the electricity sector and by the subsequent Prime Minister's Decree dated May 11, 2004.

The parties have agreed a fee of € 32.9 million for the transfer of the Acea Trasmissione equity investment. After having received the approval of the Antitrust Authority, the transaction was finalized on September 30, and was effective as from October 1, 2005.

The company has adopted the corporate name of "R.T.L. - Rete di Trasmissione Locale Società per Azioni (RTL SpA).

2005 advance dividend payment

On September 7, 2005, having obtained the opinion of the independent auditing firm KPMG envisaged by Article 2433 bis of the Italian Civil Code, the Board of Directors resolved the distribution of an advance payment on the dividend for 2005.

Taking into account that during the first half of 2005, Terna SpA achieved net income of € 138.6 million, the Board of Directors, partly in light of the outlook for the current year, resolved the distribution of an advance payment on the dividend totalling € 100 million, equivalent to € 0.05 per share.

The advance payment on the dividend, gross of any legal withholdings, was paid on November 24, 2005, subject to detachment on November 21, 2005 of coupon No. 3.

Transfer by ENEL SpA of 29.99% of Terna's share capital to Cassa Depositi e Prestiti SpA

On September 15, Enel SpA transferred to Cassa Depositi e Prestiti SpA 29.99% of Terna's share capital (equalling to 599,999,999 shares) against a payment of € 1,315 million, established on the basis of the criteria fixed in the agreement stipulated between the parties on May 23 last.

Grid Code

The Prime Minister's Decree dated May 11, 2004, in laying down the formalities for the re-unification between the ownership and management of the national transmission grid, also anticipated the definition of a supplementary document entitled "The Grid transmission, dispatch, development and safety Code" (the so-called Grid Code) which contains the technical regulations of an objective and non-discriminatory nature for accessing and using the grid, for the inter-operable nature of the grid and for the supply of the dispatching service, as well as the general criteria for the development and defence of the safety of the national electricity grid and for the maintenance measures.

The grid code, drawn up in compliance with the Prime Minister's Decree, was positively assessed by the Ministry of Production Activities and by the Electricity and Gas Authority, the latter by means of resolution No. 79/05, and is applicable as from November 1, 2005 with regards to the dealings between Terna and the grid users.

In particular, the Authority's resolution on the one hand made the Code's approval subordinate to the acknowledgement of a number of precise observations which were promptly followed through, and on the other hand invited Terna to make a more complete review of the document on the basis of several comments made by the same Authority and on the basis of the first period of experimentation of the document by November 30 2005. Within the time-limits envisaged by the resolution, Terna forwarded the updated document to the Authority and the Ministry for the related approval. By means of resolution No. 49/06, the Authority positively assessed the updated version of the Grid Code provided that a number of comments were acknowledged.

As is known, the Code anticipates the formation of a users' consultation Committee which is assigned functions of an advisory and proposal nature essentially at the time of the updating of the Grid Code. Furthermore, the Committee may express non-binding opinions on general criteria for the development of the grid, the interconnections, the defence of the safety of the grid, as well as on general criteria for the classification of sensitive information and access to the same.

In this connection, Terna has taken steps to request the associations representing the various categories of users, as identified by the Ministry of Production Activities, to appoint its own representative on the Committee. Just as soon as the representatives have been appointed, the Committee can be established and start its activities.

The new Concession

So as to complete the framework of the normative and regulatory amendments for the year 2005 linked to the unification of the ownership and management of the national transmission grid, the Concession of the

electricity transmission and dispatching activities within the national territory took place, as approved by the Ministry of Production Activities by means of decree dated April 20, 2005.

The concession has a duration of 25 years, is renewable for an identical period, and a five-year review is anticipated of some of the provisions contained therein, especially those concerning grid scheduling, maintenance, management and development.

The concession defines the content matter of the activities disciplined, establishing spheres and limits for the performance of the same. In short, in addition to the aspects associated with the concession performance formalities (revocation of the concession, sanctions, amendments, etc.) the concession disciplines:

- The activities for the development of the national transmission grid, both with regards to scheduling, foreseeing formalities and timescales for the approval of the Development plan and laying down the main content of the same, and with regards to the method for achieving the measures;
- The grid maintenance and management activities, including therein action for the pursuit of the safety objectives (Programme for the adaptation and improvement of the defence systems);
- Corporate equity investments and new acquisitions in the electricity sector and in different sectors;
- The dealings with authorities and external parties, including therein dealings with the operators of interconnected grids.

Tariff review for 2006

By means of resolution No. 202/05 dated September 29, 2005, the Electricity and Gas Authority established the 2006 review of the transmission service tariffs.

This review was carried out by the Electricity and Gas Authority in accordance with the Supplementary Act pursuant to resolution No. 05/04, specifically taking into consideration:

- The portion of the tariff intended to cover operating costs and the amortization/depreciation, the rate of change in the consumer price index for families of blue and white-collar workers reported by ISTAT (Central Statistics Institute) in the previous twelve months equalling to 1.8%;
- The portion of the tariff intended to remunerate the RAB, average annual rate of change of the deflatory factor for fixed gross investments reported by ISTAT (Central Statistics Institute) equalling to 3.9%, the expected rate of change of the electricity demand volumes in Italy equal to 1.5%, as well as the data transmitted by the individual owners relating the growth investments which came into service by June 30, 2005.

On the basis of the conjecture illustrated above and the Electricity and Gas Authority having deemed it appropriate to align the electricity estimates made in the various time bands F1, F2, F3 and F4 with the electricity

requirements effectively noted in 2004, the tariffs components paid by the distributors and by the producers for the remuneration of the transmission service were thus adjusted when compared with those for 2005:

Euro cent/kWh	2005	2006
Fee due by the producers	0.0254	0.0259
Fee due by the distributors for time band F1	0.77	0.82
Fee due by the distributors for time band F2	0.49	0.53
Fee due by the distributors for time band F3	0.32	0.35
Fee due by the distributors for time band F4	0.14	0.16
Tariff component covering the costs of the GRTN	0.0336	0.0333

As far as the tariff component covering the costs of the GRTN was concerned, shareholders are informed that, in accordance with the matters anticipated by the Electricity and Gas Authority Resolution No. 15/05, the portion of € cent/kWh 0.0238 concerns the coverage of the costs of the TSO business segment which was transferred on November 1, 2005 to Terna.

SUBSIDIARY COMPANIES

Brazil

Significant events

On December 15, Transmissora Sudeste Nordeste S.A. ("TSN") signed an agreement with the companies Control Y Montajes Industriales CYMI S.A. and Fluxo Engenharia Ltda for the acquisition of the entire share capital of Munirah Transmissora de Energia S.A. ("Munirah"). Munirah is the concession holder of 106 km of transmission lines and two sub-stations in the State of Bahia, operative as from last October, which represent the extension of TSN's 500 kV lines closing the North-North-east circuit. The price for 100% of the company's share capital was set at Reais 48 million (around € 17 million). The concession, which the company holds, envisaged annual revenues of Reais 18 million (approximately € 6 million). The closure of the transaction is anticipated for the end of March 2006 and is subject to approval by the local regulatory authority ANEEL and the authorization of BNDES, the bank financing both TSN and Munirah.

ANEEL resolutions and authorizations

On June 30, 2005 ANEEL established the new values of the Concession Fee (RAP) in force as from July 1, 2005 until June 30, 2006. The TSN and Novatrans fees were respectively set at R\$ 245 million and R\$ 269 million, reflecting the adjustment for inflation (IGPM rate) accumulated between June 2004 and May 2005, equalling to 9.0752%. ANEEL also acknowledged an additional one-off increase, to be received in 12 monthly instalments as from July 2005 relating mainly to the adjustment for the additional PIS/COFINS rates paid by the companies up until May 30, 2005, amounting to around R\$ 13 million for TSN and R\$ 14 million for Novatrans. In August, Aneel authorized the agreement with Transener for the management of the Novatrans lines. On September 12, 2005, having obtained the prior authorization of ANEEL, an extraordinary general shareholders' meeting of TSN was held, which amended the corporate purpose by extending it so as to permit the company to take part in other concessions or in other companies who are electricity grid concession holders.

Payments to Terna

During the accounting period, TSN paid out € 15.2 million in interest on capital and € 9.6 million in dividends to Terna.

Exchange rate performance

During the period, the Brazilian Real appreciated against the US Dollar, and even further against the Euro.

The appreciation relating to the Real is attributable: (i) to high internal interest rates (the SELIC base rate rose to

19.75% only to then drop at period end to 18.0% on an annual basis); (ii) the improvement in the fundamentals of the Brazilian economy also witnessed by the sharp improvement in the spread between Brazilian and American government securities which fell from 463 basis points at the end of 2004 to 306 basis points at period.

EXCHANGE RATE VALUES AT THE END OF EACH QUARTER

Euro	Jan '05	Mar '05	Jun '05	Set' 05	Dec '05
BRL/US\$	2,62	2,67	2,35	2,22	2,32
BRL/EUR	3,42	3,46	2,85	2,67	2,74
EUR/US\$	1,30	1,30	1,21	1,20	1,18

Operations

TSN

During the period, the Sudeste - Nordeste kV 500 transmission line, with an extension of 1,062 km ⁽¹⁾, from Serra da Mesa (Goiás State) to Sapeaçu (Bahia State), including the intermediate sub-stations of Rio das Eguas, Bom Jesus da Lapa and Ibicoara, was fully operative.

Construction activities

The supply and installation of the Capacitive Voltage Transformers (TVC) on the primaries of the transformers at the Sapeaçu and Bom Jesus da Lapa stations was carried out. Two additional reserve reactors were supplied and installed.

Service Quality

The ratios relating to availability and fault rate for 2005 are indicated in the table below, excluding external causes and unforeseeable circumstances. The 2004 figures are shown in brackets. The fault rate on the lines is conditioned by a series of faults affecting the lines reactors, deriving from an oil corrosion problem; the necessary corrective action is currently underway. Shareholders are informed that the line function is considered unavailable in the event of the unavailability of the related reactors even if the line is operative.

AVAILABILITY AND FAULT RATE

	AVAILABILITY %		FAULT RATE ⁽²⁾	
	2005	2004	2005	2004
Power lines	90.65	99.90	0.00	0.85
Bar reactors	99.98	99.99	0.00	0.00
ATR	99.07	99.94	0.25	0.25
SVC	99.88	99.83	4.01	5.01

⁽¹⁾ Length "As Built" of the 500Kv lines (compared with 1,050km in the concession agreement), in addition to 15km relating to the 230 kV double-circuit stretches (considering them as two individual circuits) for a total of 1,077 km.

⁽²⁾ Number of faults per line (100Km)/component (units).

NOVATRANS

During 2005, the North-South II kV 500 connection, with an extension of 1,278 km, from Samambaia (Federal District) to Imperatriz (Maranhão State) including the intermediate sub-stations of Serra da Mesa, Gurupí, Miracema and Colinas, was fully operative.

Construction activities

During 2005, activities continued for the creation of the new Ancillary Services of all the stations with a power supply which is independent from Furnas and Eletronorte. The Samambaia and Gurupí generators were started up. Supplies and installations are underway for the MV lines and the MV/Iv transformations. Two reserve reactors have been installed at the Samambaia and Serra da Mesa stations. The emergency situation which came about following the presence of corrosive oil in part of the Novatrans and TSN reactors, made it advisable to provisionally install the Samambaia reserve reactor at another station. The emergency satellite link has been installed, permitting communication between the Samambaia, Serra da Mesa and Sapeaçu stations with the Rio De Janeiro offices.

Service Quality

The ratios relating to availability and fault rate for 2005 are indicated in the table below, excluding external causes and unforeseeable circumstances. A comparison with the same period last year is not possible since : (i) some of the plants have become operative during 2004; (ii) since the period of grace for the purposes of Parcela Variavel was applicable during 2004, extraordinary maintenance measures were carried out reducing the availability and increasing the fault rate.

Shareholders are informed that the figures relating to the Capacitor Stand functions, both fixed (FSC) and variable (TCSC), are conditioned by a number of project errors made by the supplier which are being corrected by means of measures which have led to extraordinary out-of-service conditions.

AVAILABILITY AND FAULT RATE

	AVAILABILITY	FAULT RATE ⁽²⁾
	2005	2005
Power line (including reactors)	99.82	0.24
FSC	99.87	0.67
TCSC	98.12	28.03

⁽²⁾ Numbers of faults for (100Km)/component line

Italy

RTL Rete di Trasmissione Locale

As already mentioned, as from October 1, 2005 Terna acquired the equity investment in RTL SpA (formerly Acea Trasmissione SpA) from ACEA SpA.

This change led to a series of corporate changes described below:

As of September 29, 2005 the letters of resignation of the members of the Board of Directors and the Board of Statutory Auditors were signed, effective as of September 30, 2005.

As of September 30, 2005, Acea Trasmissione's general shareholders' meeting resolved:

- The appointment of the Chairman and the members of the new Board of Directors;
- The appointment of the Chairman and the members of the new Board of Statutory Auditors;
- The amendments to the Articles of Association, in particular the corporate name from Acea Trasmissione SpA to RTL Rete di Trasmissione Locale SpA.

Subsequently and once again on September 30, 2005 a Board Meeting was held which resolved on:

- The appointment of the Chief Executive Officer;
- The appointment of the Secretary to the Board;
- The structure of powers within the corporate sphere;
- The transfer of the registered offices to Via Arno, 64 Rome.

Operations

Up until September 30, 2005 RTL SpA had directly ensured the control, maintenance and development of the overhead power lines conferred, including the portion of the National Transmission Grid which it availed of, whilst with regards to the underground power lines forming part of the same National Transmission Grid, these activities had been carried out under service agreements by ACEA Distribuzione. At the same time, ACEA Trasmissione ensured the control and maintenance of the entire network of high voltage overhead power lines owned by this company, equalling to approximately 409 Km, under service agreements carried out by ACEA Distribuzione.

As a result of the transfer of the shareholding from Acea SpA to Terna, these agreements have been concluded.

As from October 1, 2005, by contrast Terna was entrusted, under a specific contract, with the operating activities (with the exclusion of the running) and the ordinary maintenance activities in relation to the power lines belonging to RTL, and more specifically comprising: (i) inspections and checks; (ii) emergency

service activities; (iii) processing and implementation of plans for conventional work and that carried out on line equipment; (iv) handling of the interferences; (v) handling of unavailability and operating events; (vi) ordinary maintenance measures; (vii) damage to the assets of RTL.

Another two new contracts have been stipulated, also disciplined on the basis of current market conditions or with reference to the improvements made in relation to the cost anticipated proportionate to the product/service quantity used.

These contracts include:

- The General Services Contract, which involves Terna guaranteeing strategic policy and industrial co-ordination functions, the supply, directly or indirectly, in the interests of the company, of services of corporate interest, also taking steps to provide to: (i) the administrative and financial co-ordination of the company, including therein the layout and management of the financial activities of the same and (ii) the supply of other services in favour of the company in areas of specific corporate interest;
- A Cash Management Contract by means of which Terna ensures the management and co-ordination of all the transactions from time to time associated with the management of both the financial resources and the requirements and the cash management services as well as the performance of any other related transaction.

Once again as of October 1, 2005 all the blue and white-collar staff were transferred from RTL to Terna SpA. Therefore, as of December 31, 2005 the company had just one Executive on the workforce.

APPLICABLE LEGISLATION

Legislative framework

During 2005 and during the early part of 2006, various rulings were issued of interest to the Company, as indicated below:

Italian Decree Law No. 19 dated January 25, 2006 contained the “Transitory provisions for the reduction of natural gas consumption in the thermo-electric sector” published in the Italian Official Gazette No. 21 dated 26 January 2006

- The ruling lays down exceptional measures for a temporary period - until March 31, 2006 - aimed at containing the consumption levels of natural gas in the thermo-electric sector in order to deal with critical situations within the national energy system. The measures adopted make it possible to temporarily re-start plants, which are not running and which can be powered by fuel oil, and the exception, already agreed by means of interministerial decree dated January 27, 2006, to the emission limits of the power stations, envisaged by current legislation for the plants which use fuel oil. The Decree also envisages that the Minister for Production Activities, having consulted the Minister for the Environment and the Electricity and Gas Authority, may establish additional fees payable by the electricity producers in relation to the withdrawals of natural gas made by the latter. It is also anticipated that Terna acknowledges the dispatching priority of the fuel oil plants and the plants powered by renewable sources, assimilating them to essential units for the safety of the electricity system, again until March 31, 2006; Terna is also assigned the task of drawing up a weekly schedule for the maximization of the use of the fuel oil plants to be forwarded to the Ministry of Production Activities, the Ministry of the Environment and the Electricity and Gas Authority.

Decree of the Minister for Production Activities dated December 12, 2005 “Review of the emergency procedures for dealing with the lack of coverage of natural gas requirements, in the event of unfavourable climatic events” published in the Italian Official Gazette No. 297 dated December 22, 2005

- The emergency climatic procedure defines the logical-timing sequence of the measures and identifies the natural gas companies and the operators in the gas and electricity sector responsible for its implementation so as to deal with emergency situations in the balance of the overall natural gas system. Thus, each time a comparison between the forecasts relating to availability and those relating to the gas requirement indicates

a critical situation linked to unfavourable climatic events, which cannot be surmounted by means of recourse to the procedures existing for the normal operation of the physical balance. Within the sphere of the procedures, Terna adopts the reference role of the entire national electricity sector for the purposes of the operational management of the afore-mentioned procedure; in particular, Terna is responsible for providing the Technical Emergency and Monitoring Committee, set up at the Ministry of Production Activities, and Snam Rete Gas SpA with the data and information envisaged by the climatic emergency procedure, forwarded by the electricity producers which own the plants running on natural gas.

Italian Law No. 266 dated December 23, 2005 “2006 Finance Bill” published in Ordinary Supplement No. 211/L to the Italian Official Gazette No. 302 dated December 29, 2005

- Under Article 1.325, the Law introduces new regulations for the depreciation of operating assets used for regulated activities, which as from 2006 anticipate amendments to the discipline for the fiscal depreciation of the electricity distribution and transmission grids, aligning it to the technical-economic depreciation established, for tariff purposes, by the Electricity and Gas Authority. The methods for calculating the depreciation have been specified by means of Inland Revenue Circular No. 50/2005. By way of implementation of the Law, an integration to the income tax consolidation act has been anticipated, preparatory for the implementation of this new discipline, according to which: “The depreciation of the cost of operating assets for the performance of regulated activities [...] is deductible to an extent of no more than that which is obtained by dividing the cost of the assets by the duration of the respective useful lives, as determined for tariff purposes by the Electricity and Gas Authority, and reducing the result by 20 percent”.
- On the subject of corporate law, the Law introduces a number of so-called “anti-scaling” provisions concerning the companies in which the Government holds a significant equity investment. On the basis of these provisions, said companies can envisage (in their Articles of Association) the issue, in favour of the shareholders or one or more shareholders, of new shares or new financial instruments, also endowed with voting rights at ordinary and extraordinary shareholders’ meetings (section 381). The definition of the criteria for the determination of the issue price has been deferred to a subsequent decree of the Minister of Justice, together with the Chancellor of the Exchequer, having consulted the CONSOB.

Italian Law No 131 dated July 13, 2005 converting with amendments Italian Decree Law No. 81 dated May 14, 2005 concerning “Urgent provisions on the subject of equity investments in companies operating on the electricity and gas market” published in the Italian Official Gazette No. 161 dated July 13, 2005.

- By means of this ruling, the limit of 2% to the exercise of the voting right fixed, by means of Italian Decree Law No. 192 dated May 25, 2001 (so-called anti - EDF norm), for the equity investments acquired in companies operating in the electricity sector by parties, directly or indirectly controlled by a Government or by other public bodies, holders on their national market or in a dominant position and not listed on organized financial market “is not applicable if the competent Authorities of the States concerned have approved norms, defined policies and launched the procedures for the privatisation of said parties, such as listing on organized financial markets or other equivalent procedures and agreements have been established with the Italian Government aimed at safeguarding the safety of the supplies and the opening up of the market”.

Italian Law No. 15 dated February 11, 2005 “Amendments and integrations to Italian Law No. 241 dated August 7, 1990, concerning general norms on administrative action” published in the Italian Official Gazette No. 42 dated February 21, 2005.

- Italian Law No. 15/05 introduces a number of amendments and integrations to Italian Law No. 241/90 which are of matter in the administrative procedures for authorization of the construction of long-distance power lines. Specifically, Articles 14 bis and 14 ter envisage that, if the Environmental Impact Assessment (VIA) is requested, the deadline for the decision of the Services’ Conference can be suspended for up to 90 days pending the sentence of environmental compatibility and that, in the event of the inactivity of the competent authorities (Ministry of the Environment, Ministry for the Arts and Cultural Heritage and the Regional Authority concerned), or if the VIA has not been issued by the afore-mentioned deadline, the same will voice themselves during the Services’ Conference. Furthermore, the assent of the competent authority is considered to have been obtained if the representative has not definitively expressed the will of said authority.

Italian Ministerial Decree dated October 21, 2005 containing the “Formalities and criteria for the issue of exemption from the discipline of the right of third parties to access new power lines by means of the electricity systems of other States” published in the Italian Official Gazette No. 256 dated November 3, 2005

- The Decree in question, anticipated by Italian Law No. 290/03, in compliance with Regulation No. 1228/03/CE envisages the conditions for the issue of exemption from the right of third parties to access the new power lines linked with abroad built by private parties (so-called merchant lines), who are not holders of electricity distribution and transport concessions. These continual current power lines or, in

exceptional cases, alternated current lines can be managed outside the national transmission grid, provided that the safety of the national electricity system is guaranteed. Specifically, the exemption cannot be agreed for the power lines which are currently being constructed by Terna itself, or which, albeit not yet started up, have been included in the company's Growth Plan within the last four years. By way of implementation of the Decree, Terna is responsible for indicating to the Ministry of Production Activities, by December 31 of each year, the capacity which can be granted under exemption for the subsequent year, specifying this quantity for each border. Furthermore, within the sphere of the individual procedures for the issue of the exemption, Terna will have to indicate the additional capacity which may be subject to exemption.

Summary of the regulatory decrees directly concerning Terna

A brief summary is presented below of the main resolutions adopted by the Electricity and Gas Authority during 2005 and the first few months of 2006, which have an impact on Terna also taking into account the transmission and dispatch activities whose business segment, in accordance with the Prime Minister's Decree dated May 11, 2004, was acquired by Terna as of November 1, 2005.

Ruling associated with the unification of the ownership and management of the national transmission grid.

Resolution No. 15/05

In view of the unification between the ownership and management of the NTG, by means of this ruling the Authority, besides re-defining the portion of the component covering the costs associated with the activities which will not be transferred, confirmed the criteria for the acknowledgement and coverage of the costs for the provision of the services pursuant to the supplemented text of resolution No. 05/04, assigning to a separate ruling the provisions for guaranteeing the coverage of the costs associated with compliance with the agreements relating to cross-borders transits of electricity and the costs associated with the realization of the programme for the adaptation and improvement of the defence systems for safety.

Resolution No. 79/05 and No. 49/06

By means of resolution No. 79/05, the Authority favourably assessed the Grid transmission, dispatch, development and safety Code, drawn up in accordance with Article 1.4 of the Prime Minister's Decree dated

May, 11 2004 which contains the technical regulations of an objective and non-discriminatory nature for accessing and using the national electricity transmission grid and the directly associated equipment, for the inter-operable nature of the grids and for the supply of the dispatching service, as well as the general criteria for the development and defence of the safety of the national electricity grid and for the maintenance measures on the same.

The resolution also anticipated that by November 30, 2005 Terna would take steps to review the Code on the basis of the observations contained in said resolution and on the basis of the initial period of application of the document.

By means of resolution No. 49/06, the Authority favourably assessed the updated version of the Grid Code, subordinate to the acknowledgement in the same of a number of observations.

Resolution No. 226/05

On October 31, 2005, immediately before the date of transfer to Terna of the transmission and dispatch activities, the Authority adopted resolution No. 226/05 containing “Provisions regarding the transmission and dispatch of electricity within the structure for the unification of the ownership and management of the national transmission grid”.

By means of this resolution, the Authority:

- Set forth the new definition of the transmission service and the dispatching service for the purposes of the regulation and control of the public services, in particular “moving” the NTG plant running activities and the functional development of the NTG from the transmission segment to the dispatch segment;
- Established November 1, 2005 as the date of enforcement of the Grid Code;
- Introduced the concept of incentive regulation for the dispatch service, authorizing its offices to study incentive mechanisms on the basis of similar European experiences.

Other rulings

Resolutions regarding dispatching (Nos. 54/05, 64/05, 97/05, 133/05, 161/05, 175/05, 293/05)

As far as the regulation of the dispatch activities is concerned, the Authority intervened during the year by means of several resolutions so as to lay down provisions supplementing and/or amending resolution No. 168/03 which represents the reference text containing the conditions for the provision of the public dispatch service. Specifically, in addition to measures streamlining the ruling:

- The discipline of the production units pursuant to Italian Legislative Decree No. 387/03 and Italian Law No.

239/04 was envisaged, in other words the plants, using renewable sources or otherwise, less than 10 MVA;

- Contract outlines have been approved for the dispatch service concerning incoming and outgoing electricity, which the dispatch users are obliged to stipulate with Terna;
- Provisional conditions have been defined for 2006 on a consistent basis with 2005 (for example: anticipating Terna's possibility of making additional offers; calculation and invoicing timescales anticipated on a provisional basis for 2005 confirmed);
- A specific regime has been anticipated for the electricity production and pumping units of strategic importance in relation to their essential nature for the purposes of the safety of the electricity system in force as from February 1, 2006.

With reference to this latter aspect, by means of **Resolution No. 20/06** the Authority approved the amendments made by Terna to section 4 of the Grid Code - Dispatch Regulations - so as to take into account the new regulation of the electricity production and pumping units of strategic importance. In this connection, the Milan regional administrative Court, by means of sentence dated February 28, 2006 cancelled resolution No. 175/05 in relation to the part where it envisaged the particular regime of the strategic production and pumping units.

Again in relation to the dispatch activities, by means of **Resolution No. 282/05**, the Authority approved the new division into zones of the relevant grid as emerges from the proposal formulated by Terna, establishing the operations of the new zone-based structure as from January 1, 2006 subject to the appropriate operational checks to be carried out by Terna.

Resolution No. 213/05 concerning interruptible services

By means of this resolution, the Authority established the conditions for the supply of additional interruptible resources with respect to those already activated, for the safety needs of the national electricity system. For this purpose, the concession holder of the dispatch activities is obliged by December 31, 2005 to supply resources for the instantaneous and with warning interruptible service of the quantities established by the same Authority, on the basis of procedures already adopted for the assignment of the service during 2003 and 2004 and remunerating the resources in accordance with the matters established by resolution No. 151/03.

Resolution No. 269/05 concerning imports

By means of this resolution, the Authority established the formalities and the conditions for imports and exports of electricity for 2006, by way of implementation of the criteria envisaged by the decree of the Minister for Production Activities dated December 13, 2005. In particular, partly on the basis of the matters anticipated by

EC Regulation No. 1228/03, for 2006 market mechanisms have been anticipated both for the handling of the congestions (resorting to the day ahead energy market of the electricity exchange), and for the allocation of the coverage from the risk associated with the differentials between the external price and the internal price of the import area (CCCI).

In particular, as far as the allocation of the CCCIs is concerned, the mechanism established by the authority concerns 50% of the total import capacity available; the remaining 50% is assigned according to the regulations laid down by the individual bordering nations (France, Switzerland, Austria, Slovenia and Greece). The allocation is made by Terna via competition procedures and takes place on a decreasing price order basis with the aim of maximizing the value of the offers accepted, it being understood that the allocation price is unique and equal to the price indicated in the offer per CCCI with the lowest price amongst those accepted.

Resolution No. 281/05 concerning plant connection

By means of resolution No. 281/05, the Electricity and Gas Authority disciplined the conditions for the supply of the service relating to the connection to electricity grids with a nominal voltage of more than 1 kV by Terna and other distributors.

The ruling makes changes to the current conditions both from a technical point of view - for example, two levels of design of the connection are envisaged, one of a general nature and one more detailed - and from a fee point of view; in fact, the resolution established both the fees due to Terna for the activities concerning the management and analysis of the connection requests in relation to the two project stages, and the fees which the owners of the production plants who intend to connect up to the grid are obliged to pay over for the creation of the connection. On the basis of this resolution, Terna is obliged to establish the contractual formalities and conditions for the provision of the connection service and forward them to the Authority by April 20, 2006.

Resolution No. 6/06 concerning the quality of the service

By means of resolution No. 06/06, the Electricity and Gas Authority approved the expected levels of quality of the transmission service, within the framework of the regulations established by said Authority on the subject of the Grid Code. The expected levels of quality of the transmission service concern any possible shortfalls in supplies to users directly linked to the national transmission grid which are attributable to Terna, with the exclusion of significant incidents, in relation to which it is envisaged that Terna must draw up a specific report to be forwarded to the Authority.

The new parameters anticipated include:

- The average national number of supply outages per user;

- The energy not used for outages;
- The maximum number and the maximum duration of the supply problem for each individual customer.

The expected levels, approved by the Authority, have been published in the company's website.

Advisory document on the incentives for the re-unification of the grid

“Incentive mechanisms for the aggregation of the ownership of the national transmission grid” Article 2 of the Prime Minister’s Decree dated May 11, 2004 established that, for the purposes of improving the safety and running efficiency of the NTG, the Authority should assess and, if need be, arrange for the adoption of incentive mechanisms - also tariff-based - aimed at furthering the complete unification of the national electricity transmission grid. In this connection, it is left to the faculty of the Authority to differentiate between the afore-mentioned mechanisms if the unification of the ownership involves an equity investment in the share capital of Terna by other owners, thus favouring the pluralist composition of the shareholding structure. The afore-mentioned Prime Minister’s Decree has established April 30, 2006 as the deadline for the applicability of the incentive mechanisms. The Electricity and Gas Authority has initially followed up the Prime Minister’s Decree by means of the publication on August 3, 2005 of an advisory document which contains illustration of the direction which it intends to adopt with regards to the definition of the incentives pursuant to Article 2 of the afore-mentioned Prime Minister’s Decree.

The following mechanism is proposed in the document:

- The application of an incentive/deterrent to be applied in the event that the merger transactions take place, respectively, by/not beyond April 30, 2006;
- As an additional measure in the event of merger by April 30, 2006, an increase of the RAB remuneration.

The amount of the incentive/deterrent, in the Authority’s proposal, had to be estimated by the GRTN on the basis of conditions established by the Authority so as to reflect to efficiency expected of the aggregation to the charge of the unified Transmission Operator of the remaining portions of the NTG. Whilst it is proposed that the incentive be paid to the sellers by the unified Transmission Operator and recovered by the same by means of the tariff revenue, the deterrent is imposed on the owners decreasing the tariff revenues pertaining to them.

An additional incentive measure provided by the increase of the remuneration of the RAB by 1% - 2%, would be applicable for a period of 3 - 5 years, extendable for an additional period of 2 - 3 years in the event the seller opts for an equity investment in Terna’s share capital.

ENERGY SCENARIO

Energy requirements in Italy

During 2005, according to the first provisional figures, electricity demand reached 329,441 GWh, involving an increase of 1.3% on the previous year, in turn characterized by similar growth (+ 1.5%) compared to 2003. The 2005 result felt the effect of the differing calendar (despite being a leap year, in fact, 2004 had four working days more in total) and differing climatic conditions. As a point of fact, in 2005 average monthly temperatures which were moderately colder occurred in the Winter months and which were warmer in the Summer (apart from August). Therefore, aside from the calendar and temperature effects, the change in electricity demand came to +1.6%.

During 2005, the electricity demand of the grid was 85.1% satisfied by national production (86.0% in 2004), for a value equalling to 280,286 GWh net of the consumption of ancillary services and pumping and with an increase of 0.2% on 2004. The remaining portion (14.9%) was covered by exchanges with abroad, for a value in 2005 of 49,155 GWh compared to 45,635 last year.

Analysing the trend in the direction of the foreign trade flows, imports recorded an increase (+ 8.3%), reaching 50,264 GWh as against 46,426 GWh in 2004. The rise in imports is essentially due to the fact that the temporary measures decided in 2004 by the Gestore della Rete di Trasmissione Nazionale SpA ("GRTN") for the safety requirements of the electricity system, were no longer applicable. Exports, on the other hand, rose from 791 GWh to 1,109 GWh disclosing growth of 40.2%.

ELECTRICITY BUDGET IN ITALY

GWh	2005*	2004	Change	%
Gross production	302,359	303,321	-962	-0.3%
Ancillary services	12,704	13,299	-595	-4.5%
Net production	289,655	290,022	-367	-0.1%
Received from foreign suppliers	50,264	46,426	3,838	8.3%
Sold to foreign customers	1,109	791	318	40.2%
Destined for pumping	9,369	10,300	-931	-9.0%
TOTAL DEMAND - ITALY	329,441	325,357	4,084	1.3%

* Provisional values

Consumption

During 2005, total electricity consumption amounted to 308,000 GWh, involving an increase of 1.2% with respect to the previous year. Electricity intended for the market shows, over time, an increase in the portion covering the consumption of eligible customers and a consequent reduction in the portion destined for captive customers. During 2005, the portion of consumption relating to the captive market (150,800 GWh) represented 49.0% of the total, compared to 51.3% in 2004. The eligible market by contrast came to 135,700 GWh, involving an increase of 6.8% on 2004. This increase reflects the extension of the qualification of eligible customer as from July 1, 2004 to all non-domestic customers.

In conclusion, the table shows essential stability in the portion of internal consumption which in 2005 came to 7.0% of total consumption.

ELECTRICITY CONSUMPTION IN ITALY BY MARKET TYPE

GWh	2005*	2004	Change	%
Captive market	150,800	156,330	-5,530	-3.5%
Eligible	135,700	127,063	8,637	6.8%
Internal	21,500	21,097	403	1.9%
Total	308,000	304,490	3,510	1.2%
Loss	21,441	20,867	574	2.8%
% of	(6.5%)	(6.4%)		
TOTAL REQUIREMENT	329,441	325,357	4,084	1.3%

* Provisional values

The distribution of electricity consumption by economic sector, illustrated in the following table, shows increases above average (+ 3.4%) for the tertiary sector which absorbs 82,300 GWh, with a quota equalling to 26.7% of total consumption; increases just under the average were registered in the domestic sector (+ 0.9%), which produces a value of 67,170 GWh, representing 21.8% of the total.

When compared to the previous year, consumption in the industrial sector was steady (+ 0.1%), amounting to 153,300 GWh, or 49.8% of total consumption. The temperature effects mentioned previously, a little colder in the Winter and warmer in the Summer, are able to justify the increases in consumption registered in the domestic sector when compared to last year.

ELECTRICITY CONSUMPTION IN ITALY BY ECONOMIC SECTOR

GWh	2005*	2004	Change	%
Agriculture	5,230	5,185	45	0.9%
Industry	153,300	153,155	145	0.1%
Tertiary	82,300	79,558	2,742	3.4%
Domestic	67,170	66,592	578	0.9%
Total	308,000	304,490	3,510	1.2%

* Provisional values

Production

During 2005, net national production remained essentially stable when compared to the previous year, -0.1% (see following table). Separating the data relating to production net of ancillary services up by source, during 2005 there was an increase in thermo-electric production of +2.9% when compared to 2004. Net production from renewable sources, excluding the hydro-electric source, increased by 1.0%. The increase was considerable for wind power production (and photovoltaic) up +15.6%, while geothermoelectric production was down, -2.1%. As far as hydro-electric production was concerned, a net decrease was seen in 2005, - 15.0%, due essentially to lower availability from natural sources when compared to 2004. The annual hydro-electric producibility index in fact was lower than the corresponding value last year, disclosing 0.79 compared to 0.97 reported in 2004.

ELECTRICITY GENERATION IN ITALY

GWh	2005*	2004	Change	%
Gross hydro production	42,482	49,908	-7,426	-14.9%
Gross thermal production	252,412	246,125	6,287	2.6%
Gross geothermal production	5,325	5,437	-112	-2.1%
Gross wind and photovoltaic	2,140	1,851	289	15.6%
Total gross production	302,359	303,321	-962	-0.3%
Hydro ancillary	573	625	-52	-8.3%
Thermal ancillary	11,824	12,361	-537	-4.3%
Geothermal ancillary	304	310	-6	-1.9%
Wind and photovoltaic ancillary	3	3	0	-
Total ancillary services	12,704	13,299	-595	-4.5%
Net hydro production	41,909	49,283	-7,374	-15.0%
Net thermal production	240,588	233,764	6,824	2.9%
Net geothermal production	5,021	5,127	-106	-2.1%
Net wind and photovoltaic production	2,137	1,848	289	15.6%
Total net production	289,655	290,022	-367	-0.1%

* Provisional values

Power generation plants

During 2005, the net efficient generation power came to 86.8 GW, involving an increase of 6.4% when compared to 2004. The greatest increases took place in the thermoelectric base, involving a rise of 4,410 MW, with growth of 7.5% on 2004. In percentage terms, the greatest increases took place in the wind power and photovoltaic sector, + 47.6%, corresponding to 540 MW. The increases in net hydro-electric efficient power, 256 MW (+ 1.2%), and net geothermal efficient power, 45 MW (+ 7.0%), were of a more modest extent.

ELECTRICITY GENERATION IN ITALY

MW	2005*	2004	Change	%
Gross hydro power	21,350	21,073	277	1.3%
Gross thermal power	66,100	61,531	4,569	7.4%
Gross geothermal power	729	681	48	7.0%
Gross wind and photovoltaic power	1,680	1,139	541	47.5%
Total gross power	89,859	84,424	5,434	6.4%
Net hydro power	21,000	20,744	256	1.2%
Net thermal power	63,400	58,990	4,410	7.5%
Net geothermal power	687	642	45	7.0%
Net wind and photovoltaic power	1,675	1,135	540	47.6%
Total net power	86,762	81,511	5,251	6.4%

* Provisional values

DISPATCHING AND SALES

By means of the acquisition in November 2005 of the TSO business segment, TERNA became the company responsible in Italy for the transmission and dispatch of electricity onto the high and very high voltage grid throughout the whole of Italy.

During the accounting period, the safety of the supplies was guaranteed, ensuring the adequacy of the resources covering the demand and the continual balance over time between energy requirements and available resources.

Dispatching activities present three main processes, separated by the timescale taken into consideration:

- In real time: the action aimed at balancing the energy requirements by means of the dispatch of units, maintaining adequate margins of reserve on the basis of the resources which can be supplied, and at guaranteeing the safety of the electricity system and the service quality;
- Over the short-term: the exchange of preliminary information with the Electricity Market Operator (GME) and the performance of the Market for Dispatching Services for the acquisition of power generation resources in accordance with optimum economic criteria so as to ensure the adequacy and the safety of the electricity system for the day after that of performance of the market;
- Over the medium-term: the scheduling of grid maintenance and of generating units so as to cover the requirement and the preparation of an adequate level of reserve.

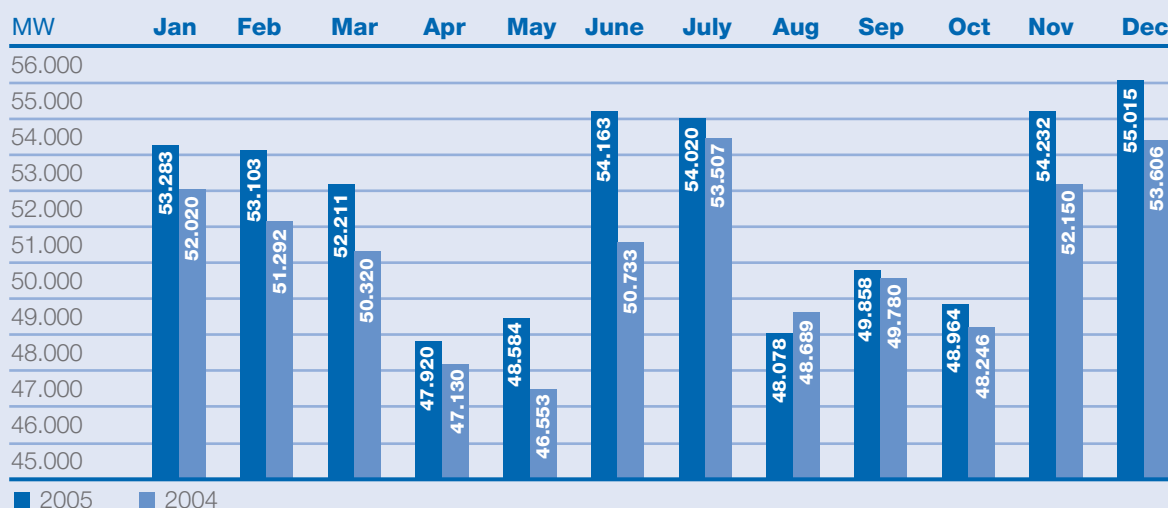
During 2005, the management of the system made it possible to overcome the criticalities satisfactorily, guaranteeing the safety and adequate margins of reserve.

Performance of the electricity business

The performance of the peaks in the power requirement is shown in diagram 1. The maximum value of the Summer period came to 54,163 MW, reported on June 28, 2005, involving an increase of 1.2% when compared to the previous Summer peak on July 23, 2004 (53,507 MW). On the same day, another all-time-high was also recorded in the daily electricity demand, equalling to 1,098 GWh.

On December 20, 2005 at 6.00 p.m., a new time peak record in requirement was reported with a value of 55,015 MW, greater by 2.6% than that in 2004 (53,606 MW on December 16, at 5.00 p.m.). The ratio between energy and power at peak in the period under review (hours of utilization) dropped from 6006 in 2004 to 5988 in 2005. The slight decrease was caused by a rise in power demand at peak greater than that of the total energy demand for the year (2.5% compared to 1.3%).

REQUIREMENT IN MONTHLY MAXIMUM POWER - DIAGRAM 1



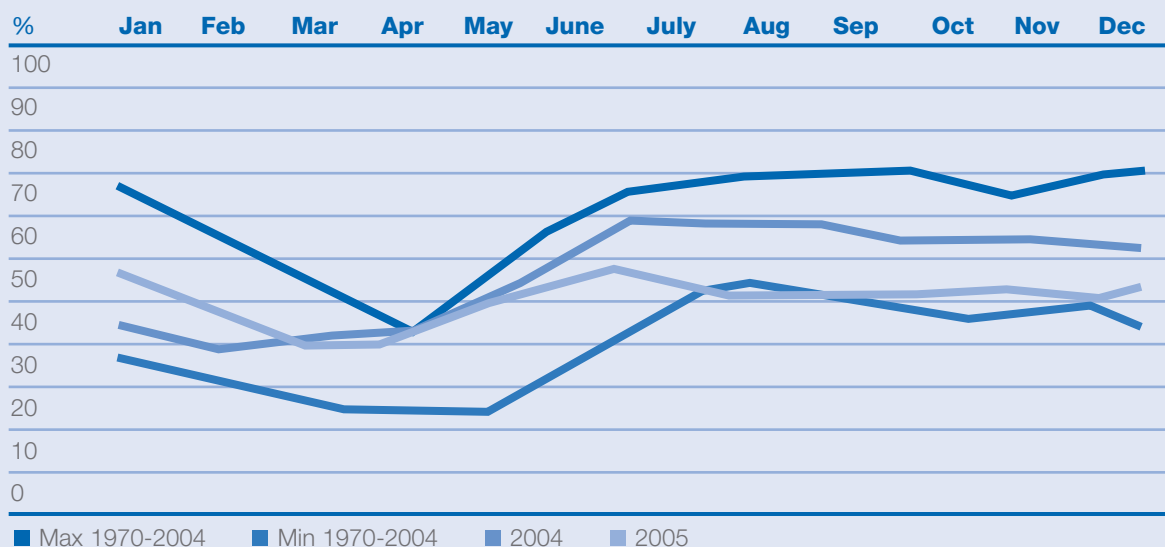
Coverage of the requirements

During the 2005 Summer period, a crisis in water resources occurred, placing the availability of the thermo-electric plants located along the course of the River Po at risk, due to the potential lack of cooling water. In fact, due to the scarce snow falls in North Italy, during the Winter period, the water situation during the Summer period was characterized by low indices of hydraulicity in relation to the corresponding average indices for the period. Diagram 2 shows the storage levels of the reservoirs in Italy which indicate how in 2005 the minimum all-time-low levels of the reservoirs were reached.

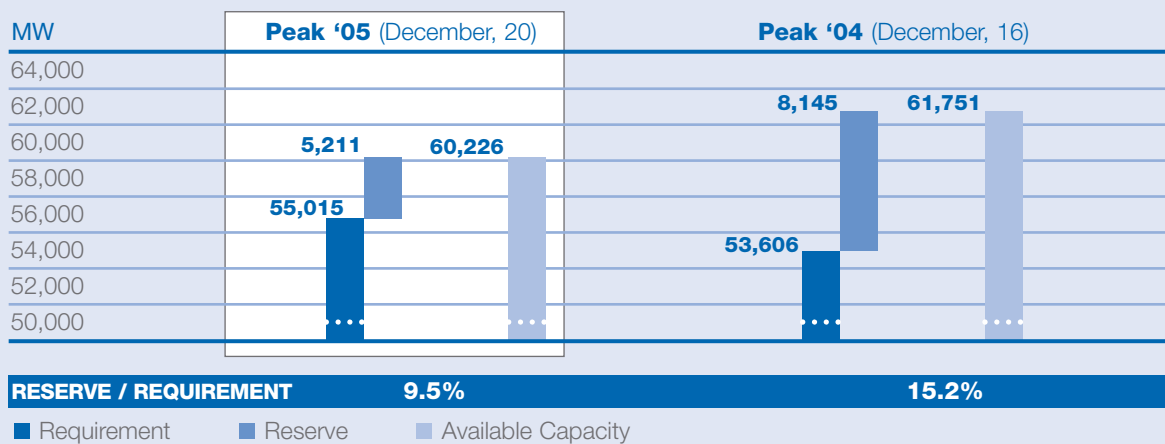
For this reason, the Po River basin Authority put together a memorandum of understanding for the joint management of the water crisis in the River Po basin, signed by all the parties operating within the sphere of this basin, so as to organize activities for the survey and control of the water balance aimed at preventing exceptional droughts in the water basin. As part of these activities, Terna had the task of collating and processing the water data originating from the producers of the hydro-electric belonging to the Po basin.

As from December, considerable demand was registered for exports of power abroad made by Italian operators. These events can be justified in the first instance by the upwards trends in prices of the Central-European electricity market, contributed partly to by the particularly rigid weather conditions

STORAGE LEVELS OF THE ITALIAN RESERVOIRS - DIAGRAM 2



MARGINS OF RESERVE AT PEAK 2005 VS 2004 - DIAGRAM 3



which affected Central Europe, and to new market strategies drawn up by the Italian operators. The phenomenon of exporting power abroad led, on certain days in December, to critical situations in the coverage of the Italian requirement, thereby reducing the reserve margins.

The decreased use of the interconnection capacity with abroad, in concurrence with the coming onto stream of new gas-run plants, when compared to last year, led to a consistent increase in thermo-electric consumption of methane.

Such circumstances, in addition to the noted reductions in the supply of gas imported from abroad, led to

an emergency situation in the supply of the necessary natural gas reserves. So as to contain the consumption of gas for thermo-electric plants and safeguard the powering adequacy of the electricity system, Terna proposed transitory measures for maximizing the use of fuel oil for thermo-electric generation, to the detriment of gas use. These proposals contributed towards the definition of Italian Decree Law No. 19 dated January 25, 2006, concerning “Urgent measures for guaranteeing the supply of natural gas”.

The action set underway in 2005 with regards to production plant maintenance scheduling, in line with the action carried out in 2004, in any event made it possible to achieve a reserve margin of 9.5% (see diagram 3) during maximum Winter peak periods.

Supply of dispatch resources

On January 1, 2005 the last stage of the Electricity market was launched, characterized by admission of the application to the Day Ahead Energy Market (DAEM).

Considering the technical difficulties faced by the operators, particularly during the start-up phase, when estimating its consumption the Electricity and Gas Authority, by means of resolution No. 168/03, entrusted GRTN (from November 1, Terna) with the task of supplementing the demand expressed by the market in the event that this differed significantly (by more than 5%) from Terna's aggregate demand forecasts. The integration took place by means of the formulation of a supplementary supply offer on the DAEM. Furthermore, the day before Terna published the estimate of the energy requirement (operation preliminary to the opening of the market), it made the declaration of the transport limits between the areas and, subsequent to the closure of the Day Ahead Energy Market DAEM, acquired the resources for balancing the residual forecast errors and failures and for resolving the congestion and regulating the electricity system.

During 2005, Terna was enabled, as already mentioned, to present sales or purchase offers on the DAEM for the purposes of the realignment of the total of the demand expressed on the energy markets with the requirement forecast, in the cases where this difference emerged as greater than 5%. In reality, due to the reduced forecast ability demonstrated by the operators of the withdrawal, Terna operated on the DAEM market on a daily basis, selling energy for around 3.5 TWh and purchasing energy for approximately 5.3 TWh.

At monthly level, the quantities acquired and sold were extremely variable, in relation to the differing conduct of the operators. In January, the maximum purchase balance was registered, equalling to 579 GWh, while in April the maximum sale balance of 266 GWh was disclosed.

In contrast to the DAEM, the Market for Dispatching Services (MDS) is a “pay as bid” market, in other words each unit is remunerated at the price offered and not at the marginal price. The operators are obliged to present an energy purchase price and an energy sales price for each unit. The prices presented are valid both in the MDS ex ante and the MDS ex post.

- MDS ex ante

During the scheduling phase which is carried out on the day prior to the flow date, energy is purchased and sold for the purposes of supplying the power reserve, resolving the residual congestion pertaining to the markets (DAEM and RTE) and covering the residual requirement error.

11.8 TWh of energy was purchased and 13.1 TWh of energy was sold on the MDS ex ante.

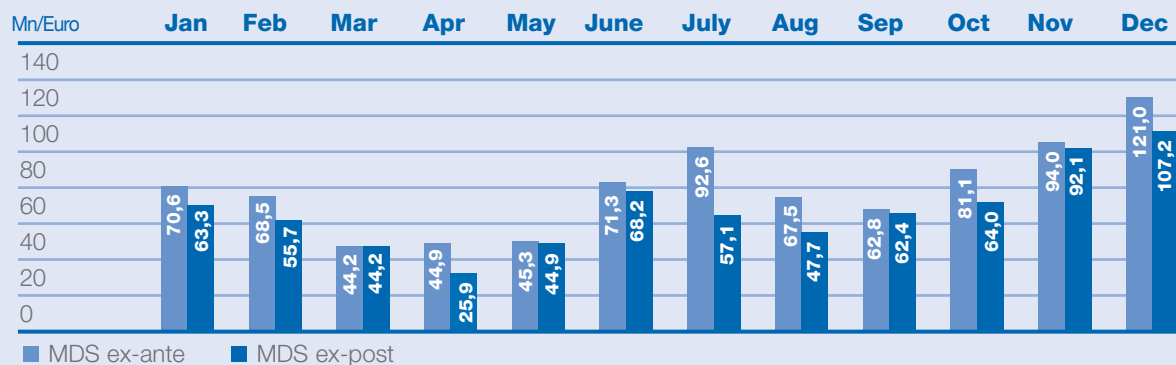
The quantities acquired and sold were variable over the months due to the differing requirement correction needs, which emerged as greater in April (467 GWh) and lower in February (13 GWh). The net charge by contrast was up during the year as a result of the significant increase in energy sales prices, passing from an average value in January of 86 €/MWh to around 111 €/MWh in December, as can be seen in the table which follows.

- MDS ex post

In real time, energy is purchased and sold for the purposes of balancing the grid by means of the forwarding of orders to the enabled production units.

9.8 TWh of energy was purchased and 8.0 TWh of energy was sold on the MDS ex post.

The quantity acquired was as normal greater than the quantity sold due to the need to cover the average negative imbalances of the power generation plants, while the differences between the real demand and the estimated value were extremely reduced. The maximum purchase balance was registered in December, with 411 GWh.



The difference between the consumption programmes, expressed by means of the purchase offers on the DAEM and the bilateral platform, and the energy effectively withdrawn at final balance (imbalance) generated a total net settlement item vis-à-vis TERNA of 0.3 TWh.

Interruptible service

The load interruptible service, with or without warning, permits TERNA to avail of a quantity of interruptible power which can be used:

- In the event of instantaneous interruptibility, in other words without warning, mainly for rapidly re-establishing reserve and balance in real time;
- In the event of notified interruptibility, so as to define the recourse to the activation of load lightening procedures in relation to situations of effective risk for the national electricity service.

The interruptible service was launched back in 2001. The service was associated with the transport capacity reserve on the interconnection with abroad to clients willing to accept the interruption of the load, but, as from January 1, 2004, the interruptible service with or without warning was assigned for the three-year period 2004/2006 with a specific remuneration for the service provided.

During November 2005, Terna assigned for 2006, in accordance with the Authority resolution No. 213/05, an additional 100 MW for the interruptible service with warning and 210 MW for the interruptible service without warning.

The additional allocation of the “with warning” service complies with the needs manifested by Terna to increase the quantity of available resources for the “with warning” interruptible service which were reduced following the revocation of the rights of the assignees in breach and following the reduction of the power contracted by the assignees themselves.

The additional allocation of the “without warning” service complies, by contrast, with the need to avail of additional interruptible power so as to deal with the eventuality of particularly serious inefficiencies deriving from Switzerland further to the coming onto stream of the new extremely high voltage S. Fiorano - Robbia interconnection line.

The table below illustrates the number of parties who provided the interruptible service during 2005 and the contractual power.

	Number of customer	Contracted power (MW)
Without warning	84	1,732
With warning	76	1,051

Real time controls

Real time operating essentially involves ensuring the continuity and the quality of the electricity service under safety conditions by means of the continual balance of the deviations in demand from forecasts and the re-establishment of the safety conditions following the accidental losses of the grid elements, such as power generation units or power lines. For this purpose, it is essential to ensure the functions for the transmission of the energy from the generation sources to the consumption centres, so as not to exceed the transport capacity limits of the individual long distance power lines. During 2005, the new duty line, set up for the safety checks of the transits of the interconnection lines and the on-going monitoring of the foreign sections, contributed towards enhancing the ability to interact with the foreign operators and improving the ability to prevent possible criticalities on the interconnection lines.

Service quality, energy not supplied and inefficiencies

During 2005, energy not supplied, referring to the relevant grid, came to approximately 2,102 MWh and this value was net of the interruptions on the load contractually interruptible. Specifically with regards to the Rome headquarters area, the diffuse utility outages caused by the heavy snow falls in the central Italian regions (in particular, Abruzzo and the Adriatic strip of the Marche and Molise) during the last few days of January 2005, which mainly affected the 150 - 132 kV grid of said area, weighed in considerably (over 600 MWh).

With reference to just the outages attributable to faults of the NTG elements, the value of energy not supplied came to around 600 MWh.

Recourse was made to the interruptible service, with or without warning, for accidental events in particular in Sardinia and Sicily, so as to restore an adequate reserve and the system safety conditions. The most significant events which should be recalled include:

- On January 20, at 06.58 a.m., due to the shutdown of a number of important generating units in Sardinia, recourse was made to the interruptibility disconnection plan in order to restore an adequate tertiary reserve;
- On February 22, at 6.40 p.m., as a consequence of the cut-out of an important generating unit and the delay in the activation of a production unit, in order to restore the safety conditions on the Calabrian-Sicilian grid, recourse was made to the plan for the disconnection of the interruptible loads in real time and with warning;
- On September 17, at 12.27, following the cut-out of a number of generating units in Sardinia, the disconnection plan of the utilities which can be interrupted with warning was applied and, subsequently, at 12.38 following the cut-out of an additional unit, recourse was made to the disconnection of the utilities which can be interrupted without warning.

So as to guarantee adequate voltage profiles on the EHV-HV transmission grid, action was carried out for containing the voltage on the transformers of the primary stations of the distribution plants during the last few days of June, which were characterized by a brief but intense heat-wave; in fact, as already mentioned the all-time-high daily request for energy at national levels was registered on June 28. The progressive values, noted as of December 31, 2005, for the three reference indicators of the service's quality are summarized below:

- ASA (Average system availability - Total Terna availability) = 99.262 %
- AIT (Average interruption time of supply - Average duration of system supply interruptions) = 0.681 mins/period
- SAIFI (System average interruption frequency index - Average number of interruptions per User directly linked to the Terna NTG) = 0.184

Start-up of new grid elements

As far as the start-ups of new grid elements on the various voltage levels are concerned, such as auto-transformers, various types of generating units, primary stations, power lines, mention is made of the following for 2005:

Power lines

- The new 380 kV double-circuit interconnection power line with Switzerland S.Fiorano-Gorlago-Robbia, brought onto stream on January 18, 2005;
- The 380 kV La Spezia - Acciaiolio connection, finally up and running on May 20 following the completion of the work c/o the La Spezia S/E;
- The 380 kV Rizziconi - Feroletto - Altomonte - Laino long distance power lines, activated during the Autumn, which together with the stations of Altomonte and Feroletto create the second backbone of the Calabrian grid.

Power generation plants

- Edison 800 MVA Altomonte thermo-electric power station;
- Enipower 1,170 MVA Brindisi thermo-electric power station;
- Edison 360 MVA Candela thermo-electric power station;
- Endesa 400 MVA Tavazzano thermo-electric power station;
- Tirreno Power 400 MVA Torrevadalis Sud thermo-electric power station;
- Enel Produzione 340 MVA Sulcis thermo-electric power station.

NATIONAL TRANSMISSION GRID

2006 Development plan for the National Transmission Grid

Following the acquisition of the GRTN business segment and on the basis of the matters anticipated in the Concession and in the Grid Code, Terna annually draws up the NTG Development Plan (DP), subject to assessment by the Ministry of Production Activities (MAP); this plan contains an analysis of the current and future criticalities of the grid and the identification of the main developmental measures. The 2006 DP, resolved by the Terna Board of Directors during the meeting held on December 21, 2005, was forwarded in January 2006 to the MAP, the Electricity and Gas Authority, the Departments of Infrastructures, the Environment, the Arts and Cultural Heritage, the Economy and the Regional Authorities.

Institutional agreements

During 2005, Terna signed a memorandum of understanding with the Umbria, Tuscany and Marche regions for the application of the Strategic Environmental Assessment (SEA) to electricity planning relating to the regional territory. Whilst, with the Ministry for the Arts and Cultural Activities, a protocol was signed for the integration of the Changeover dimension in the SEA applied to the development of the national electricity grid.

Authorizations

During the course of 2005, Terna completed the technical-administrative procedures relating to the authorization courses for the following developmental measures:

- SAPEI Fiume Santo (Sardinia) - Latina (Lazio) 500 kVcc 1,000 MW connection: the authorization request for the construction and operation was forwarded in accordance with Italian Legislative Decree No. 190 (implementation of Objective Law No. 443) on October 19, 2004. The connection project was approved by the CIPE during the session held on December 2, 2005;
- Matera - S.Sofia 380 kVca long distance power line: the variant for the completion of the Matera-Santa Sofia power line measuring 27km was judged as environmentally compatible on June 6, 2005; the authorization request for construction and operation was forwarded, in accordance with Italian Legislative Decree No. 190 (implementation of Objective Law No. 443) on November 26, 2004. The variant project was approved by the CIPE during the session held on December 2, 2005;
- 150kV cable connection between Sardinia and Corsica (SARCO): the authorization request for the construction and operating of the cable was presented on December 15, 2003. Final authorization, by the Department of Infrastructures, was given on July 25, 2005.

Investments in tangible fixed assets

In line with the types of activities carried out by the Company, investments can be broken down in four main categories:

Development: measures which concern the variation or the enhancement of the transport, transformation and/or interconnections capacities. This category also includes the acquisition of portions of the National Transmission Grid.

Upgrades: measures for updating Terna's plants in accordance with legislative provisions or authorization requirements, with special focus on legislation regarding electromagnetic fields and the environmental impact of the structures.

Renovation/Modifications: measures which have concerned the essential modification of the technical and functional features of the plant and/or upgrading of the plant configurations, so as to significantly increase the useful life.

Rationalization: measures targeted at changing the configuration of the plants so as to improve the running efficiency.

INVESTMENTS IN TANGIBLE FIXED ASSETS MADE DURING THE YEAR

In millions of Euro	2005	2004
Development	156.5	176.0
- assigned directly	139.0	145.2
- under tender	9.1	22.8
- for acquiring portions of the NTG	0.0	8.0
- interconnections with abroad and Defence Plan	8.5	0.0
Modifications	15.5	15.2
Rationalization	11.2	9.8
Upgrades	3.2	3.3
Renovation	62.2	65.8
Other	10.6	7.7
Total	259.4	277.8

The breakdown of investments by plant type in 2005 is as follows:

TOTAL INVESTMENTS

In millions of Euro	2005	2004
Power lines	121.3	154.1
Transformer stations	121.7	110.9
Other	16.4	12.8
Total	259.4	277.8

The main investments made during the year were as follows:

LINES

In millions of Euro	Plant	Amount
Turbigo-Rho	Construction of 380 kV power line	23.8
Laino-Feroletto-Rizziconi	Construction of 380 kV power line	21.7
S.Fiorano-Robbia	Construction of 380 kV power line	7.5
Matera-S.Sofia	Completion of 380 kV power line	7.6
Sardinia-Corsica	Construction of Sardinia Corsica connection	7.3

STATIONS

In millions of Euro	Plant	Amount
Santa Barbara	Construction of new armoured 380kV section	10.0
Rumianca	Construction of new 220 kV section and installation of new ATR	5.0
Sparanise	New 380kV station and related connections	4.5
Pianezza	Plant renovation	3.9
Casellina	Construction of new 380kV section	3.6
Verderio	Plant renovation	3.2
Ferrara	New station	3.2
Santa Maria C.V.	Installation and new 220kV section	2.8
Vicenza Monteviale	Construction of new 132 kV section and installation of new ATR	2.7

Significant O&M activities

The following significant activities were started up or launched during 2005:

- Acknowledgement, during the fourth quarter, of the indications deriving from the “efficiency project” with amendments to the criteria for the controls, for maintenance and overhauling of the equipment;
- Continuation of the campaign for the replacement of the glass insulators with other in composite materials or glass pre-coated with silicon resins so as to eliminate vulnerability in highly polluted areas (saline – industrial/agricultural pollution);
- Increase in work carried out with technical LST (work on live equipment);
- Targeted measures for replacing equipment, systems of protection devices or components if overall renewal measures are not envisaged, so as to guarantee the continuity of the services with the levels of quality anticipated by the plan;

- Full use of the MBI system (expert system supporting the power line and station maintenance activities) which permits the optimisation of the maintenance measures - carried out almost exclusively on condition;
- Full use of the GIS system, with the complete geo-referencing of the National Electricity Grid.

Initiatives undertaken for reducing the environmental impact

During 2005, the initiatives undertaken by Terna for the reduction of the environmental impact concerned the use of technologies for the construction of new plants which minimize the use of public and private areas, the impact on the landscape and the emission of electrical or magnetic fields. The main measures of this type included the significant construction of the new 380 kV Turbigo-Rho power line, which starts off from the Turbigo station, runs approximately 20 km on overhead piles and then turns into buried cable lines, for a stretch of 8 km (the first of this type constructed in Italy and one of the most important in Europe), which has made it possible to reduce the visual impact in relation to a highly antropized territory as the Milan hinterland is.

Other project devices adopted include:

- The adoption of particular paints for the finishing of the supports which permit the camouflage of the aerial part of the structure
- Finishings consistent with the local construction types and screening by means of wings of trees shielding the two air/cable transition stations in the municipalities of Pogliano and Rho
- The construction of specific screening created with metallic materials with high magnetic permeability which make it possible to decrease the electrical and magnetic field even at reduced distances from the axis of the underground cables
- The real time monitoring of the operating conditions of the cables so as to avoid the risk of local overheating and deterioration of said cables and the quality of the connection

The other leading project which has taken advantage of solutions of particular interest from an environmental placement point of view, is the new continual current connection between Sardinia and the Italian peninsula, which will be completely constructed using underground and submarine cables.

In this case, Terna has taken steps to entrust a firm of professionals specialized in industrial architecture with the architectonic design of the only two emerging parts, or rather the two alternate current / continual current conversion stations located in north Sardinia and at Latina.

The architectonic appearance of the two stations has been particularly appreciated by the public authorities

who participated in the Services' Conference called by the Department of the Infrastructures for the approval of the project; this made it possible to complete the preliminary stage without particular difficulties. In conclusion, it is considered appropriate to remind the shareholders that, over the last few years, Terna has consolidated a relationship scheme with the local authorities which envisages the achievement of measures with a highly environmental value on the existing grid (burying of underground lines, layout variants, improvement work for the environmental placement of the stations), with financing partly or fully provided by the petitioning authorities.

TERNA plant and equipment

The following table shows the number of Terna's installations:

TERNA PLANT AND EQUIPMENT

	December 31, 2005	December 31, 2004
Stations	n. 302	n. 300
Transformers	n. 572 109,968 MVA	n. 569 108,749 MVA
Bays	n. 3,947	n. 3,902
Lines	35,129 km	34,958 km
Double-circuit lines	n. 1,953 38,976 km	n. 1,931 38,696 km

In relation to the number of stations, the two new 150 kV stations at Celle S. Vito and Ulassai came onto stream. With regards to the number of transformers, there was a total increase of 3 units due to the following changes:

- The installation of a new 220 / 132 kV 160 MVA auto-transformer at the Biella East station
- The installation of a new 380 / 132 kV 250 MVA auto-transformer at the Rondissone station
- The installation of a new 380 / 150 kV 250 MVA auto-transformer at the Rome east station
- The installation of a new 380 / 150 kV 250 MVA auto-transformer at the Taranto North station
- The demolition of a 220 / 150 / 15 kV 100 MVA auto-transformer at the Codrongianos station

Overall, the total transformation capacity rose from 108,749 MVA at the end of 2004 to 109,968 MVA, involving a total increase of 1,559 MVA.

As far as power lines were concerned, an increase was seen in the overall length of the double-circuit lines by around 280 km when compared to December 31, 2004. This increase was mainly due to the bringing onto stream of the following new connections:

- 380 kV double-circuit power line (around 42 km) for interconnection with Switzerland (S. Fiorano - Robbia);
- 150 kV Taloro 3 - Taloro 2 and Taloro 2 - Taloro 1 lines (for an approximate total of 14 km);
- 380 kV Altomonte - Feroletto line (approximately 105 km);
- 380 kV Feroletto - Rizziconi line (approximately 67 km);
- 150 kV Celle S. Vito - Montefalcone line (approximately 21 km);
- 380 kV SET - S. Maria Capua Vetere line (approximately 3 km).

OPERATING AND FINANCIAL REVIEW

The financial statements as of December 31, 2005 closed with net income of € 268.0 million, after having provided amortization and depreciation on fixed assets amounting to approximately € 157.4 million, net financial expense of € 9.9 million, net extraordinary expense of € 7.6 million and income taxes totalling € 160.8 million.

The value of production amounted to around € 1,675.4 million, of which € 864.9 million for sales and services mainly referable to the payment due to the company for use of the National Transmission Grid, and € 740.8 million relating to other energy revenues of a transitory nature. More specifically, on the basis of the calculations deriving from the application of the Electricity and Gas Authority's Resolution No. 05/04 and taking into account the effect of the conferral of the business segment by GRTN, fees for grid rental have been assessed for a total of around € 786.8 million, involving a decrease of approximately € 24 million (+ 3%) when compared to the same period in 2004.

Production costs amounted to around € 1,229 million, of which € 740.8 relating to purchase costs and services energy items of a transitory nature, € 176.9 million relating to staff and € 157.4 to amortization/depreciation.

Net extraordinary expense totalling approximately € 7.6 million, was essentially attributable to the charges for the redundancy incentives.

Income taxes for the year, amounting to € 160.8 million, include € 136.6 million for IRES (corporate income tax) and € 28.6 for IRAP (regional tax on productive activities); net prepaid taxes were also recorded for € 2.7 million in addition to net deferred taxes of € -7.1 million.

The balance sheet discloses net tangible fixed assets amounting to € 4,002.5 million, net capital employed of € 3,710.1 million covered by shareholders' equity amounting to € 1,866.0 million (50.3%, compared to 54.0% as of December 31, 2004) and by net financial debt of € 1,844.1 million (49.7%, compared to 46.0% as of December 31, 2004). Terna SpA's reclassified income statement for 2005 and 2004 is summarized in the following table, obtained by classifying the data presented in the income statement and adding the transitory revenues and costs.

THE MANAGERIAL ECONOMIC ACCOUNT OF TERNA SPA

In millions of Euro	2005	2004	Change
REVENUES			
Energy revenues margin items	793.7	810.8	-17.1
Other sales and services	71.2	62.8	8.4
Other sundry revenues and income	43.2	32.0	11.2
Total Revenues	908.1	905.6	2.5
OPERATING COSTS			
Payroll and related costs	176.9	163.2	13.7
Services and use of third-party assets	107.8	115.3	-7.5
Materials	23.9	20.0	3.9
Other costs	21.3	28.7	-7.4
Capitalized costs	-26.5	-22.5	-4.0
Total operating costs	303.4	304.7	-1.3
Gross Operating Margin	604.8	600.9	3.9
Amortization and depreciation	157.4	143.4	14.0
Accruals	1.1	10.4	-9.3
Total amortization, depreciation and accruals	158.4	153.8	4.6
OPERATING INCOME	446.4	447.1	-0.7
FINANCIAL ITEMS			
Income	44.4	34.9	9.5
Expense	58.7	47.2	11.5
Exchange gains/(losses) and Revaluations/(Writedowns) of equity investments	-4.4	4.9	-9.3
RESULT BEFORE EXTRAORDINARY ITEMS AND TAX	436.5	429.9	6.6
Net extraordinary income/(expense)	7.6	-409.6	417.2
INCOME BEFORE TAXES	428.9	839.5	-410.6
Income taxes for the period	160.8	165.2	-4.4
NET INCOME FOR THE PERIOD	268.0	674.3	-406.3

Revenues amounting to € 908.1 million disclosed an increase of € 2.5 million, divided up as follow

- Energy revenues margin items - € 17.1 million;
 - lower revenues amounting to approximately € 36.9 million for the grid usage fee essentially attributable to the tariff process (zone effects, Cross Border Trade and adaptation of NTG ownership percentage);
 - greater revenues deriving from the activities pertaining to the acquisition of the TSO business segment amounting to around € 19.8 million;
- Other sales and revenues up € 8.4 million, essentially attributable to the freeing up of revenues for contract work in progress concluded and inspected during the year totalling € 21.9 million, offset by lower services provided to Enel Group companies, with particular reference to the contract for the maintenance of the high voltage power lines belonging to ENEL Distribuzione.

- Other sundry revenues and income, up € 11.2 million essentially attributable to :
 - greater out-of-period income amounting to € 32.4 million, registered for adjustments on the grid rental fee for the years 2002/2004 (around € 19.9 million) and the freeing up of provisions for risks and charges (approximately € 15.0 million)
 - minor changes in contract work in progress for around € 15 million, essentially attributable to the completion of the SCTI project
 - lower operating grants and other sundry revenues for a total of around € 5 million.

Operating costs amounting to around € 303.4 million, disclosed a slight drop when compared to the previous year by around € 1.3 million which derives from the algebraic sum of:

- Higher payroll and related costs by around € 13.7 million essentially attributable to;
 - the additional cost (around € 8 million) consequent to the inclusion of the human resources forming part of the GRTN “transmission and dispatching” business acquired on November 1, 2005
 - the charges pertaining to the year for the long-term incentive plan (LTI) for around € 3.7 million
 - the higher unit cost
- Greater consumption of materials for approximately € 3.9 million;
- Lower costs for services and other costs, for a total of about € 14.9 million, essentially identifiable in the lower out-of-period income for grid usage fees (€ 15.0 million), higher costs incurred in 2004 for the stockmarket listing of the Company (€ 10.3 million), additional costs for taxes relating to the acquisition of the business segment from GRTN (€ 2.8 million) and for taxes paid abroad which are not deductible in Italy (€ 4.3 million);
- A rise in capitalized costs by around € 4.0 million.

Amortization and depreciation amounting to € 157.4 million, disclosed an increase of around € 14.0 million of which € 5.6 million for intangible fixed assets and € 8.3 million for tangible fixed assets, essentially attributable to the acquisition of the GRTN business segment.

Provisions and accruals amounting to around € 1 million essentially concern the adjustment of the provision for legal disputes.

Net financial expense amounting to around € 9.9 million, disclosed a decrease of € 7.3 million when compared to 2004 and is essentially attributable to:

- Higher financial income of around € 9.5 million, mainly deriving from the additional dividends (€ 5.4 million) and the greater Interest on Equity (€ 3.5 million) deriving from the Brazilian subsidiary;
- Greater financial expense of € 11.5 million made up as follows : a decrease in financial expense due to ENEL SpA by around € 25.6 million, greater interest on the bond issue of about € 53.1 million (which in 2004 had generated interest for just two months), higher interest on EIB loans amounting to around € 1.8 million, greater net income on derivative hedging products totalling approximately € 17.8 million;
- Higher exchange gains amounting to € 4.3 million (of which € 1.7 million realized). During 2004, € 4.8 million had also been recorded in charges for the writedown made on the equity investment in the subsidiary company TSN following the distribution of the 2003 dividends.

Net extraordinary expense amounting to approximately € 7.6 million was essentially attributable to the combined effect of the provisions made during the year for the redundancy incentive (€ 15.2 million) and higher income taxes recorded in the previous year with respect to the liability which effectively emerged as due to the tax authorities at the time of the income tax declaration (€ 5.6 million). The balance of the item in question also disclosed a sharp decrease compared to 2004 for the transactions concerning the elimination of tax interference carried out in the previous year (€ 421.3 million).

Income taxes amounting to approximately € 160.8 million, even if essentially in line with the previous year, underwent a considerable variation, as shown in the table below, between net current and deferred/prepaid taxes as a result of the effects of the new tax legislation on amortization/depreciation (Article 102bis of the Income Tax Consolidation Act) for the assets falling within the similar categories of the electricity sector, as determined by the Electricity and Gas Authority, which anticipates longer useful lives when compared to those envisaged by previous tax legislation.

Specifically, the re-formulation of the determination of the fiscally deductible portion of amortization/depreciation also refers to two additional parameters:

- The original purchase cost of the asset;
- The residual useful life taking into account the “original” placed in relation to the assets, also in the event of the purchase of used or conferred assets.

The incidence of income taxes on pre-tax income came to 37.5%.

Net income for the year therefore amounted to € 268.0 million, disclosing an increase of around € 15.1 million when compared with the 2004 result, net of the tax clean-up.

Euro	2005	2004	Change
Current taxation	165.2	104.5	60.7
Net (Prepaid) Deferred taxation	-4.4	60.7	-65.1
Total	160.8	165.2	4.4

Balance sheet

Terna SpA's reclassified balance sheet for 2005 and 2004 is summarized below, obtained by reclassifying the figures presented in the balance sheet.

BALANCE SHEET OF TERNA SPA

In millions of Euro	2005	2004	Change
NET FIXED ASSETS			
Tangible and intangible	4,156.5	3,848.3	308.2
Long-term financial assets	299.0	308.8	-9.8
Total	4,455.5	4,157.1	298.4
NET WORKING CAPITAL			
Trade receivables	978.6	139.2	839.4
Inventories	17.8	32.6	-14.8
Other assets	70.4	46.4	24.0
Net tax receivables/(payables)	-16.7	-3.2	-13.5
Trade payables	-935.5	-177.4	-758.1
Other liabilities	-302.0	-238.2	-63.8
Total	-187.5	-200.6	13.1
Gross capital employed	4,268.0	3,956.5	311.5
Sundry provisions	-557.9	-550.3	-7.6
Net capital employed	3,710.1	3,406.2	303.9
Shareholders' equity	1,866.0	1,838.0	28.0
Net financial debt	1,844.1	1,568.2	275.9
Total	3,710.1	3,406.2	303.9

Net financial debt is analysed as follows.

TOTAL NET FINANCIAL DEBT

In millions of Euro	2005	2004	Change
Bond issue	1,400.0	1,400.0	0.0
EIB loans	400.0	318.2	81.8
Short-term loans	55.0	0.0	55.0
Novatrans Shareholder Loan	0.0	-6.0	6.0
Bank balances	-15.7	0.0	-15.7
Cash and equivalents on hand	-0.1	-144.0	143.9
RTL intercorporate current account	4.9	0.0	4.9
Total	1,844.1	1,568.2	275.9

The increase of € 308.2 million in the item tangible and intangible fixed assets was sharply influenced by the acquisition of the GRTN business segment. In further detail:

Intangible fixed assets

- The increase of € 154.0 million entirely refers to the assets present within the business segment acquired as of November 1, 2005, which are essentially attributable to the value of the concession totalling € 134.5 million, net of the amortization set aside in the income statement, which came about as the difference between the equity acquired and the price paid for the business segment. The other € 19.5 million concerned costs incurred for the development of the applications software developed internally or acquired as part of the creation of programmes for the development and evolution of the systems.

Tangible fixed assets

The change in this item, € 154.2 million, is analysed in the following table.

In millions of Euro	
Investments	
- Power lines	121.3
- Transformer stations	121.7
- Other	16.4
Total Investments	259.4
GRTN business segment	64.9
Depreciation	-151.7
Net disposals	-4.2
Operating grants pertaining to new plant up and running	-14.2
TOTAL	154.2

The value of the fixed assets acquired together with the TSO business segment from GRTN essentially refers to the National Control Centre in Rome and the various distribution centres present throughout Italy.

The decrease in long-term financial assets (€ 9.8 million) is entirely attributable to the item equity investments and concerns:

- A decrease of € 44.9 million in the value of the equity investment in TSN following the redemption, by Terna SpA, of 175 million preference shares redeemable at a unit redemption value of R\$ 0.94108;
- An increase of € 33.4 million due to the acquisition of the equity investment in the company RTL as of September 30, 2005 which was effective as of December 1, 2005;
- An increase, following the acquisition of the TSO business segment from GRTN, amounting to € 1.7 million, relating to the equity investment in CESI SpA. By means of this acquisition, the shareholding in CESI came to 24.4% and is classified among Equity investments in associated companies.

The net working capital was negative for a total of € 187.5 million, at the end of 2004 it had been negative by € 200.6 million, undergoing a change of € 13.1 million, essentially in line with the previous year. There was a considerable increase in the items Trade receivables and Trade payables which was attributable to the new dispatch activities; these are of a transitory nature.

The increase in provisions by around € 7.6 million, is essentially attributable to the increase in the employee termination indemnity provision (€ 15.3 million) being the consequence of the staff included in the business segment, offset by decreases for the release to the income statement of risk provisions which are no longer necessary.

The net invested capital therefore amounted to € 3,710.1 million, disclosing an increase of € 303.9 million which as already mentioned essentially reflects the net fixed assets.

Financial flows

Cash Flow

STATEMENT OF CASH FLOWS

In millions of Euro	2005	2004	Change
A) OPENING SHORT-TERM FINANCIAL DEBT (-) ASSETS (+)	144.0	289.4	-145.4
Cash and Banks	0.1	0.1	0.0
Intercompany current account	143.9	289.3	-145.4
B) CASH FLOW FROM OPERATIONS			
Net income	268.0	674.3	-406.3
Effects of tax clean-up	0.0	-421.3	421.3
Amortization and depreciation	157.4	143.5	13.9
Net writedowns (revaluations)	0.0	0.0	0.0
Net change in provisions	-7.8	3.9	-11.7
Net change in employee termination indemnity provision	15.3	-10.3	25.6
Net loss (gain) on the disposal of assets	1.6	1.8	-0.2
Cash generated by operations	434.5	391.9	42.6
Change in net working capital			
- (Increase) decrease in net working capital	-854.7	46.6	-901.3
- Increase (decrease) in payables	770.4	-24.0	794.4
- Changes in other balance sheet items	71.2	-23.6	94.8
TOTAL B) - CASH FLOW FROM OPERATIONS	421.4	390.9	30.5
C) CASH FLOW FROM (FOR) INVESTMENT ACTIVITIES			
- Investments in tangible fixed assets	-259.4	-277.8	18.4
- Investments in intangible fixed assets	-4.1	0.0	-4.1
- Other changes in tangible fixed assets	-203.5	31.1	-234.6
- Other changes in long-term financial assets	-0.1	3.0	-3.1
- Changes in equity investments	9.8	-143.2	153.0
TOTAL C)	-457.3	-386.9	-70.4
D) CASH FLOW FROM (FOR) FINANCING ACTIVITIES			
- New medium and long-term loans	155.0	3,093.6	-2,938.6
- Repayment of medium and long-term loans	-12.2	-1,997.9	1,985.7
- Repayment of loans from subsidiary companies	0.0	125.2	-125.2
- Dividends and other capital transactions	-240.0	-1,370.3	1,130.3
TOTAL D)	-97.2	-149.4	52.2
E) CASH FLOW GENERATED FOR THE PERIOD	-133.1	-145.4	12.3
F) CLOSING NET SHORT-TERM DEBT (-)ASSETS (+)	10.9	144.0	-133.1
Cash and Banks	15.8	0.1	15.7
Intercompany current account	-4.9	143.9	-148.8

Net debt position

NET DEBT POSITION

In millions of Euro	2005	2004
OPENING NET FINANCIAL DEBT	-1,568.2	-202
Liquidity generated by operations	421.4	390.9
Investments in tangible and intangible assets	-263.5	-277.8
Decrease/(increase) in equity investments	45.0	-143.8
Disposals (purchases) of equity investments	-35.2	0.6
Other changes in fixed assets	-203.6	34.1
Liquidity absorbed by investment activities	-457.3	-386.9
Dividends distributed	-240.0	-170.2
Increases/decreases in the share capital	0.0	-1,200.0
Shareholders' equity flows	-240.0	-1,370.2
Change in financial debt	-275.9	-1,366.2
CLOSING NET FINANCIAL DEBT	-1,844.1	-1,568.2

The liquidity generated by operations during the period came to around € 421.4 million and is mainly attributable to cash generated by operations during the period (income, amortization/depreciation, provisions - € 434.5 million) as well as to the increase (€ 13.1 million) in net working capital.

Investment activities absorbed net financial resources for around € 457.3 million and concerned a greater number of transactions; in particular, shareholders are informed of the investments in tangible fixed assets for the period (€ 259.4 million), amounts collected due to the redemption of the redeemable shares of the subsidiary company TSN (€ 49 million), the acquisition of the equity investments (RTL SpA for around € 33.4 million and CESI SpA for approximately € 1.7 million) and the tangible and intangible fixed assets acquired together with the TSO business segment (€ 220.4 million). Operating grants and the disposal of assets generated resources of around € 18.4 million.

The absorption of the liquidity of flows of shareholders' equity derives exclusively from the disbursement of dividends to the shareholders (balance for 2004 and advance payment on 2005) during the year. Therefore total liquidity absorbed by investment activities and by flows of shareholders' equity led, during the period, to a total requirement of € 697.3 million covered by liquidity generated by operations for € 421.4 million, while the remaining portion, € 275.9 million, was covered by recourse to new borrowing (amounting to € 142.8 million) and the use of liquidity (€ 133.1 million).

Net financial debt (€ 1,844.1 million) as of December 31, 2005 and the related maturities are as follows:

NET FINANCIAL DEBT AND RELATED MATURITIES

In millions of Euro	Dec. 31, 2005	Dec. 31, 2004	Change
A) MEDIUM/LONG-TERM DEBT			
Bond issue	1,400.0	1,400.0	0.0
EIB loans	370.5	300.0	70.5
Total A)	1,770.5	1,700.0	70.5
B) SHORT-TERM DEBT (LIQUIDITY)			
Bond issue	0.0	0.0	0.0
EIB loans	29.5	18.2	11.3
Shareholder Loan to Novatrans	-	-6.0	6.0
Other loans - Italy	55.0	0.0	55.0
Net position with banks and liquidity - Italy	-15.8	-0.1	-15.7
Net cash position with intercompany current account	4.9	-143.9	148.8
Total B)	73.6	-131.8	205.4
TOTAL A+B	1,844.1	1,5068.2	275.9

OIC 3 – Derivative instruments

When carrying out its activities, Terna is exposed to the risk of interest rate fluctuations. The main source of interest rate risk derives from the components of the net financial debt which generate financial charges. The financial debt strategy is directed towards debt recourse instruments with long maturities which reflect the useful life of the corporate assets, and an interest rate risk hedge policy has been followed, aimed at combining these choices with a regulatory context which in four-year cycles establishes the reference cost of the debt within the sphere of the formula adopted for fixing the remuneration of the RAB.

The instruments used for the hedging therefore comprise, on different maturities, both derivatives which take the debt from fixed rate to floating rate, and derivatives which take the debt from floating rate to fixed rate. All the derivative contracts entered into by Terna, in observance of the risk management policies, satisfy the requirements imposed by national accounting standards and are designated as "hedging". With the aim of reducing the sum total of financial debt subject to interest rate fluctuations and of reducing the cost of funding, plain vanilla types of derivative contracts have been used such as interest rate swaps and interest rate collars. At year end, taking into account the transactions in derivative instruments, the fixed rate portion of Terna SpA's gross total debt came to 66.8% while the fixed rate portion of the net debt came to 67.4%.

All the derivative contracts have a notional and maturity date less than or equal to those of the underlying financial liabilities, so that each change in the fair value and/or the expected cash flows of these contracts is balanced by a corresponding change in the fair value and/or in the expected cash flows of the underlying position.

The table below shows the notional value and the fair value of the derivatives net of the accruals outstanding as of December 31, 2005. The fair value of the derivative instruments is determined by discounting back the expected cash flows to the curve of the market interest rates as of the reference date.

In millions of Euro	NOTIONAL		FAIR VALUE	
	2005	2004	2005	2004
Hedging derivatives on P.O. at fixed rate	1,280.0	1,200.0	106.1	39.0
Hedging derivatives on loans at floating rate	269.0	285.7	-17.8	-18.9
Other hedging derivatives	850.0	650.0	-11.2	-12.6
Total	2,399.0	2,135.7	77.0	7.5

Shareholders are informed that the fair value of the two bond issues, € 600 million maturing in 2014 and € 800 million maturing in 2024, also determined by discounting back the expected cash flows to the curve of the market interest rates as of the reference date, amounted net of the accruals to € 1,498 million.

When carrying out its activities, Terna is exposed to the risk associated with the Euro/Real exchange rate relating to the outstanding equity investments and the repatriation flows of capital. Terna SpA's equity investments held in Brazil are considered to be long-term and of strategic importance, therefore the equity invested is not subject to specific coverage. In relation to the financial flows deriving from Brazil (repatriation of capital and payments of dividends or interest on shareholders' equity) the currency exposure is evaluated from time to time and any transactions hedging the risk of depreciation of the Real are defined. At year end, the intercompany credit, due solely to the interest on capital, came to € 27.2 million and was not subject to hedging.

As far as the risk associated with the management of the liquidity is concerned, given the negative differential normally existing between the lending rate relating to loans and the borrowing rate relating to debt, the financial optimisation activities were targeted at minimizing the position of liquidity compatibly with the requirements of the corporate operations.

RESEARCH & DEVELOPMENT ACTIVITIES

As far as research and development activities which require specific professional skills were concerned, Terna essentially avails of the collaboration of CESI SpA in which it holds a 25% equity investment; during 2005, collaboration was also started up with the University of Bologna.

These activities are always aimed at improving the efficiency of the processes with particular reference to the realization and maintenance of the plants.

The projects of greatest interest developed during 2005 concerned:

- The extension and optimisation of the expert system supporting the power line and station maintenance and overhaul activities, entitled MBI, which besides being a technical database, supports the proposals and the handling of the maintenance operation plans;
- The search for new diagnostic methods for power line insulators and station equipment;
- The realization of a number of on-line transformer monitoring systems;
- The structural design of power line supports;
- The setting up of innovative solutions for reducing electromagnetic fields.

During the latter part of the year, activities were also continued, as launched in 2005 by GRTN and acquired within the TSO business segment, relating to the dispatch activities (which mainly involved CESI SpA the University of Pisa and qualified consulting firms). These activities can be summarized as follows:

- Restarting Plan: simulations under dynamic conditions;
- Review of load Lighting Plan;
- Prototype of new Automatic load Disconnection system (EDA);
- Implementation of new models of continual current connections for the grid simulator;
- New grid monitoring system for the detection and study of grid transients;
- Voltage Regulation System design;
- Realization of Operator Training System.

The related costs incurred by Terna during the year for the collaboration of CESI amounted to around € 3.3 million (of which € 1.6 capitalized).

The following activities are planned for 2006:

- Application and experimentation in the field of on-line diagnostic systems for power line insulators;
- Analysis and experimentation in the field of innovative solutions for reducing electromagnetic fields;
- Further extension with implementation of new functions for the MBI maintenance management system;
- The setting up of additional diagnostic techniques and experiments in the field.

During 2006, in relation to the Dispatching sector, the activities already launched in 2005 will be developed, possibly integrated by further initiatives necessary for the completion of the Defence Plan and the improvement of the simulation instruments.

Innovation

Other activities more fully directed towards practical application for optimising and improving the efficiency of the processes, carried out mainly by means of internal work groups, include:

- Field experimentation and standardization of new work methods under live conditions for power lines: replacement of protection cables, also with fibre optics, and insulator cleaning;
- Experimentation and introduction of work methods under live conditions at electricity stations;
- Experimentation and introduction of work on power lines using helicopters;
- Installation and setting up of innovative systems for the on-line detection of the temperature of conductors aimed at the best use of the same;
- Executive design and supply of materials for the realization of an experimental section of line with conductors featuring a greater transport capacity;
- The search for innovative methods for underground HV cable diagnostics;
- Experimentation on an operative power line of detection methods using helicopter-borne laser systems for monitoring power lines;
- The search for new plant engineering solutions for the construction of electricity stations;
- The search for and set up of HV compact equipment systems;
- The set-up of new criteria for the control of power lines and stations, with the introduction of newly conceived methods, and optimisation of the review criteria for the main station electrical equipment for improving the operating efficiency.

New systems

During 2005, significant measures were carried out within the sphere of the computerized information systems so as to deal with three main requirements:

- Integration between the GRTN business segment (TSO) acquired and Terna
- Support for the core processes and system safety
- Support for the operating processes of the company

Integration between the GRTN business segment (TSO) acquired and Terna

In order to reduce the operative impact of the integration and guarantee the running efficiency, various projects were realized, the most important being:

- Standardization of the administrative and management processes by means of the adoption and the extension of the SAP system, used for some time now within Terna, to TSO as well
- Integration of the settlement systems for TSO energy with the SAP system for the purpose of the integrated and uniform handling of the economic items relating to the energy within the administrative processes.
- Creation of a new institutional internet site which integrates the information contents of the integrated parties.

Support for the core processes and system safety

As far as the core processes are concerned, significant measures have been carried out for improving the efficiency, safety and efficacy of the operating processes:

- Dispatching and Running:
 - Start up of the System for the Control and the Remote Integrated Running of the electricity grid (SCTI) for the Dispatching process, with benefits for the safety of the grid and the integration of the processes.
 - The technical/operating improvement of the computerized information systems supporting the market processes with particular regard to the processes/systems for the planning of the requirement and the assessment of the safety (Forecast), the dispatch of the services for the tertiary regulation of the energy (command system), the settlement of the energy items (settlement, metering, Eneforbil)
 - The structural enhancement of the basic technological infrastructure by means of the realization of specific superabundance on the systems and the business continuity logic telecommunications and the continuation of the disaster recovery projects whose completion is anticipated during 2006
- Plant maintenance:
 - Improvement of the system (Equipment management) for the classification of the equipment by Operating Groups, collation of references and norms for the management, scheduling of the maintenance measures (legal, anticipated by the manufacturers, envisaged by Terna)
 - Integration of the geo-referencing system of the National Electricity Grid (GIS) with SAP for all the operating activities and with the database of the Ministry for the Environment for national mapping. This solution introduced during 2005 will be optimised by means of new functions during 2006.

- Grid design:
 - Completion of the Advanced Station Design System (SDSA) integrated by means of activities for estimating and acquiring external resources with the libraries of the design models of the three voltage levels 380 - 220 - 150kV; this creation will be operatively introduced during the first few months of 2006.

Support for the operating processes of the company

During the year, projects were realized with the purpose of improving the company's control capacity over technical/economic aspects and the efficiency of the purchases, specifically:

- An advanced system was created for supporting the process for the purveying of external resources integrated with SAP and with SDSA systems. The new system was used on three pilot projects during 2005 with a positive outcome and will therefore be extended as from the first few months of 2006;
- The system for the estimation and analysis of the final balances of the plant maintenance and overhaul activities was improved, involving integrations with SAP, MBI, and the Service Quality Observatory
- The System for the Analysis and Reporting of the Maintenance Budget was developed;
- The new Planning System was launched for the management of the corporate budget structured on all the Business units on a consistent basis with the analysis and reporting system of the Maintenance Budget;
- The system for the management and monitoring of the control activities on supplies (MOQ) was created, which includes the scheduling, activity balance, non-compliance handling, preventive action and corrective action phases.

HUMAN RESOURCES

New organizational structure

The exit from the Enel Group and the integration with the business segment acquired from GRTN, determined the need to carry out organization, operational and managerial changes aimed at ensuring the autonomy and full operational functioning of the Company, continuing to guarantee the efficiency, safety and reliability of the national electricity system. On a consistent basis with this outlook, during the initial integration stage Terna adopted a structure characterized by:

- The maintenance of the organizational set up of the GRTN business segment converged within the sphere of an organizational unit (Dispatching Division) set up for this purpose under the Chief Executive Officer;
 - The functional dependence of the staff functions of the Dispatching Division on the company staff functions.
- On a parallel, so as to seize the synergies deriving from the integration within Terna of the activities of the GRTN, the work groups launched during the previous year continued with the activities for:
- Defining the functioning formalities of the processes, both core and support, with a view to full functioning of said processes;
 - Definition of the integration logics and the subsequent rationalization of the organization.

On December 21, 2005, the Board of Directors resolved the new basic organizational structure of the Company, which envisages:

- The establishment of the Italy Operation Division, which is entrusted with responsibility for co-ordinating the activities relating to the planning and development of the grid, dispatching, running and maintenance of the plants;
- The enhancement of the staff functions;
- The focusing of a Division and the business development and international activities.

Headcount

The following table shows a breakdown of the workforce by category. The figures for both years are net of leavers as of December 31 (amounting to 59 as of December 31, 2005 and 25 as of December 31, 2004). The increase in the headcount is due to the inclusion, on October 1, 2005, of 34 individuals (5 middle management, 19 office staff, 10 workers) due to the acquisition of ACEA Trasmissione and the inclusion, as of November 1, 2005, of 586 individuals (36 senior management, 179 middle management, 371 office staff) of the TSO business segment acquired from GRTN. Terna's headcount as of December 31, 2005 net of these inclusions (and related evolution) would have come to 2,782 units, involving a reduction of 89 units when compared to December 31, 2004.

BREAKDOWN OF THE WORKFORCE

	Dec. 31, 2005	Dec. 31, 2004	Change
Senior management	74	34	40
Middle management	403	221	182
Office staff	1,813	1,467	346
Workers	1,098	1,149	-51
Total	3,388*	2,871	517

*Including ACEA Trasmissione and TSO business segment staff

With regards to the **training and development of resources**, during 2005 efforts were concentrated on the objective of consolidating and increasing the wealth of distinctive skills within the sphere of the core business, by means of intense and targeted specialist training activities addressing line workers, in particular on the contents concerning technological innovations and work methods.

On a parallel, specialist training activities were increased for staff workers, so as to support the requirements for increasing the skills required by the changes underway. The commitment was also considerable for the training of newly employed workers according to a plan which developed their organizational abilities (team working, communication, working by objectives, etc.), their business orientation (basic economics), and the technical-professional know-how inherent to the business context in which Terna operates.

As far as managerial training was concerned, alongside a programme for the development of “people management” skills, aimed specifically at line middle management, a plan of personalized initiatives has been launched (managerial development programmes selected from Italian and European Business School prospectuses). During 2005, 2,878 resources participated in at least one training course (including the post-integration phase with GRTN).

Furthermore, during the first six months of 2005, within the sphere of the initiatives supporting the Terna-TSO business segment integration process, joint training activities on the subject of the Corporate Governance of listed companies were achieved and saw the participation of management and specialists from the two companies.

Again within the sphere of the activities supporting the Terna-TSO business segment integration process, on the subject of **internal communication** a comparative survey was carried out at the start of 2005 into the organizational culture of the two companies, involving all the staff with the aim of furthering maximum participation in the changeover process and identifying spheres of action in order to support the imminent integration process. The process for the re-definition of policies and action plans (on the subject of professional system, development, education and training, compensation, etc.), on a consistent basis with the changed

context, was launched starting off from the activities for the evaluation of the intellectual capital and risk management activities, which also included the preliminary mapping of the distinctive expertise of the company.

Long-term incentive systems

With regards to the managerial incentive systems, alongside confirmation of the extension of the MBO to all middle management, on May 9, 2005 the Board of Directors voted for the adoption of the first stock option plan intended for Terna Spa executives and/or those of its subsidiaries pursuant to Article 2359 of the Italian Civil Code, covering the most significant functions for the purposes of the achievement of the Company's strategic results.

On December 21, 2005, with reference to the proposals presented by the Remuneration Committee, the Board of Directors also voted for the adoption of the stock option plan for 2006, intended for executives of the Terna Group who cover the most significant functions for the purposes of the achievement of the Group's strategic results. The beneficiaries also include the Chief Executive Officer, since he is an executive of the company. With regards to the executives not involved in this plan, the implementation of a long-term incentive plan (LTI) was decided, linked to the achievement of challenging long-term objectives, whose specific content matter (objectives, parameters and result/bonus correlation curves) were established during the first few months of 2006.

Regulations of the first stock option plan (resolved on May 9, 2005)

The plan anticipated the offer of 9,950,000 options to be distributed, in total, to around 20 executives, belonging to Terna Spa and/or its subsidiaries pursuant to Article 2359 of the Italian Civil Code, who cover the most significant functions for the purposes of the achievement of the Company's strategic results. The overall number of the beneficiaries also includes the GRTN executives who subsequently joined Terna; the Plan was intended to be extended to the latter individuals at the time of the merger under the same terms and conditions, with the exception of the subscription price which was established at the time of the offer itself to the executives, according to the formalities indicated below. Since the acquisition of the business segment from GRTN only effectively took place as of November 1, 2005 steps were not taken to extend the plan to the executives originating from GRTN.

The regulations of the stock option plan:

- 1 • Envisaged that the strike price of each share was determined to the extent equal to the arithmetic average of the reference prices of ordinary Terna SpA stock struck by Borsa Italiana SpA's screen-based system in the period running from the date of the offer and the same day of the previous calendar month;
- 2 • Defined the following as the conditions for the exercise of the options - having the nature of abeyance conditions:
 - (a) the Terna SpA. Group EBITDA relating to the year of allocation (2005) and indicated in the Group budget approved by the Board of Directors, is to have been exceeded;
 - (b) the percentage change between the reference price of the Terna SpA. stock reported by Borsa Italiana SpA's screen-based system as of January 1, in the year in which the allocation of the options took place and the same price as of December 31, of the same year, must be greater than the percentage change reported in the same period of time by the Reference Index (50% MIBTEL and 50% FTSE 300 Electricity). For the purposes of this calculation, both the percentage change of the reference price of the Terna SpA stock and the percentage change of the Reference Index will be adjusted in order to take into account the effect of the distribution of the respective gross dividends (ordinary and extraordinary including therein any bonus allocations of shares), within a logic of Total Shareholders' Return. The regulations of the stock option plan laid down that both exercise conditions described above would have to be met for the exercise of the options themselves by the beneficiaries to be possible.
- 3 • Meant that the subscription of the shares, at a price equal to the "strike price", is the entire responsibility of the beneficiaries, since the plan does not anticipate any concession in this connection;
- 4 • Laid down that the options, if the exercise conditions are achieved, can be exercised (i) in relation to a portion of 30% as from the year following that of allocation, (ii) in relation to a portion of 60% as from the second year following that of allocation and (iii) in relation to a portion of 100% as from the third year following that of allocation. All the options allocated and which have become exercisable must be exercised by March 31, 2010. The options can be effectively exercised only on open stockmarket days including the last 10 days of each month, unless these fall within the 3 open stockmarket days prior to the so-called "coupon detachment" or in the two "blocking periods", lasting one month each, established in proximity of the approval of the draft statutory financial statements and the interim report by the Board of Directors.

During the first half of 2005, the application of the stock option plan led to the allocation of 3,899,000 options, characterized by a strike price of € 2.098, to 9 executives of the Company. On March 15, 2005, on the basis of the indications provided by the Remuneration Committee, the Board of Directors ascertained that the second of the exercise conditions indicated in point 2 above had not been met and therefore, on the basis of the matters envisaged by the Regulations of the stock option plan, it declared the options assigned could not be exercised.

Regulations of the stock option plan for 2006 (resolved on December 21, 2005)

The plan anticipates the offer of a maximum number of 10,000,000 options, to be distributed to around 20 executives belonging to the Terna Group, who cover the most significant functions for the purposes of the achievement of the Group's strategic results, also including the Chief Executive Officer, since he is an executive of the company.

The approved regulations of the stock option plan:

- 1 • Anticipate that the strike price of each share is determined to the extent equal to the arithmetic average of the reference prices of ordinary Terna stock struck by Borsa Italiana SpA's screen-based system in the period running from the date of the offer and the same day of the previous calendar month;
- 2 • Identify two performance parameters whose achievement is a condition for the exercise of the options and, therefore, the right to subscribe the newly issued Terna ordinary shares, and precisely:
 - (a) the Terna Group EBITDA relating to the year of allocation (2006) and indicated in the Group budget approved by the Board of Directors, is to have been exceeded;
 - (b) the performance of each beneficiary during 2006 has been assessed favourably by the Chief Executive Officer, with the expectation of a reduction of 50% of the options which can be exercised by the individual beneficiary in the event of failure to meet this second condition.
- 3 • Lays down that the options, if the exercise conditions are achieved, can be exercised, by the respective beneficiaries, by March 31, 2010 and within the limits of the following maximum quantities: (i) in relation to a portion of 30% of the options which can be exercised, as from the date which will be indicated in the communication confirming that the exercise conditions have been met, (ii) in relation to a portion of 60% of the options which can be exercised, as from the first day of the first calendar year following that of communication confirming that the exercise conditions have been met, (iii) in relation to a portion of 100% of the options which can be exercised, as from the first day of the second calendar

year following that of communication confirming that the exercise conditions have been met. The options can be exercised only on open stockmarket days included in the last 10 days of each month; the faculty to exercise the options will be suspended (i) in the period running between the third to last and last open stockmarket day prior to the so-called "coupon detachment"; (ii) in the period running between the date anticipated for the approval of the draft statutory financial statements by the Board of Directors and the same day of the previous month; (iii) in the period running between the date anticipated for the approval of the interim report by the Board of Directors and the same day of the previous month.

As of December 21, 2005, the application of the 2006 stock option plan led to the allocation of 9,992,000 options characterized by a strike price of € 2.072, to 17 executives of the Company. Verification of the achievement of the exercise conditions will be made by the Board of Directors at the time of the approval of the draft financial statements for 2006.

RELATED PARTIES

Related parties were identified taking as reference the provisions of Article 2 of the CONSOB Issuers' Regulation pursuant to CONSOB resolution No. 14990 dated April 14, 2005 as well as international accounting standard IAS 24 concerning financial statement disclosure on transactions with related parties. With regard to the Company's transactions during the 2005 accounting period, the related parties are represented by the transactions with the subsidiary companies TSN-Transmissora Sudeste Nordeste S.A., Novatrans Energia S.A. and R.T.L. SpA and with the associated company CESI SpA.

The transactions carried out by Terna with the related parties RTL SpA and CESI SpA mainly concern the exchange of goods, the provision of services, the borrowing and lending of financial resources, the coverage of insurance risks, assistance activities concerning staff organization and management, as well as administrative, tax, legal and corporate assistance. All the transactions form part of the ordinary operations and are regulated on an arms'-length basis, in other words at conditions which would be applied between two independent parties.

As far as the Brazilian subsidiaries are concerned, by contrast, economic transactions and the related balance sheet asset balances outstanding as of December 31, 2005, derive from the so-called Interest on equity (IOE), the financial income due to the Parent Company by way of remuneration of the capital invested and paid out periodically against specific authorization of the local financing banks (BNDES-IDB) and the Brazilian Central Bank.

Lastly, shareholders are reminded that within the sphere of the corporate governance regulations which the Company has adopted and which are detailed in the specific section of this Report on Operations, the conditions have been anticipated for ensuring that the transactions with related parties are carried out in observance of the criteria of procedural and substantive correctness.

Transactions with related parties are indicated in the explanatory notes within the commentary to the individual balance sheet items and summarized in the specific section "Transactions with related parties" to which reference should be made.

Disclosure on the shares held by the Directors and the Statutory Auditors is presented below:

Pursuant to the matters laid down by Article 79 of CONSOB Resolution No. 11971/99, the table below presents a list of the Terna SpA shares and the shares of its subsidiary companies held by the Directors and by the Statutory Auditors, as well as by the spouses not legally separated and by dependent children, directly or via subsidiary companies, trust companies or third parties, emerging from the shareholders' register, communications received and information acquired by said Directors and Statutory Auditors. Therefore, all the individuals who during 2005 covered the offices of Director or Statutory Auditor are included.

DISCLOSURE ON THE SHARES HELD BY DIRECTORS AND THE STATUTORY AUDITORS

	Investee company	N. of shares held at the end of the previous year (2004)	N. of shares acquired (in 2005)	N. of shares sold (in 2005)	N. of shares held at the end of the current year (2005)	Title ⁽¹⁾
Luigi Roth ⁽²⁾	Terna SpA	0	0	0	0	-
Flavio Cattaneo ⁽²⁾	Terna SpA	0	0	0	0	-
Luigi De Paoli ⁽²⁾	Terna SpA	7,805 ⁽³⁾			7,805 ⁽³⁾	owned
Mario Garraffo ⁽²⁾	Terna SpA	0	0	0	0	-
Carmine Macrì ⁽²⁾	Terna SpA	0	0	0	0	-
Piero Giuseppe Maranesi ⁽²⁾	Terna SpA	0	0	0	0	-
Massimo Ponzellini ⁽²⁾	Terna SpA	2,000	0	0	2,000	owned
Franco Smurro ⁽²⁾	Terna SpA	0	0	0	0	-
Salvatore Machì	Terna SpA	0	0	0	0	-
Massimo Romano	Terna SpA	12,000	1,200 ⁽⁴⁾	0	13,200	owned
Fulvio Conti ⁽⁵⁾	Terna SpA	12,000			12,000	owned
Sergio Mobili ⁽⁵⁾	Terna SpA	0	0	0	0	-
	RSN - Transmissora Sudeste Nordeste S.A.	1	0	0	1	owned
	Novatrans Energia S.A.	1	0	0	1	owned
Luca Arnaboldi ⁽⁵⁾	Terna SpA	0	0	0	0	-
Paolo Cantarella ⁽⁵⁾	Terna SpA	0	0	0	0	-
Davide Croff ⁽⁵⁾	Terna SpA	0	0	0	0	-
Claudio Machetti ⁽⁵⁾	Terna SpA	12,000	1,200 ⁽⁴⁾	13,200	0	owned
Paolo Ruzzini ⁽⁵⁾	Terna SpA	12,000	0	0	12,000	owned
Salvatore Sardo ⁽⁶⁾	Terna SpA	12,000	0	0	12,000	owned
Giovanni Ferreri	Terna SpA	0	0	0	0	-
Giancarlo Russo Corvace	Terna SpA	0	0	0	0	-
Roberto Tasca	Terna SpA	3,000	0	0	3,000	owned
Bruno Franceschetti ⁽⁷⁾	Terna SpA	0	0	0	0	-
Daniela Gallucci ⁽⁸⁾	Terna SpA	0	0	0	0	-
Fabrizio Orazi ⁽⁸⁾	Terna SpA	0	0	0	0	-

⁽¹⁾ This column - added to the format of attachment 3C anticipated by Article 79 of CONSOB resolution No. 11971/99 for providing the indications requested - shows if the equity investment is owned, pledged, under usufruct, deposited, carried over, etc.

⁽²⁾ In office as from November 2, 2005

⁽³⁾ Of which: 5,204 personally and 2,601 by spouse

⁽⁴⁾ Assigned by way of share bonus

⁽⁵⁾ In office until November 2, 2005

⁽⁶⁾ In office until June 30, 2005

⁽⁷⁾ In office, as Acting Auditor, until April 1, 2005

⁽⁸⁾ In office until April 1, 2005

CORPORATE GOVERNANCE

Section I: governance structure

Introduction

The corporate governance system in existence within the Company is consistent with the principles contained in the Code of Self-governance for listed companies, with the recommendations formulated by the CONSOB on the subject and, more generally, with the best practice established internationally.

This corporate governance system essentially has the aim of creating value for the shareholders, in awareness of the social importance of the activities which the Group is involved in and the consequent need to adequately consider, with regards to related performance, all the interests involved.

Shareholding set up

The Company's share capital is entirely made up of ordinary shares, which are completely unrestricted and endowed with the right to vote both during ordinary general meetings of the shareholders and extraordinary sessions. On the basis of the results of the shareholders' register and the information available, no body - with the exception of Cassa Depositi e Prestiti SpA (joint-stock company owned by the Ministry of the Economy and Finance of the Italian Republic) holder of 29.9% of the share capital, Enel SpA holder of 6.142% of the share capital and the Assicurazioni Generali Group, holder of 5.042% of the share capital - holds an interest in the share capital greater than 2%, in addition, there is no evidence of shareholders' agreements covering the Company's shares.

Organization of the Company

In accordance with the matters laid down by Italian legislation concerning listed companies, the organization of the Company features the presence of:

- A Board of Directors appointed to see to the corporate management;
- A Board of Statutory Auditors required to (i) oversee the observance of the law and the memorandum of association, as well as the observance of the correct principles of administration when performing the corporate activities and (ii) also check the adequacy of the Company's organizational structure, internal auditing system and administrative-accounting system as well as perform all the duties attributable to the Board by law;
- The shareholders' meeting, responsible for resolving amongst other things - in ordinary and extraordinary

session - with regards to (i) the appointment and removal of the members of the Board of Directors and the Board of Statutory Auditors and concerning the related remuneration and responsibilities, (ii) the approval of the financial statements and the allocation of the net income, (iii) the acquisition and disposal of own shares, (iv) the amendments to the Articles of Association, (v) the issue of convertible bonds.

The accounts auditing activities are entrusted to a specialized company, duly enrolled in the CONSOB register, specifically appointed for this purpose by the general meeting of the shareholders subject to the agreement of the Board of Statutory Auditors.

The company appointed to audit Terna's accounts performs the same role for the subsidiary companies. In accordance with the provisions of the Ethical Code adopted by the Company, the auditing of the Company's statutory financial statements and the consolidated financial statements is incompatible with the performance of consulting activities provided to Terna or its subsidiaries, such incompatibility extending to the entire network of the Independent Auditing Firm.

Section II: implementation of the provisions of the Code of Self-governance for listed companies and other information

Board of Directors

Role and functions

The Company's Board of Directors covers a central role within the sphere of the corporate organization and it heads up the functions and responsibilities of the strategic and organizational policies, as well as the verification of the existence of the controls necessary for monitoring the performance of the Company and its subsidiaries. Within this context, and on the basis of the matters laid down by the law and that which is anticipated by its own specific resolutions, the Board of Directors:

- Grants and withdraws powers of attorney to an Executive Committee and/or to one or more Directors, establishing the content, limits and any operating formalities.

The current Board structure provides for the presence of just one Chief Executive Officer. On the basis of the current powers of attorney, the Chief Executive Officer is vested with the widest powers for the management of the Company, with the exception of those otherwise assigned by the law, the Articles of Association or reserved for the Board of Directors on the basis of the resolutions of the latter body described hereunder;

- Receives, on the same basis as the Board of Statutory Auditors, on-going and comprehensive disclosure from the Chief Executive Officer regarding the activities carried out when exercising the powers of attorney, summed up on a quarterly basis in a specific report. Specifically, as far as all the transactions of greatest significance are concerned (including therein any atypical or unusual transactions or those with related parties, whose approval is not reserved for the Board of Directors), the Chief Executive Officer reports to the Board itself with regards to (i) the characteristics of said transactions, (ii) the parties involved and their possible correlation with the Company or its subsidiaries;
- Establishes, on the basis of the proposals formulated by the specific committee and having heard the opinion of the Board of Statutory Auditors, the remuneration of the Chief Executive Officer and the other Directors who cover specific offices;
- Defines and assesses the adequacy of the general organizational and administrative set-up of the Company and its subsidiaries;
- Examines and approves the strategic, industrial and financial plans. From this point of view, the current structure of the powers within the Company anticipates, in particular, that the Board of Directors resolves on the approval of the annual budget and the Company's long-term plans (which in aggregate form also contain the annual budgets and the long-term plans of the subsidiary companies) drawn up by the Chief Executive Officer;
- Examines and approves the transactions of significant economic, equity and financial importance, especially if carried out with related parties or otherwise featuring potential conflicts of interest. More specifically, the following are dependent on the prior approval of the Board of Directors: (i) the approval of the grid development plan proposal, (ii) the purchase and sale of equity investments in other companies, (iii) the stipulation of agreements (with Ministries, Local Bodies, etc.) of particular strategic relevance for the Company or for amounts greater than € 10 million, (iv) the approval of investments and the stipulation of contracts of a significant size (by this we mean in general those with a value greater than € 20 million, with the exception of contracts concerning the dispatch activities and all the related services, while this threshold is reduced to € 2 million for infraGroup contracts, with the exception of contracts concerning the dispatch activities and all the related services), (v) the participation in bids for tenders which involve a commitment greater than € 5 million, (vi) the issue of bonds, (vii) the issue of fidejussory and secured guarantees for amounts greater than € 5,000,000 per individual transaction, not envisaged by the budget and by the approved financial plans, (viii) purchases, exchanges, disposals of property assets and leases over nine years for amounts greater than € 1,000,000, not envisaged by the budget and by the approved financial plans, (ix) the stipulation of management consultancy contracts for a unit amount of more than € 500,000, not envisaged by the budget and by the approved financial plans, (vi) the undertaking of specific decisions on transactions with a unitary level of more than € 1 million;

- Makes arrangements with regards to the exercise of the voting right to be expressed during the general meetings of the subsidiaries and other companies in which investments are held;
- Evaluates the general performance of corporate operations, with particular emphasis on situations of conflict of interest, using the information received from the Chief Executive Officer and from the Internal Auditing Committee and periodically checking the achievement of the scheduled results;
- Reports to the shareholders during general meetings.

Appointment, composition and duration in office

In accordance with the provisions of the Company's Articles of Association, the Board of Directors is made up of between seven and thirteen members, appointed for a period of no longer than three accounting periods and who can be re-appointed at the end of their mandate. It can be supplemented by a Director without the right to vote, whose possible appointment is reserved for the Italian State by virtue of the legislation on privatisations; so far, this power to appoint has not been exercised by the State. The Company's Directors must possess the requisites of respectability and professionalism in common with those applicable to the statutory auditors of listed companies; at least a third of the Directors in office must possess the independence requisites anticipated by the Code of Self-governance for listed companies; in conclusion, the requisites of independence anticipated by Article 10 of EC Directive 2003/54 as laid down in Article 15.5 of the Articles of Association, are applicable to the executive directors, taking into account the specific activities performed by the Company. The Articles of Association also anticipate - by way of implementation of the matters laid down by privatisation legislation, the matters required by the Prime Minister's Decree dated May 11, 2004 and in compliance with the matters envisaged by Italian legislation with regards to listed companies - that the appointment of the entire Board takes place by means of the "list voting" mechanism, aimed at guaranteeing a presence within the management body of members appointed by the minority shareholders to the extent of three tenths of the directors to be elected with rounding off, in the event of a fractional number lower than the unit, to the next unit up. This elective system anticipates that the lists of the candidates may be presented by the outgoing Board of Directors or by the shareholders who, alone or together with other shareholders, represent at least 1% of the share capital. It is also anticipated that the lists be deposited at the registered offices and published in newspapers with a national coverage suitably in advance with respect to the date of the shareholders' meeting - the deadline anticipated is 20 days if the list is presented by the outgoing Board of Directors and 10 days if the lists are presented by the shareholders - thereby guaranteeing a transparent procedure for the appointment of the Board.

In-depth disclosure with regards to the personal and professional characteristics of the candidates, accompanied by indication of the possible suitability of the same to qualify as independent, will be

deposited at the registered offices at the same time as the lists, as well as immediately published on the Company's website, with a specific reference which will be included in the general meeting's notice of convocation.

In conclusion, the Articles of Association also envisage - by way of implementation of the matters requested by the Prime Minister's Decree dated May 11, 2004 - a limit equal to 5% of the share capital for operators of the electricity sector in relation to the right to vote when appointing the Directors.

At present, steps have not been taken to form a specific Committee, as part of the Board, for the appointment proposals since so far no problematic situations have been noted by the shareholders when drawing up adequate candidatures, which would allow a Board composition in line with the matters recommended by the Code of Self-governance for listed companies.

In accordance with the matters resolved by the ordinary shareholders' meeting held on November 2, 2005, the Board of Directors currently in office is made up of ten members, whose mandate will expire at the time of the approval of the 2007 financial statements. In relation to the appointments made during said meetings, the Board currently comprises the following members, whose brief professional resume is presented below, together with indication of the lists they came from:

• *Luigi Roth, 65 years old - Chairman (indicated on the list presented by Cassa Depositi e Prestiti SpA)*

A Business Studies graduate from Bocconi University in Milan. Since 2001, he has been the Chairman of the Fiera Milano Foundation and, since 2004, Deputy Chairman of Cassa Depositi e Prestiti SpA. Currently, he is a Board member of TELECOM Italia SpA. He started his managerial career within the Pirelli Group, carrying out activities both in Italy and abroad. Subsequently, he worked within Metropolitana Milanese as Planning Director. Since 1980 he has run medium-sized companies both in the manufacturing and real estate property sector in the position of General Manager and Chief Executive Officer. From 1986 until 1993, he was Chief Executive Officer of Ernesto Breda SpA; from 1993 until 2001 he was Chairman and Chief Executive Officer of Breda Costruzioni Ferroviarie SpA; from April 1996 until January 1998 he was Chairman of Società Ferrovie Nord Milano SpA; from December 1996 until January 1998, he was Chairman of Società Ferrovie Nord Milano Esercizio SpA; from May 1998 until December 2000 he was Chief Executive Officer of Ansaldo Trasporti SpA as well as Top Manager of the transport section of Finmeccanica SpA.

• *Flavio Cattaneo, 42 years old - Chief Executive Officer (indicated on the list presented by Cassa Depositi e Prestiti SpA)*

An Architecture graduate from the Polytechnic of Milan, he has covered important positions of

responsibility and administration in various Italian companies in the radio-television, services, new technologies, construction, public services and facilities sectors. As from 1999 at the helm of the former Ente Autonomo Fiera Internazionale in Milan as Extraordinary board member, he then saw to its stockmarket listing as Fiera di Milano SpA, becoming Chairman and Chief Executive Officer until 2003. He has been a board member of numerous companies in the energy sector (from 1999 until 2001), including: AEM SpA in Milan (in the office of Deputy Chairman), Serenissima Gas, Triveneta Gas SpA, Seneca S.r.l. and Malpensa Energia. As from April 2003, he was appointed to the senior management of the public television company R.A.I. SpA as General Manager until August 2005.

• *Luigi De Paoli, 56 years old - Director (indicated on the list presented by Cassa Depositi e Prestiti SpA)*

A Nuclear Engineering graduate from the Polytechnic of Milan, Professor of Business economics and management at Bocconi University in Milan and Director of the Masters' course in Environmental economics and management. Director of the IEFE - Institute of Energy and Environmental Economics and Politics and Director of the publication "Economia delle fonti di energia e dell'ambiente (Economics of energy sources and the environment)", as well as member of the scientific committee of Gaz de France and director of AIEE-Italian Association of Energy Economists. He has covered various university lecturing posts both in Italy and abroad. Between June 1999 and May 2002 he was a board member of ENI SpA. A member of various ministerial committees concerned with the development of the national energy sector, restructuring of the electricity sector, public utility services and tariff regulation; since July 2005, he has been a member of the "Commission for natural gas and fuel prices" established at the Ministry of Production Activities. He is the author of many publications in the field of economics and energy.

• *Mario Garraffo, 68 years old - Director (indicated in the list presented by Cassa Depositi e Prestiti SpA)*

A Business Studies graduate from Bocconi University in Milan, he has covered positions of growing responsibility and administration in various Italian companies: Controller and Development Director of La Centrale Finanziaria Generale from 1960 until 1970; Investments Director with the IFI Group between 1970 and 1980; Chief Executive Officer of IFIL-Finanziaria di Partecipazioni between 1980 and 1985; Chairman of IFINT (now EXOR) from 1985 until 1993; Chief Executive Officer of Lazard Italia from 1993 until 1998 and of UNIM-Unione immobiliare between 1998 and 2000; from 2000 until 2004 he was Chairman of General Electric Italia. He is currently Senior Advisor of General Electric Europe and covers the office of Independent Director, member of the Executive Committee and the Remuneration Committee of Recordati SpA as well as Independent Director of Pirelli &C SpA. He is a Trustee of the Johns Hopkins

University in Baltimore and the Johns Hopkins School for Advanced International Studies (SAIS) in Bologna. Chairman of the Bocconi University Alumni Association and member of the Board of Directors of the Donna Gavotte Bocconi Foundation (founding body of Bocconi University).

• *Salvatore Machì, 68 years old - Director (indicated in the list presented by institutional investors)*

Graduate in electronic engineering. Following a specialization course at the Higher Institute of Telecommunications and professional experience gained at Esso and IBM, he joined Enel in 1965. Here he worked until 1999 covering various roles, including the head of the Transmission Division, national head of thermo-electrical production and director of purchasing and contract work. Chief Executive Officer (from July 1999 until April 2000) and, therefore, Chairman (until July 2003) of Gestore della Rete di Trasmissione Nazionale SpA (GRTN), also during this period he was a board director of “Gestore del Mercato Elettrico SpA”. Since March 2003, he has chaired the Board of CESI - Centro Elettrotecnico Sperimentale Italiano SpA, where previously (from July 1999 to October 2001) he covered the role of Chief Executive Officer; he also currently covers the office of board director at Api Energia SpA and, since September 2004, he is also a Board Member of Terna SpA.

• *Carminè Macrì, 56 years old - Director (indicated on the list presented by Cassa Depositi e Prestiti SpA)*

A law graduate from the Rome “La Sapienza” University, he carries out his professional activities as cassation lawyer. Since 1996, he has been Professor of Banking Law and Legislation at the Business Studies faculty of Rome’s second university “Tor Vergata”, after having covered various academic posts until 1986. Between 1997 and 2003, he was a board member of Italgas SpA. For approximately 8 years, he performed consulting activities for the Associazione tra le Casse di Risparmio Italiane (ACRI). Since Autumn 2004, he has been a board member of SUDGEST S.C.a R.L., a company in which the Ministry of Public Functions holds an investment via “Formez”.

• *Piero Giuseppe Maranesi, 64 years old - Director (indicated on the list presented by Cassa Depositi e Prestiti SpA)*

A Physics graduate from Milan University. Since 1990, he had been Professor of Electronics at Milan University and director of a research laboratory after having covered, until 1968, other academic postings also in other Italian universities and frequented research laboratories abroad. He is active within the international scientific community, has undertaken operative roles on behalf of the Institute of Electrical and Electronic Engineers (IEEE), including, between 1990 and 1996, the role of Board Director of IEEE-Power Electronics Society. Chairman of Transparency International Italia in 1995. Between 1997 and

2001, he was Councillor of the Province of Como. He collaborates with industrial companies which operate in the space electronics sector and is the author of numerous scientific publications.

- *Massimo Ponzellini, 55 years old - Director (indicated on the list presented by the Assicurazioni Generali Group)*

Chief Executive Officer of the Istituto Poligrafico e Zecca dello Stato SpA since February 2006 and Deputy Chairman and Chief Executive Officer of Patrimonio dello Stato SpA since November 2002. He is also a Board Director of NA and Banca Nazionale del Lavoro and honorary Deputy Chairman of EIB (European Investment Bank), of which between 1994 and 2003 he was Deputy Chairman and Chief Administrative Officer for loans and finance. During his career he has been a board director of various important industrial groups such as Alitalia (1986-1994) and Finmeccanica (1986-1990). From 1986 until 1990 he was Chief Executive Officer of SOFIN SpA. Between 1990 and 1994 he was a member of the Transitional Team for the formation of the BERS-European Bank for reconstruction and development and following that Director of operations of the Bank. Between 1981-1982 he was General manager of NOMISMA SpA. At IRI, in 1983, he took over the position of senior executive and executive secretary of the Committee for Restructuring and Privatisation and from 1984 until 1986 he was the head of the Strategy and Studies Division.

- *Massimo Romano, 46 years old - Director (indicated in the list presented by Enel SpA)*

From 1990 until 1994 he was head of Institutional Relations at ILVA SpA (IRI Group). Director of External relations of the Lucchini Group from 1994 until 1997, he was employed by Enel in 1997 as director of Institutional Relations. As from 1999 he undertook responsibility for the Institutional and International Affairs Divisions which from February 2004 also integrated the activities of the Regulatory Affairs Division. Member of the management committee of the Istituto di Economia Politica dell'Energia e dell'Ambiente at the "Luigi Bocconi" University in Milan, he also covers the role of senior advisor to the task force for the internationalisation of the Italian manufacturing system set up by the Foreign Office. Member of the Confindustria Council and Management Committee of Assoelettrica, since March 2004 he had also been Board Director of Terna SpA.

- *Franco Smurro, 48 years old - Director (indicated in the list presented by Cassa Depositi e Prestiti SpA)*

A Pedagogy graduate from Rome's "La Sapienza" University. After academic collaboration with the IInd Chair of Special Pedagogy at Rome's "La Sapienza" University between 1986/1987, he started his managerial career within Telecom Italia SpA in the External Affairs Division from 1987 until 1997. From 1997 and until 2001 he carried out consulting activities with the Authority for the Guarantee of

Communications and, until 2002, at Nortel Networks SpA and, at Bull SpA, until 2004. Since May 2005, he had been a Board Director of Asteimmobiliari SpA.

All the Directors dedicate time for a profitable performance of their duties, irrespective of the offices covered outside the Company, since they are fully aware of the responsibilities concerning the position covered; they are kept constantly informed by the competent corporate divisions on the main legislative and regulatory innovations concerning the Company and the exercise of their roles. The directors perform their duties with cognition of the facts and autonomously, pursuing the objective of creating value for the shareholders.

Board meetings and the role of the Chairman

During 2005, the Board of Directors held 9 meetings with an average duration of 2 hours and 20 minutes each, which involved the due participation of the Directors and the presence of the Board of Statutory Auditors.

The Board's activities are co-ordinated by the Chairman. The latter calls the board meetings, establishes the agenda and directs the related business, ensuring that the Directors are provided on a timely basis - with the exception of in urgent cases or in the event of necessity- with the documentation and the information necessary so that the Board may express itself consciously with regards to the business submitted for their examination. He also checks on the implementation of the Board resolutions, chairs the general meeting of the shareholders and - on a par with the Chief Executive Officer - is empowered to legally represent the Company.

The Chairman is also responsible - on the basis of the board resolution dated November 2, 2005 - for the task of (i) taking care of the dealings of the Company in Italy and abroad with the institutions, public and administrative, national and international bodies and authorities, both central and peripheral, financial, banking, insurance and welfare institutions, private bodies and corporate bodies and individuals, seeing to the relative international relations, in co-ordination with the Chief Executive Officer, as well as (ii) overseeing the internal auditing activities.

Non-executive directors

The Board of Directors is mainly made up of non-executive members (in that they lack operating powers of attorney and/or executive roles within the corporate sphere), capable of guaranteeing, by number and authoritativeness, that their opinion may have a significant effect when board decisions are adopted. The non-executive Directors contribute with their specific skills to board discussions, so as to encourage an examination of the business being discussed from different points of view and a consequent undertaking of resolutions which are pondered, aware and in line with the corporate interests.

With the exception of the Chief Executive Officer, the other 9 members of the Board of Directors (Luigi Roth, Luigi De Paoli, Mario Garraffo, Salvatore Machì, Carmine Macrì, Piero Giuseppe Maranesi, Massimo Ponzellini, Massimo Romano, Franco Smurro) must consider themselves to be non-executive.

In this connection, shareholders are informed that the Chairman also does not cover an executive role, in that the indicated and albeit important functions covered in the corporate sphere- associated as much with the role, acknowledged to him by means of the provisions of the Articles of Association, of guarantor of the application of correct corporate governance within the Board of Directors, as with the representative responsibilities assigned to him by the Board itself, and the supervisory responsibilities on the internal auditing activities - do not take on the form of specific operational powers of attorney.

Independent directors

On the basis of the information provided by the individual parties concerned and by way of implementation of the matters recommended by the Code of Self-governance for listed companies, the Board of Directors meeting held on November 2, 2006 certified the existence of the independence requisite as belonging to the following 8 non-executive directors: Flavio Cattaneo, Luigi De Paoli, Mario Garraffo, Salvatore Machì, Carmine Macrì, Piero Giuseppe Maranesi, Massimo Ponzellini, Franco Smurro. Subsequently, during the same meeting, the Director Flavio Cattaneo was appointed Chief Executive Officer of the Company and was granted the necessary operating power of attorney. Consequently, the remaining 7 non-executive Directors are independent.

More specifically, the following Directors are classified as independent:

- (i) those who do not have (directly, indirectly or on behalf of third parties) or have not recently had any economic dealings with the Company, with its subsidiaries, with the Executive Director or with the majority shareholder of such a significance that they might condition the autonomy of their opinion;
- (ii) those who are not holders (directly, indirectly or on behalf of third parties) of shareholdings of such an extent that they would allow said directors to exercise control or significant influence over the Company, not even via participation in shareholders' agreements;
- (iii) those who are not close family members of the Executive Director or parties who found themselves in the conditions indicated above under points (i) and (ii).

Even if the independence of opinion characterizes the activities of all the Directors, executive and non, the presence of Directors who can be classified as "independent" according to the afore-mentioned acceptance of the term - whose role adopts significance both within the Board of Directors and within the sphere of the Committees - is considered to represent a suitable method for ensuring an adequate reconciliation of the interests of all the members of the body of shareholders.

Committees

Remuneration Committee

In 2004 a specific Remuneration Committee was formed as part of the Board of Directors, with the task of setting forth to the Board itself proposals (i) for the remuneration of the Chief Executive Officer and the other Directors who cover specific offices, as well as (ii) for the determination of the criteria for remuneration to be allocated to the Company's top management and that of its subsidiaries, on the basis of the indications of the Chief Executive Officer.

Following the renewal of the Board of Directors, during the meeting held on November 16, 2005, steps were taken to re-establish the Committee and appoint the members. The Remuneration Committee currently comprises Massimo Ponzellini (acting as co-ordinator), Mario Garraffo, Massimo Romano, Luigi Roth and Franco Smurro, all non-executive directors, and most also being independent.

During the 2005 accounting period, this Committee held 6 meetings, which involved the regular participation of the members and an average duration of one hour each. The Remuneration Committee, within the sphere of its responsibilities, aims to perform a prominent role for the purposes of the imminent implementation within the Company of specific stock option plans for management, understood to be incentive and loyalty retention instruments oriented at attracting and motivating resources of an adequate level and experience, further developing the sense of belonging and ensuring over time constant pressure for the creation of value.

In addition, as far as the remuneration of the Chief Executive Officer and the other Directors who cover specific roles is concerned, the Committee, during 2005, took steps to put forward specific proposals to the Board of Directors which anticipate that part of these fees are linked to the economic results achieved by the Company and to the achievement of specific targets.

During the meetings held in 2005, the Remuneration Committee analysed, putting forward the related proposals to the Board of Directors, an incentive system based on a stock option plan addressing the Terna Group's senior management, and the related implementing regulations as well as an incentive plan, intended for the Company's management not involved in the stock option plan, which anticipates the payment of a bonus if, over the medium term, specific income objectives are achieved and a value threshold of the Terna stock is passed.

Internal Auditing Committee

Again in 2004, an Internal Auditing Committee was also formed as part of the Board of Directors, with advisory and proposal-related tasks.

Following the renewal of the Board of Directors, during the meeting held on November 16, 2005, steps were taken to re-establish the Internal Auditing Committee defining, in particular, the following duties:

- Assist the Board of Directors in fixing the lines of policy for the internal auditing system and in periodically checking the adequacy and effective functioning of the latter;
- assess the work plan drawn up by the head of internal auditing and receive the periodic reports from the same;
- Evaluate, together with the administration managers of the Company and with the Independent Auditing Firm, the adequacy of the accounting standards used and their consistency for the purposes of drawing up the consolidated financial statements;
- Evaluate the proposals put forward by the independent auditors for the awarding of the appointment to audit the accounts, as well as the work plan drawn up for the auditing activities and the results illustrated in the report and the advice letter;
- Report at least every six months to the Board of Directors with regards to the activities carried out and the adequacy of the internal auditing system;
- Carry out additional tasks which may be delegated by the Board of Directors, especially as far as dealings with the independent auditors are concerned.

Following the afore-mentioned renewal of the Board of Directors, steps were taken on November 16, 2005 to appoint the members of the Internal Auditing Committee, which currently comprises Mario Garraffo (acting as co-ordinator), Luigi De Paoli, Salvatore Machi, Carmine Macrì and Piero Giuseppe Maranesi, all non-executive and independent directors. During the 2005 accounting period, this Committee held 7 meetings, which involved the regular participation of the members and an average duration of one hour and 35 minutes each, which were attended by the Auditor appointed by the Chairman of the Board of Statutory Auditors, in consideration of the specific supervisory functions over the internal auditing system delegated to said Board by current legislation concerning listed companies. During the 2005 accounting period, the Internal Auditing Committee paused to look in particular at the disclosure to be provided to the Board of Directors concerning the procedures for the transactions with related parties, as well as at the adoption of the IFRS/IAS accounting standards within the corporate sphere and at the consequent adaptation of the computerized information systems. The Committee also examined the lines of policy for the internal auditing system and for the auditing activities, also meeting with the Independent Auditing Firm.

Board of Statutory Auditors

In accordance with the provisions of the Company's Articles of Association, the Board of Statutory Auditors is made up of three acting Auditors and two alternate Auditors, appointed for a period of three years; they can be re-elected

on expiry of their mandate. All the members of the Board of Statutory Auditors must possess the requisites of respectability and professionalism requested by special legislation concerning the auditors of companies with listed shares, being supplemented by means of specific provisions of the Articles of Association; furthermore, on the basis of said Articles of Association, they cannot cover the office of acting auditor in more than four companies which issue securities issued on organized markets. On a similar basis to the matters laid down for the Board of Directors, the Articles of Association anticipate that the appointment of the entire Board of Statutory Auditors should take place by means of the “list voting” mechanism, aimed at guaranteeing a presence within the supervisory body of an acting Auditor and an alternate Auditor appointed by the minority shareholders. This elective system anticipates that the lists of the candidates may be presented by the shareholders who, alone or together with other shareholders, represent at least 1% of the share capital.

It is also anticipated that the lists be deposited at the registered offices and published in newspapers with a national coverage at least 10 days before the date of the general meeting. In order to ensure a transparent procedure for the appointment of the Board of Statutory Auditors, in-depth disclosure with regards to the personal and professional characteristics of the candidates will be deposited at the registered offices at the same time as the lists, as well as immediately published on the Company’s website, with a specific reference which will be included in the general meeting’s notice of convocation.

The Board of Statutory Auditors in office, appointed by the ordinary shareholders’ meeting held on April 1, 2005, has a mandate which will expire at the time of the approval of the 2004 financial statements and currently comprises the following acting members, whose brief professional resume is presented below, together with indication of the lists they come from:

- *Giovanni Ferreri, 71 years old (indicated on the list presented by Enel SpA)*

Graduate in law from the “La Sapienza” University in Rome, he passed his bar exams in 1961 and since 1975 has been a member of the counsel for the defence at the Supreme Court. He is also an auditor and joint-owner with Gianfranco Graziadei of the international law firm Graziadei - Ferreri, with head offices in Rome and branches in Milan, Munich and New York. He also covers the office of Deputy Chairman of A.S. Roma SpA.

- *Giancarlo Russo Corvace, 53 years old (indicated on the list presented by Enel SpA)*

Graduate in business studies from Rome’s LUISS University, he also gained a Masters in Business Administration at the Scuola di Amministrazione Aziendale at Turin University. Business consultant and chartered accountant, until 1985 he carried out his own activities at the Department of Financial Affairs of Banca Nazionale del Lavoro and until 1988 covered the offices of Chief Executive Officer with the

company Ifigest Fiduciaria Sim SpA (now Banca Ifigest). Since 1989 he has been a partner of the law firm Graziadei - Ferreri at the Rome head offices.

- *Roberto Tasca, 44 years old (indicated on the list presented by institutional investors)*

Graduate in Business Economics from the “Luigi Bocconi” commercial university. Since 2001 he has been an Extraordinary Professor of the Economics of Financial Brokers at the Faculty of Economics at Bologna University. Between 1992 and 2000 he covered various university lecturing positions at Bologna University and the Luigi Bocconi University in Milan. He is the author of numerous essays and monographs on various subjects dealing with the economics of financial brokerage, as well as a lecturer at SDA Bocconi and the University of Bologna for various Masters’ courses.

During the 2005 accounting period, the Board of Statutory Auditors held meetings lasting around two hours each on average; said meetings saw the regular participation of the acting auditors.

Internal auditing system

With regards to internal auditing, the Company is equipped with a specific system which is entrusted with the mission of (i) checking the adequacy of the various corporate processes in terms of efficacy, efficiency and economic nature, as well as (ii) guaranteeing the reliability and correctness of the accounting entries and the safeguarding of the corporate equity and (iii) ensuring the compliance of the operating fulfilments with internal and external regulations and the corporate directives and policies which aim to guarantee sound and efficient management.

The internal auditing system is divided up into two separate types of activities:

- The “regular control”, comprising all the control activities which the individual operating units or subsidiary companies carry out on their processes. These control activities are delegated under the primary responsibility of the operational management and are considered to be an integral part of each corporate process;
- The audit, delegated to the specific corporate division of the Company and aimed essentially at identifying and containing the corporate risks of all types by means of monitoring the regular controls, both in terms of adequacy of the controls themselves and in terms of results effectively achieved by the related application. The auditing activities in question are therefore extended to all the corporate processes of the Company and the subsidiary companies and the related managers are informed of both the indication of the corrective action deemed necessary and the performance of follow-up activities intended to check the results of the recommended action.

Responsibility for the internal auditing system falls on the Board of Directors, which takes steps – with the assistance of the Internal Auditing Committee – to fix the lines of policy and to periodically check their adequacy and effective functioning, ensuring that the main corporate risks are identified and handled suitably. The Chief Executive Officer has the task of implementing the policies of the internal auditing system defined by the Board of Directors on the basis of the indications of the specific Committee by means of the planning, management and monitoring of the internal auditing system, for which he appoints a head and ensures the suitability of the means available for the performance of the related activities. The head of internal auditing (identified as the manager of the Company's auditing division) does not depend hierarchically on any operating division manager, co-ordinates the functions delegated to internal auditing within the Company and its subsidiaries and reports regularly on his activities to the Chief Executive Officer and the Chairman as well and, on a six-monthly basis (unless the circumstances require a more timely disclosure), to the Internal Auditing Committee and to the Board of Statutory Auditors.

Transactions with related parties

Within the sphere of the Company and its subsidiaries, the conditions have been prepared for ensuring that the transactions with related parties are carried out in observance of principles of substantive and procedural correctness.

From the point of view of procedural correctness, it is anticipated that, in the presence of such transactions, the Directors who have an interest (even potential or indirect) in the transaction:

- Inform the Board of Directors on a timely basis regarding the existence of said interest, specifying the nature, the terms, the origin and the purport;
- Remove themselves from board meetings at the time of resolution, as long as this does not prejudice the permanence of the constituent quorum.

Furthermore, in such cases, the board resolutions take steps to adequately justify the reasons and the expedience of the transaction.

With regards to substantive correctness – in order to ensure the equity of the conditions stipulated at the time of transactions with related parties and if this should be required by the nature, by the value or by other features of the individual transaction – it is anticipated that the Board of Directors should avail itself of the assistance of independent experts for the valuation of the assets/goods forming the subject matter of the transactions concerned and for the performance of the financial, legal or technical consulting activities.

Handling of confidential information

During the meeting held on April 2, 2004 the Company's Board of Directors approved specific regulations for the handling and processing of confidential information, also containing the procedure for the communication outside the Company of documents and information concerning said Company and its subsidiaries, with particular reference to price sensitive information.

These regulations have the purpose of maintaining the secrecy of the confidential information, at the same time ensuring that the disclosure to the market relating to the corporate information is correct, complete, adequate, timely and non-selective. The Directors and the Statutory Auditors of the Company are obliged to observe the provisions contained in these regulations and in any event to keep the documents and the information acquired during the performance of their tasks confidential.

On a general basis, the regulations place the handling of the confidential information of related pertinence under the responsibility of the Chief Executive Officer of the Company and the delegated bodies of the subsidiary companies, laying down that the disclosure of the information relating to the individual subsidiaries must in any event come about by way of agreement with the Company's Chief Executive Officer.

These regulations also establish specific procedures to observe for the communication outside the Company of documents and information of a corporate nature— dwelling in particular on the disclosure of price sensitive information – and carefully discipline the formalities by means of which the corporate spokesmen enter into contact with the press and other mass media (or with financial analysts and institutional investors).

During the same meeting held on April 2, 2004, the Company's Board of Directors also approved the code of conduct concerning internal dealing, in observance of the regulatory instructions dictated by Borsa Italiana SpA. These instructions oblige companies with listed shares to be transparent in their dealings with the market relating to significant transactions which cover the financial instruments of these same companies or their subsidiaries, transactions which may emerge as carried out by individuals in possession of significant decision-making powers within the corporate sphere and who have access to price sensitive information (so-called "significant individuals").

With respect to the afore-mentioned regulations laid down by Borsa Italiana, the code of conduct adopted by Terna features the following qualifying elements, considered suitable for adequately raising the contents from a qualitative point of view:

- Application of the transparency obligations concerning internal dealing to around forty "significant individuals" within the sphere of the Company and its subsidiaries (in addition to Terna's Directors and the acting Statutory Auditors). In order to ensure an adequate flexibility of the scope of the "significant

individuals”, the possibility of an extension of the afore-mentioned transparency obligations to other parties is also provided for, parties whose identification is submitted for the Chairman and the Chief Executive Officer of the Company separately;

- Halving of the size thresholds of the transactions to be communicated to the market on a quarterly basis (from € 50,000 to € 25,000) or without delay after the related performance (from € 250,000 to € 125,000);
- Application of the transparency obligations also to transactions for the exercise of stock options or purchase options carried out by “significant individuals”;
- Restriction on “significant individuals” prohibiting the performance of transactions (other than those concerning purchase options) during the 30 days which precede the approval of the draft statutory financial statements and the interim report by Terna’s Board of Directors. It is also anticipated that the Board itself may identify additional blocking periods during the year, in concurrence with specific events; setting-up of an adequate sanctioning system to the charge of the “significant individuals” who violate the provisions of the code of conduct.

The regulations for the handling and management of confidential information and the code of conduct concerning internal dealing indicated, are currently being reviewed in view of the enforcement of the recent norms concerning market abuse and the implementing regulations.

Dealings with institutional investors and the body of shareholders

Since the moment of listing of its shares on the stockmarket, the Company believes that the establishment of on-going dialogue, based on the mutual comprehension of the roles, with the body of shareholders as well as with the institutional investors, complies with one of its specific interests, as well as with a duty vis-à-vis the market; dialogue intended in any event to take place in observance of both the procedure for communicating documents and corporate information outside the Company and the principles contained in the “Guide for disclosure to the market”.

In this connection it was ascertained, partly in consideration of the dimensions of the Company, that this dialogue could be facilitated by the creation of dedicated corporate structures.

Steps were therefore taken to establish within the Company (i) an investor relations area, currently located under the staff of the Chief Executive Officer and (ii) an area tasked with conversing with the body of shareholders within the “Corporate Secretariat and Legal Division”.

Furthermore, it was thought to encourage additional dialogue with the investors by means of an adequate set up of the contents of the Company’s website (www.terna.it), on which both information of an

economic-financial nature (financial statements, interim and quarterly reports, presentations to the financial community), and updated information and documents of interest for the body of shareholders (press releases, composition of the corporate bodies, Articles of Association and general shareholders' meeting regulations, information and documents on corporate governance, ethical code, the organizational and management model pursuant to Italian Legislative Decree No. 231/2001) can be found.

General Meetings

The call contained in the Code of Self-governance to consider the general meeting as a privileged moment for establishing profitable dialogue between the shareholders and the Board of Directors (despite the presence of an ample diversification of the communication methods of the listed companies with their shareholders, the institutional investors and the market) has been carefully evaluated and fully shared by the Company, who considered it opportune - in addition to ensuring the regular participation of its Directors in the meetings' work- to adopt specific measures aimed at adequately valorising the general meeting institution.

As a point of fact, partly on the basis of the matters hoped for by special legislation concerning listed companies, steps were taken to introduce specific provisions within the Company's Articles of Association, aimed at facilitating the gathering of the voting proxies from the independent shareholders of the Company and its subsidiaries, thereby encouraging the related involvement in the meetings' decision-making processes.

Furthermore, by means of the general meeting resolution dated March 3, 2004, the Company endowed itself with specific regulations aimed at guaranteeing the orderly and functional course of the general meetings by means of a detailed discipline of the various phases into which it is split up, in observance of the fundamental right of each shareholder to request clarification on the various matters being discussed, to express their opinion and to put forward proposals.

These regulations, despite not taking on the guise of provisions of the Articles of Association, are approved by the ordinary shareholders' meeting by virtue of a specific responsibility assigned to said body by the Articles of Association. The contents of the regulations are aligned to the most evolved standards drawn up specifically by certain trade associations (Assonime and ABI) for listed companies.

Ethical Code

Back in May 2002, Terna's Board of Directors voted for the adoption of the Ethical Code (revised in March 2004), in awareness of the social and environmental implications which accompany the activities carried

out by the Company, and in consideration of the importance covered as much by a co-operative approach with the stakeholders as by Terna's good reputation (both in internal dealings and externally).

This code expresses the commitments and the ethical responsibilities when conducting business, disciplining and adapting the corporate conduct to standards marked with maximum transparency and correctness towards all the stakeholders. In particular, the ethical code is split into:

- General principles in dealings with the stakeholders, which in an abstract manner define the reference values which Terna aspires to when carrying out its activities. As part of these principles, mention is made in particular of: the honesty, impartiality, correctness in the event of potential conflicts of interest, confidentiality, valorisation of the share-based investment, the value of the human resources, the transparency and completeness of the information, the quality of the services, the protection of the environment;
- Criteria concerning conduct towards each class of stakeholders, which specifically provide the guidelines and norms which Enel collaborators are obliged to follow in order to guarantee the observance of the general principles and in order to avoid the risk of non-ethical conduct;
- Implementation mechanisms, which describe the preordained system of control and ensure the observance of the ethical code and its on-going improvement.

As a result of the Enel Group having left the Company shareholding structure and the integration of the GRTN business segment, the Ethical Code adopted by Terna is currently being updated.

Organizational and management model

Back in December 2002, Terna's Board of Directors voted for the adoption of the organizational and management model of the Enel Group (integrated in July 2003) complying with the requirements of Italian Legislative Decree No. 231 dated June 8, 2001, which introduced a system of administrative responsibility (but in fact criminal) within the Italian legal system to the charge of companies for certain types of offences committed by the related directors, executives or employees in the interests or to the advantage of the companies themselves.

On June 24, 2004, Terna's Board of Directors adopted an updated version of this organizational and management model which, despite faithfully following the structure of the previous model in its contents, updates and amends certain provisions in consideration of the stockmarket listing of the Company's shares which took place.

With regards to its layout, the model is split up into three parts:

- A "general part", which contains a description, amongst other things, of the content matter of Italian

Legislative Decree No. 231/2001, the objectives and the functioning of the model, the duties of the internal auditing body called to oversee the functioning and the observance of said model, the information flows, the sanctioning system;

- A “special part A”, concerning the offences committed in dealings with government agencies;
- A “special part “B” relating to corporate offences.

This model is consistent, with regards to the contents, with the matters anticipated by the guidelines drawn up on the subject by trade associations and with the best practice, and represents an additional step towards the uprightness, transparency and sense of responsibility in internal dealings and with the outside world, at the same time offering the shareholders guarantees for an efficient and correct management.

The approved Model is, at present, under review due to the subsequent legislative measures which widened the sphere of the offences envisaged by Italian Legislative Decree No. 231/2001 as well as consequent to the acquisition of the GRTN business segment.

Terna’s Board of Directors Meeting held on December 21, 2005, partly in view of the review underway of the “Organizational and management model pursuant to Italian Legislative Decree No. 231 dated June 8, 2001” adopted by the Company and having considered the dimensions of the Company, approved the variation of the composition of Terna’s Supervisory Body set up in accordance with the same Legislative Decree No. 231/01 as envisaged by the afore-mentioned model, from monocratic to collective.

Three tables are presented below which summarize some of the most significant information contained in the second part of the document.

STRUCTURE OF THE BOARD OF DIRECTORS AND OF THE TERNA COMMITTEES

BOARD OF DIRECTORS						
Office	Members	Executive	Non executive	Independents	(5)	Number of other offices (6)
Chairman	Luigi Roth ⁽¹⁾		●		100%	3
Chief Executive Officer	Flavio Cattaneo ⁽¹⁾	●			100%	-
Director	Luigi De Paoli ⁽¹⁾		●	●	66.6%	-
Director	Mario Garraffo ⁽¹⁾		●	●	100%	4
Director	Carmine Macrì ⁽¹⁾		●	●	66.6%	-
Director	Piero Giuseppe Maranesi ⁽¹⁾		●	●	100%	-
Director	Massimo Ponzellini ^{(1) (2)}		●	●	100%	4
Director	Franco Smurro ⁽¹⁾		●	●	100%	-
Director	Salvatore Machi ⁽²⁾		●	●	100%	2
Director	Massimo Romano ⁽²⁾		●		100%	-
Chairman	Fulvio Conti ⁽³⁾		●		100%	15
Chief Executive Officer	Sergio Mobili ⁽³⁾	●			100%	1
Director	Luca Arnaboldi ⁽³⁾		●	●	66.6%	1
Director	Paolo Cantarella ⁽³⁾		●	●	83.3%	-
Director	Davide Croff ⁽³⁾		●	●	66.6%	1
Director	Claudio Machetti ⁽³⁾		●		83.3%	14
Director	Paolo Ruzzini ⁽³⁾		●		83.3%	2
Director	Salvatore Sardo ⁽⁴⁾		●		0%	-

Quorum requested for the presentation of the lists for the appointment of the Board of Directors:
1% of the share capital

Number of meetings held during 2005:

BoD: 9 Internal Auditing Committee: 7 Remuneration Committee: 6

INTERNAL AUDITING COMMITTEE		REMUNERATION COMMITTEE		POSSIBLE APPOINTMENT COMMITTEE		POSSIBLE EXECUTIVE COMMITTEE	
(7)	(5)	(7)	(5)	(7)	(5)	(7)	(5)
		●	50%	Non existent		Non existent	
●	100%						
●	100%	●	100%				
●	0%						
●	100%						
		●	100%				
		●	50%				
●	100%						
		● ⁽⁸⁾	100%				
●	66.6%						
		●	100%				
●	100%						
		●	50%				
		●	100%				

⁽¹⁾ In office as from November 2, 2005

⁽²⁾ The director was appointed by means of lists presented by the minority shareholders. (You are hereby informed that, for the first time, steps were taken to apply the "list voting" mechanism during the general shareholders' meeting held on November 2, 2005)

⁽³⁾ In office until November 2, 2005

⁽⁴⁾ In office until June 30, 2005

⁽⁵⁾ This column contains indication of the percentage of participation of each Director respectively in the meetings of the Board of Directors and the Committees. All cases of absence have been adequately justified

⁽⁶⁾ This column contains indication of the number of offices as director or statutory auditor covered by the individual concerned in other companies listed on organized markets, abroad as well, in financial, banking or insurance companies or those of significant size

⁽⁷⁾ This column indicates by means of an "●" if any of the Directors belong to Committees

⁽⁸⁾ Member of the Committee as from November 16, 2005

STRUCTURE OF TERNA'S BOARD OF STATUTORY AUDITORS

	Members	Percentage of participation at meetings of the Board of Statutory Auditors (2)	Number of other offices (3)
Chairman	Giovanni Ferreri	100%	1
Acting Auditor	Giancarlo Russo Corvace	100%	-
Acting Auditor	Roberto Tasca ⁽¹⁾ ⁽⁴⁾	100%	-
Alternate Auditor	Bruno Franceschetti ⁽⁴⁾	N.A.	-
Alternate Auditor	Vito Di Battista ⁽¹⁾ ⁽⁴⁾	N.A.	-
Acting Auditor	Bruno Franceschetti ⁽⁵⁾	100%	-
Alternate Auditor	Daniela Gallucci ⁽⁵⁾	N.A.	-
Alternate Auditor	Fabrizio Orazi ⁽⁵⁾	N.A.	-

Quorum requested for the presentation of the lists for the appointment of the Board of Statutory Auditors: **1%**

Number of meetings held during 2005: **7**

⁽¹⁾ The Auditor was appointed by means of lists presented by the minority shareholders

⁽²⁾ All cases of absence have been adequately justified

⁽³⁾ This column contains indication of the number of offices as director or statutory auditor covered by the individual concerned in other companies listed on organized markets

⁽⁴⁾ In office as from April 1, 2005

⁽⁵⁾ In office until April 1, 2005

OTHER PROVISIONS OF THE CODE OF SELF-GOVERNANCE

	YES	NO
SYSTEM OF THE POWERS OF ATTORNEY AND TRANSACTIONS WITH RELATED PARTIES		
Has the BoD assigned powers of attorney defining:		
- <i>limits</i>	●	
- <i>operating formalities</i>	●	
- <i>frequency of the disclosure?</i>	●	
Does the BoD propose to examine and approve the transactions with a particular economic, equity and financial significance (including transactions with related parties)?	●	
Has the BoD defined guidelines and criteria for the identification of the “significant” transactions?”	●	
Are the guidelines and criteria indicated above described in the report?	●	
Has the BoD defined specific procedures for the examination and approval of the transactions with related parties?	●	
Are the procedures for the approval of the transactions with related parties described in the report?	●	
PROCEDURES FOR THE MOST RECENT APPOINTMENT OF DIRECTORS AND STATUTORY AUDITORS		
Did the registration of the candidatures for the office of director take place at least ten days in advance?	●	
Were the candidatures for the office of director accompanied by in-depth disclosure?	●	
Were the candidatures for the office of director accompanied by indication of the suitability of the candidates to qualify as independents?	●	
Did the registration of the candidatures for the office of auditor take place at least ten days in advance?	●	
Were the candidatures for the office of auditor accompanied by in-depth disclosure?	●	
GENERAL MEETINGS		
Has the Company approved General Meeting regulations?	●	
Are the regulations attached to the report (or has it been indicated where they can be obtained/downloaded from)?	●	
INTERNAL AUDITING		
Has the Company appointed a head of Internal Auditing?	●	
Is this individual hierarchically independent from the heads of the operating areas?	●	
Organizational grade of the head of internal auditing ⁽¹⁾		
INVESTOR RELATIONS		
Has the Company appointed a head of Investor Relations?	●	
Organizational unit and references of the head of Investor Relations ⁽²⁾		

⁽¹⁾ Head of the Internal Auditing division

⁽²⁾ *Investor Relations* is the unit entrusted with dealings with the institutional investors.

Investor Relations: Via Arno 64 00198 Rome - Tel. 06.8313 8145 - Fax 06.8313 8389 - E-mail: www.investor.relations@terna.it

The Corporate Secretariat and Legal Division is entrusted with dealing with individual shareholders .

Corporate Secretariat: Via Arno 64 00198 Rome - Tel. 06.83138136 - 06 8313 8376 - Fax 06.8313 8317

E-mail: www.azionisti.retail@terna.it

SIGNIFICANT EVENTS SUBSEQUENT TO THE END OF THE ACCOUNTING PERIOD, OUTLOOK FOR 2006 AND OTHER INFORMATION

Significant events subsequent to the end of the accounting period

FTSE4GGOD Europe Index

On March 10, 2006 Terna was confirmed within the FTSE4GOOD EUROPE, the stockmarket index of the Financial Times Stock Exchange in London, which groups together the best European companies which distinguish themselves with regards to sustainable economic growth.

EMTN (EUROPEAN MEDIUM TERM NOTES) PROGRAMME

In relation to the growth investments envisaged by the business plan and the related requirements, the Board of Directors has resolved to make recourse to the capital market by means of the arrangement of an outline programme for future medium/long-term bond issues (EMTN - programme) for a value of up to € 2 billion.

Advisory Committee

In relation to the Advisory Committee anticipated by the Grid Code, shareholders are informed that subsequent to the end of the accounting period and further to request by Terna sent on December 9, 2005, all the associations most representative of the producers, distributors and wholesale customers, captive and industrial, specifically identified by the MAP, have taken steps to inform Terna of the names of their representatives belonging to said Advisory Committee.

OUTLOOK FOR 2006

During the next accounting period the matters anticipated by the Prime Minister's Decree dated May 11, 2004 will continue to be implemented, specifically in relation to the unification of the National Transmission Grid by means of the acquisition of the portions of NTG owned by other operators.

Particular attention will also be paid to the development of the projects which will permit us to seize cost synergies downstream from the integration of the TSO business segment.

Consolidation will also follow of the Company's expertise relating to the development and maintenance of the National Transmission Grid and the Dispatching activities. The Company will continue to scout, in search of investment opportunities abroad, with particular attention paid to profitability and the limited risk profile. Such action, which the Company intends to pursue, aims to guarantee and increase the creation of value for the shareholder.

Brazil

During 2006, Terna will continue with the stockmarket listing of the Brazilian subsidiaries with the aim of fully expressing the value of the same, permitting access to the local capital market, extending the future growth possibilities in the country and at the same time reducing the direct exposure to risk of Terna SpA.

Human Resources

During the following accounting period, steps will be taken to complete the intervention programmes on organization, the processes and the systems within the sphere of the Terna - TSO business segment integration process.

Furthermore, the new integrated Resource Management and Development system based on the professional system (divided up into areas, families, tasks) and on the skills model, overhauled in light of the new set-up and the new corporate strategic objectives, will be completed with regards to its layout and then implemented.

The focus will be on the maximum valorisation of the Company's Human Capital, with reference to the "distinctive" core business "expertise" and the managerial excellence for the "creation of value".

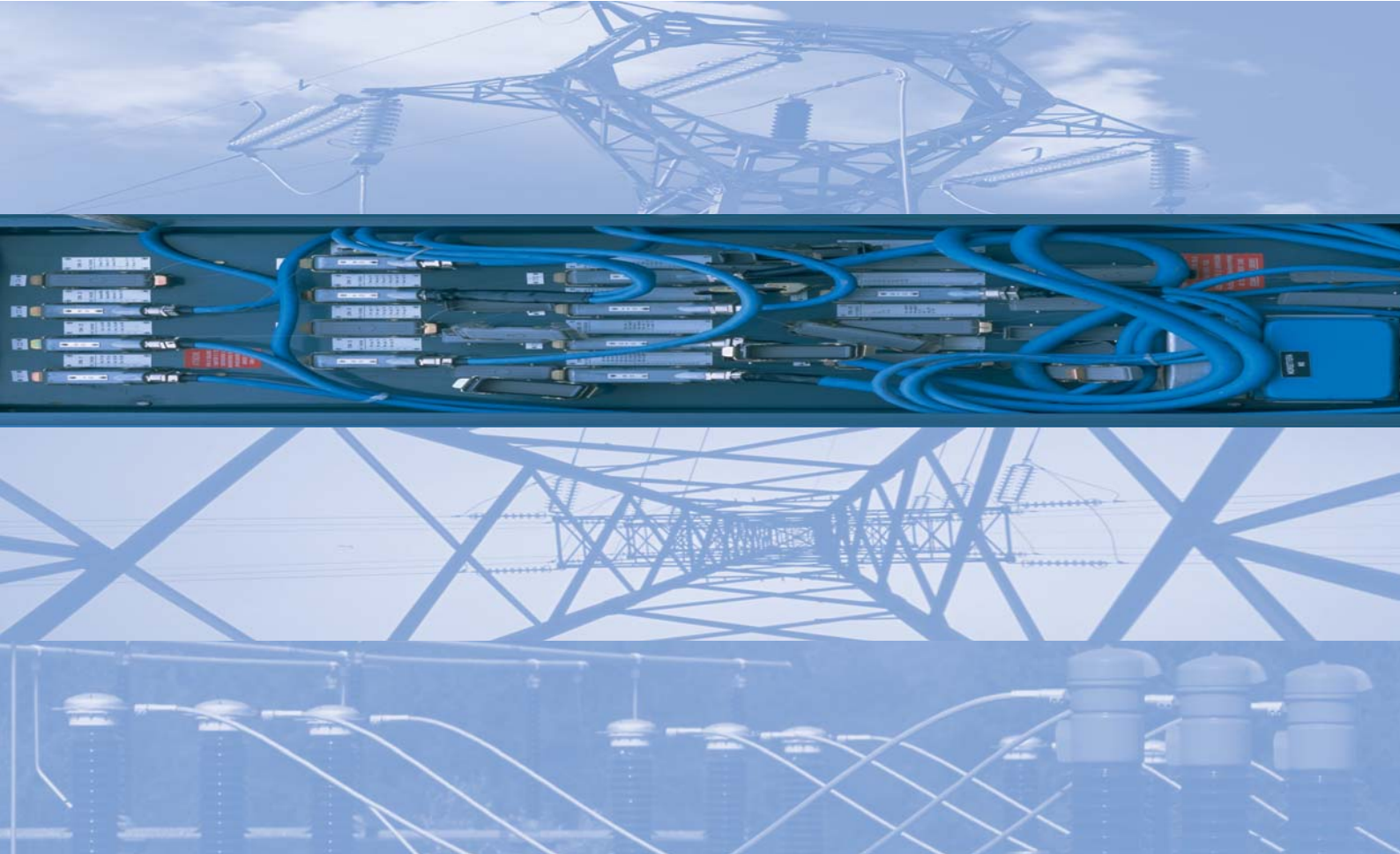
OTHER INFORMATION

Code concerning the protection of personal data (Italian Legislative Decree No. 196 dated June 30, 2003)

During 2003, Terna Spa drew up the Programmatic Security Document in accordance with Italian Presidential Decree No. 318/1999. The document will be updated in compliance with Italian Legislative Decree No. 196 dated June 30, 2003 by the legal deadline anticipated as March 31, 2006.

Own shares

The Company does not hold any own shares or shares in Parent Companies, nor has in acquired or sold any such shares during the accounting period, indirectly or otherwise.



STATUORY FINANCIAL STATEMENTS AS OF DECEMBER 31, 2005

BALANCE SHEET - ASSETS

In millions of Euro	Book values as at 31.12.2005	Book values as at 31.12.2004	Changes for the period
A) SHARE CAPITAL NOT PAID IN	0	0	0
B) FIXED ASSETS:			
I - Intangible assets			
1) Incorporation costs	0	0	0
2) Research, development and advertising	0	0	0
3) Industrial patents and intellectual property rights	0	0	0
4) Concessions, licenses and trademarks	134.496.260	0	134.496.260
5) Work in progress and advances	8.237.582	0	8.237.582
6) Others	11.255.280	0	11.255.280
Total	153.989.122	0	153.989.122
II - Tangible assets			
1) Land and buildings	358.146.411	329.105.450	29.040.961
2) Plant and machinery	3.248.126.260	3.125.465.914	122.660.346
3) Commercial and industrial equipment	12.715.174	12.022.499	692.675
4) Other assets	10.439.078	1.768.198	8.670.880
5) Work in progress and advances	373.063.586	379.975.702	-6.912.116
Total	4.002.490.509	3.848.337.763	154.152.746
III - Financial assets			
1) Equity investments in			
a) subsidiaries	288.493.407	300.007.357	-11.513.950
b) affiliates	4.570.765	0	4.570.765
c) Parent Company	0	0	0
d) others	0	2.866.457	-2.866.457
2) Receivables from			
a) subsidiaries	0	6.012.074	-6.012.074
b) affiliates	0	0	0
c) Parent Company	0	0	0
d) others	5.916.612	5.868.084	48.528
<i>- due within 12 months</i>	<i>834.862</i>	<i>6.444.144</i>	<i>-5.609.282</i>
3) Other securities	0	0	0
Total	298.980.784	314.753.972	-15.773.188
TOTAL FIXED ASSETS B)	4.455.460.415	4.163.091.735	292.368.680

In millions of Euro	Book values as at 31.12.2005	Book values as at 31.12.2004	Changes for the period
C) CURRENT ASSETS			
I - Inventories			
1) Raw materials	7.175.173	10.039.942	-2.864.769
3) Contract work in progress	10.641.957	22.612.806	-11.970.849
Total	17.817.130	32.652.748	-14.835.618
II - Receivables			
1) Trade			
a) sundry items	224.668.616	139.113.562	85.555.054
b) energy-related items	754.068.733	0	754.068.733
2) Subsidiaries	27.599.843	12.651.396	14.948.447
3) Affiliates	120.000	0	120.000
4) Parent Company	0	143.916.271	-143.916.271
4-bis) Tax receivables	5.158.894	12.702.492	-7.543.598
4-ter) Advanced taxes	12.105.321	14.837.169	-2.731.848
5) Others	13.247.572	12.779.211	468.361
- due beyond 12 months	9.435.046	10.997.777	-1.562.731
Total	1.036.968.979	336.000.101	700.968.878
III - Short-term investments			
4) Other equity investments	0	0	0
6) Other securities	0	0	0
Total	0	0	0
IV - Cash and cash equivalents			
1) Bank and post office deposits	15.723.625	0	15.723.625
3) Cash on hand	67.603	92.025	-24.422
Total	15.791.228	92.025	15.699.203
TOTAL CURRENT ASSETS C)	1.070.577.337	368.744.874	701.832.463
D) ACCRUED INCOME AND PREPAID EXPENSES			
1) Accrued income	13.151.142	10.008.219	3.142.923
2) Prepaid expenses:			
- issue discounts	3.000.331	3.169.817	-169.486
- other	13.277.762	8.043.301	5.234.461
TOTAL ACCRUED INCOME AND PREPAID EXPENSES (D)	29.429.235	21.221.337	8.207.898
TOTAL ASSETS	5.555.466.987	4.553.057.946	1.002.409.041

BALANCE SHEET - LIABILITIES AND SHAREHOLDERS' EQUITY

In millions of Euro	Book values as at 31.12.2005	Book values as at 31.12.2004	Changes for the period
A) SHAREHOLDERS' EQUITY			
I - Share capital	440.000.000	440.000.000	0
II - Share premium reserve	0	0	0
III - Revaluation reserve	0	0	0
IV - Legal reserve	88.000.000	84.491.220	3.508.780
V - Reserve for own shares	0	0	0
VI - Statutory reserve	0	0	0
VII - Other reserves			
- capital reserve	396.066.445	396.066.445	0
- earnings	332.617.031	332.617.031	0
VIII - Retained earnings (losses)	441.278.092	522.937	440.755.155
IX - Interim dividends 2005	-100.000.000	-90.000.000	-10.000.000
Earnings (losses) for the year	268.044.434	674.263.935	-406.219.501
TOTAL A)	1.866.006.002	1.837.961.568	28.044.434
B) PROVISIONS FOR RISKS AND CHARGES			
1) Retirement benefits	1.704.973	717.399	987.574
2) Taxes and deferred taxes	456.849.516	463.968.279	-7.118.763
3) Others	35.675.117	40.090.796	-4.415.679
TOTAL B)	494.229.606	504.776.474	-10.546.868
C) EMPLOYEE TERMINATION INDEMNITY	75.741.861	60.424.427	15.317.434

In millions of Euro	Book values as at 31.12.2005	Book values as at 31.12.2004	Changes for the period
D) PAYABLES			
1) Bonds	1.400.000.000	1.400.000.000	0
- <i>due beyond 12 months</i>	<i>1.400.000.000</i>	<i>1.400.000.000</i>	<i>0</i>
2) Convertible bonds	0	0	0
3) Trade payables from loans	0	0	0
4) Bank loans			
- <i>medium and long-term bonds</i>	<i>400.031.065</i>	<i>318.215.715</i>	<i>81.815.350</i>
- <i>due beyond 12 months</i>	<i>370.485.611</i>	<i>300.033.897</i>	<i>70.451.714</i>
- <i>short-term loans</i>	<i>55.000.000</i>	<i>0</i>	<i>55.000.000</i>
5) Other loans	0	0	0
6) Advances	34.877.433	36.171.630	-1.294.197
- <i>due beyond 12 months</i>	<i>24.608.077</i>	<i>15.804.605</i>	<i>8.803.472</i>
7) Trade payables			
- <i>sundry items</i>	<i>185.442.461</i>	<i>176.256.682</i>	<i>9.185.779</i>
- <i>due beyond 12 months</i>	<i>431.090</i>	<i>2.984.028</i>	<i>-2.552.938</i>
- <i>energy-related items</i>	<i>747.201.164</i>	<i>0</i>	<i>747.201.164</i>
8) Payables represented by credit instruments	0	0	0
9) Payables to subsidiaries	5.807.996	0	5.807.996
10) Payables to affiliates	2.622.625	0	2.622.625
11) Payables to Parent Company	0	1.702.059	-1.702.059
12) Tax payables	22.042.794	16.098.080	5.944.714
13) Social security payables	11.472.724	7.917.083	3.555.641
14) Other payables	27.961.741	12.748.513	15.213.228
TOTAL D)	2.892.460.003	1.969.109.762	923.350.241
E) ACCRUED LIABILITIES AND DEFERRED INCOME			
1) Accrued liabilities	23.906.679	19.025.199	4.881.480
2) Deferred income			
- <i>premium on bond issues</i>	<i>0</i>	<i>0</i>	<i>0</i>
- <i>other</i>	<i>203.122.836</i>	<i>161.760.516</i>	<i>41.362.320</i>
TOTAL E)	227.029.515	180.785.715	46.243.800
TOTAL LIABILITIES	3.689.460.985	2.715.096.378	974.364.607
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	5.555.466.987	4.553.057.946	1.002.409.041
COMMITMENTS			
Guarantees granted	260.626.162	313.906.434	-53.280.272
Other commitments	3.219.567.819	2.519.259.113	700.308.706
TOTAL	3.480.193.981	2.833.165.547	647.028.434

INCOME STATEMENT

In millions of Euro	2005	2004	Changes
A) VALUE OF PRODUCTION			
1) Revenues from sales and services:			
- CTR grid usage component	786.782.978	810.779.378	-23.996.400
- MIS metering component	1.643.793	0	1.643.793
- DIS dispatching component	5.286.520	0	5.286.520
- other let-through energy revenue items	740.773.781	0	740.773.781
- other sales and services	71.231.695	62.789.292	8.442.403
3) Change in contract works in progress	-11.970.849	3.306.658	-15.277.507
4) Capitalized costs	26.460.510	22.525.364	3.935.146
5) Other income and revenues :			
- contribution received	10.242.884	15.262.356	-5.019.472
- other	44.925.211	13.454.569	31.470.642
TOTAL A)	1.675.376.523	928.117.617	747.258.906
B) OPERATING COSTS			
6) Raw materials:			
- let-through energy cost items	622.724.116	0	622.724.116
- other costs for raw materials	21.019.151	21.670.140	-650.989
7) Services			
- let-through energy cost items	98.949.857	0	98.949.857
- other service costs	95.002.199	102.935.197	-7.932.998
8) Leases and rentals			
- let-through energy cost items	19.099.806	0	19.099.806
- other leases and rentals	12.767.111	12.370.444	396.667
9) Personnel:			
- social security contributions	126.915.881	115.662.916	11.252.965
- employee termination indemnity	33.427.051	31.392.130	2.034.921
- retirement benefits	9.631.218	8.981.616	649.602
- retirement pay	942.185	967.731	-25.546
- other costs	6.001.858	6.166.142	-164.284
(10) Amortization, depreciation and writedowns			
- intangible assets	5.625.621	0	5.625.621
- tangible assets	151.732.556	143.452.786	8.279.770
- other writedowns of fixed assets	132.323	704.202	-571.879
- writedowns of current receivables	0	0	0
11) Change in inventories	2.864.769	-1.654.173	4.518.942
12) Accruals to provisions for risks and charges	931.277	9.671.630	-8.740.353
13) Other provisions	0	0	0
14) Other operating costs	21.250.901	28.707.688	-7.456.787
TOTAL B)	1.229.017.880	481.028.449	747.989.431
OPERATING INCOME	446.358.643	447.089.168	-730.525

In millions of Euro	2005	2004	Changes
C) FINANCIAL INCOME AND EXPENSE			
15) From equity investments in :			
- subsidiaries	10.316.279	4.882.457	5.433.822
- affiliates	0	0	0
- other companies	0	0	0
16) Other financial income:			
a) from long-term receivables:			
- subsidiaries	0	0	0
- affiliates	0	0	0
- other companies	127.587	169.602	-42.015
b) from long-term financial assets	277	113	164
c) from marketable securities	941.112	0	941.112
d) other income:			
- subsidiaries	28.939.342	25.461.561	3.477.781
- affiliates	0	0	0
- Parent Company	0	4.353.182	-4.353.182
- other companies	4.118.221	21.609	4.096.612
17) Interest and other financial expense:			
- subsidiaries	22.131	0	22.131
- affiliates	0	0	0
- Parent Company	0	25.661.302	-25.661.302
- other companies	58.678.874	21.505.546	37.173.328
17-bis) (earnings) and losses from exchange rates	-4.358.814	-23.254	-4.335.560
TOTAL C)	-9.899.373	-12.255.070	2.355.698
D) ADJUSTMENTS OF FINANCIAL ASSETS			
18) Revaluation:			
a) of equity investments	0	0	0
b) of long-term financial assets	0	0	0
c) of marketable securities	0	0	0
19) Writedowns:			
a) of equity investments	0	4.882.457	-4.882.457
b) of long-term financial assets	0	0	0
c) of marketable securities	0	0	0
TOTAL D)	0	4.882.457	-4.882.457
E) EXTRAORDINARY ITEMS			
20) Income:			
- gains on disposals of assets	0	0	0
- other	7.618.965	673.663.552	-666.044.587
21) Expense:			
- losses on disposals of assets	0	0	0
- prior-year taxes	0	2.148.473	-2.148.473
- other	15.209.412	261.955.209	-246.745.797
TOTAL E)	-7.590.447	409.559.870	-417.150.316
INCOME BEFORE TAXES	428.868.823	839.511.511	-410.642.686
22) Income taxes, current, deferred and prepaid	160.824.389	165.247.576	-4.423.187
- current	165.211.304	104.498.489	60.712.815
- prepaid	2.731.848	7.457.414	-4.725.566
- deferred	-7.118.763	53.291.673	-60.410.436
23) EARNINGS (LOSSES) FOR THE YEAR	268.044.434	674.263.935	-406.219.499



NOTES TO THE FINANCIAL STATEMENTS

FORM AND CONTENT OF THE FINANCIAL STATEMENTS

The form, content and classification of items in the Balance Sheet, Income Statement and the accompanying notes comply with the regulations set forth in the Italian Civil Code and with the new regulations on the matter of corporate Financial Statements as referred to in Legislative Decree no. 6 of January 17, 2003 and subsequent amendments. The statements also contain additional information that, although not required by law, is deemed necessary to provide a true and fair view of the Company's situation.

The statement of cash flow is included in the Report on Operations, prepared pursuant to Article 2428 of the Italian Civil Code, and in which the information prescribed by the aforesaid article can also be found.

No recourse was made to the departures provided under Article 2423, sub-section 4 of the Italian Civil Code. The figures in the notes to the Balance Sheet and Income Statement are expressed in millions of euro in view of their importance.

As required by law, the Company, which holds significant controlling interests, has also prepared Consolidated Financial Statements that are presented with its statutory Financial Statements.

ACCOUNTING POLICIES

The accounting policies used in the preparation of the Financial Statements at December 31, 2005 are the same as those used in the Financial Statements for the previous year. Such policies are in line with provisions of Article 2426 of the Italian Civil Code, amended further by the corporate law reform implemented with Legislative Decree no. 6 of January 17, 2003 and subsequent amendments, if necessary and where applicable, supplemented by the accounting principles issued by the National Council of the Italian Accounting Profession, as modified by the Italian Accounting Authority in relation to the corporate law reform. The most significant policies are illustrated below.

Balance Sheet

Intangible assets

Intangible assets are recorded at purchase or realization cost inclusive of the additional expenses directly attributable and reflect the residual value of expenditures whose economic utility spans over several years. Amortization is calculated on a straight-line basis with reference to the expected useful economic life of the assets.

Concessions

This item refers to the difference between the price paid for the acquisition of the TSO activities from GRTN SpA (the independent system operator) and the book value of the assets and liabilities acquired. Said difference is ascribed to the value of the concession for electricity transmission and dispatching activities in Italy, previously issued by the Ministry of Productive Activities to GRTN and transferred to the company upon acquisition of the TSO activities. As established by Decree of the Ministry of Productive Activities of April 20, 2005, said concession has a twenty-five year validity commencing from November 1, 2005, date of the effective transfer to Terna of the activities, functions, assets and active and passive legal relationships pertaining thereto. The length of the amortization period corresponds to the length of the concession.

Other intangible assets

Other intangible assets chiefly refer to costs incurred for the purchase of software applications in relation to the acquisition of the TSO business activities. Said software is amortized over a period representing the residual useful life (generally within three years, given the high obsolescence rate of these assets).

Tangible assets

Tangible assets are recorded at purchase or production cost, inclusive of any additional expenses and of the monetary revaluations carried out by Enel SpA pursuant to the applicable regulation. The above defined cost is written down to reflect any permanent impairment in value. If the conditions causing the impairment cease to exist, the cost value (net of depreciation) is restored.

Costs incurred in maintaining or restoring the efficiency and proper operation of plant, in so far as these do not modify the magnitude or potential of plant, are charged to the financial year in which the maintenance and repair work is carried out.

Tangible assets are depreciated on a straight-line basis at the following rates, which are determined based on the estimated useful life of the assets.

DEPRECIATION RATES

Buildings	2.50%
Power lines	2.50%
Transforming substations:	
- <i>Electrical machinery</i>	2.38%
- <i>Other electrical equipment</i>	3.13%
- <i>Automation and control systems</i>	6.70%
Central systems for management and control:	
- <i>Electronic equipment and auxiliary plant</i>	5.00%
- <i>Computers</i>	10.00%

Financial assets

Equity investments

Equity investments in subsidiaries and other companies are accounted for under the cost method. The investment is written down in the event of a permanent impairment in value. If the factors causing the impairment cease to exist, the value of the equity investment is restored to the original amount and the revaluation is recognized in the Income Statement as a write-up.

Inventories

Raw material, auxiliary and consumption goods used in the operation of plant and equipment are valued at their purchase price calculated by the weighted average method. Obsolete and slow-moving inventories are written down to their estimated realizable value, with the amount posted to a specific provision.

Contract work in progress is valued at the amounts of the contractually agreed payments, according to the percentage-of-completion method.

Advances received from customers for contractual work not yet completed are recorded as deferred revenues.

Receivables

Receivables are recorded at their estimated net recoverable value and classified under “Financial assets” or “Current assets”, according to their use and to the nature of the debtor.

Accruals and deferrals

Accruals and deferrals are recorded based on the accrual method of accounting. The issue discounts and premiums, as well as other charges on loans, are systematically recorded in the Income Statement throughout the life of each loan.

Conversion of items denominated in foreign currency

Transactions effected in currencies other than the euro are reported at the exchange rate existing at the transaction date. The monetary assets and liabilities denominated in currencies other than the euro are subsequently adjusted to the exchange rate in force at year-end date.

Provision for risks and charges

Provision for retirement benefits

The provision includes compensation payable in lieu of notice to employees who are entitled to the compensation under the terms of the national collective bargaining agreement and union agreements currently in force.

Other provisions for risks and charges

These provisions are recorded against known or probable losses and liabilities whose amount or timing is undetermined at the end of the Balance Sheet date. Amounts accrued reflect the best possible estimate based on available information.

Provision for employee termination indemnities

The provision covers amounts owed to employees pursuant to the Italian law and collective bargaining

agreements in force at the Balance Sheet date, net of advances made and contributions to the sector pension funds to which employees have subscribed.

Accounts payable

Accounts payable are stated at face value.

Memorandum Accounts

Guarantees granted are recorded at an amount equal to the percentage of the contract guaranteed.

Commitments with suppliers are determined on the basis of contracts in force at year end that do not fall within the normal operating cycle, limited to the part of the contract not yet executed.

Income Statement

Expenses and revenues are recognized on an accrual basis.

Revenues

Margin revenues relating to remuneration of the portion of the National Transmission Grid (NTG) and to the activities of dispatching and metering are recognized in accordance with the tariffs set by the Italian Authority for Electricity and Gas, applying these to the quantitative data available at reporting date. Other revenues from let-through energy, without margin for the company, are determined in the same way and concur with the other let-through energy costs entered under production costs. The other sales and services relate to revenues which do not pertain to the activity of energy transmission and dispatching and are recorded at the time the service is provided or when the title of ownership of the goods is transferred.

Dividends

Dividends and interim dividends are recorded in the period in which their distribution has been approved.

Operating grants

Grants received for the execution of specific works requested by third parties, whose value is recorded among tangible assets, are recorded (for facilities already in operation at December 31, 2002) as deferred income when legal title to the grant is recognized and the amount can be reasonably determined. Grants are deferred and recorded in the Income Statement, under other income and revenues, over the

depreciable life of the assets to which they relate.

As from the year 2003, grants for new plant put in service are recognized as a reduction in book value of the assets.

Advance payments received are recognized in a separate caption under liabilities.

Income tax

Current taxes on income are recorded under taxes payable on the basis of estimated taxable income in conformity with tax regulations, net of advances paid.

Deferred tax assets and liabilities are calculated on temporary differences between the values recognized in the Statutory Financial Statements and the corresponding values recognized for tax purposes, on the basis of the applicable tax rate at the time the differences are reversed. Deferred tax assets are carried as receivables to the extent that it is reasonably certain that they can be recovered.

Deferred tax liabilities are provided to the extent such liability is expected to occur.

The principal components of the aforesaid temporary differences include depreciation of the tangible assets, for which the following information is provided.

Up to 2003 accelerated depreciation was charged, pursuant to Article 67, sub-section 3 of Presidential Decree 917/86, directly to a Shareholder's Equity reserve, determined at the time the Shareholders' Meeting appropriated the company's earnings, with the deferred tax being recognized in the Income Statement. The reserve is defined as equity reserve available upon taxation of said accelerated depreciation charges.

For the year 2004, additional depreciation (equal to the difference between ordinary depreciation and the maximum amount that may be detracted for tax purposes) was deducted for all tangible assets. Deferred taxes were calculated on this additional depreciation.

From 2005 additional depreciation has been deducted with exclusive reference to assets not used for electricity operation and transmission activities, with consequent recording of deferred taxes. From 2005, in compliance with Article 102-bis of the Consolidation Act on Income Tax, the depreciation rates of power lines and transforming substations (tangible operating assets used in the operation of the NTG) recorded in the balance sheet, correspond to depreciation rates deductible by less than 20% which will be deducted throughout a useful life which is longer than those prescribed by previous tax regulations. The accruals concept is guaranteed by effecting appropriate adjustments to the deferred taxes.

Environmental costs

Environmental costs refer to the prevention, reduction and monitoring of the environmental impact of production activities. If the costs are recurrent, they are recognized to Income Statement when incurred. Cost relating to increase of the useful life, capacity or safety of tangible assets, are capitalized as part of the costs of the respective assets. Provisions for risks and charges associated with disputes connected with environmental matters are accrued when it is probable or certain that a liability will be incurred and the amount can be reasonably estimated.

Hedging activity

In order to hedge against the risk of fluctuations in interest rates, the Company has entered into derivative contracts to hedge both the risk associated with specific transactions and its overall exposure.

The interest differentials to be received or paid on derivative financial instruments are recognized under financial income or expense in a manner consistent with the charges in respect of the underlying liabilities. Derivatives effected for hedging purposes but for which the original asset or liability to be hedged has been redeemed in advance or is not specifically identifiable, are valued at year end as the lesser between the cost and the market value, and are recorded under financial expense.

ASSETS

A) SHARE CAPITAL NOT PAID-IN

At December 31, 2005 this item had a balance of zero.

B) FIXED ASSETS - Euro 4,455.5 million

1) INTANGIBLE ASSETS - Euro 154.0 million

Intangible assets amount to € 154.0 million (at Dec. 31, 2004 the item had a balance of zero). The increase is mainly due to the acquisition of the TSO business activities from GRTN and chiefly refers to the reporting of the concession for exclusive performance of electricity transmission and dispatching activities.

The other intangible assets chiefly refer to:

- Development and evolution of software applications for managing the energy billing process;
- Development and evolution of software applications aimed at protecting the electricity system;
- Software applications linked to the development of the electricity exchange with particular regard for the operators' register, consumption units and development of foreign procedures.

The table below shows values and changes for each category:

ELECTRICITY PRODUCTION IN ITALY

Euro	Concessions	Other	Work in progress and advances	Total
BALANCE AT DEC. 31, 2004				
Previous year value				
CHANGES IN 2005				
Acquisition of business activities (TSO)	135,398,920	15,978,241	4,149,213	155,526,374
Capital expenditure	0.00	0.00	4,088,368	4,088,368
Amortization	-902,659	-4,722,961		-5,625,620
BALANCE AT DEC. 31, 2005	134,496,261	11,255,280	8,237,581	153,989,122

2) TANGIBLE ASSETS - Euro 4,002.5 million

Tangible assets amount to € 4,002.5 million (€ 3,848.3 million at Dec. 31, 2004). The following table shows the values and the changes for each category of assets:

Euro	Land and buildings	Plant and machinery	Industrial and commercial equipment	Other assets	Work in progress and advances	Total
(A) BALANCE AT DEC. 31, 2004						
1. Historical cost	476,239,722	5,639,788,341	39,396,413	12,343,247	379,975,702	6,547,743,424
2. Revaluations	60,528,382	860,481,958	149,019	27,742	0	921,187,101
3. Book value (1+2)	536,768,104	6,500,270,298	39,545,432	12,370,989	379,975,702	7,468,930,525
4. Accumulated depreciation	-207,662,654	-3,374,804,384	-27,522,933	-10,602,791	0	-3,620,592,762
5. Balance A) at Dec. 31 2004 (3-4)	329,105,450	3,125,465,914	12,022,499	1,768,198	379,975,702	3,848,337,763
(B) CHANGES IN 2005						
6. Capital expenditure	10,926,878	84,053,192	2,903,924	1,480,982	160,059,182	259,424,158
7. Net reclassifications:						
- Book value	9,096,945	160,753,570	-47,086	149,746	-169,953,175	0
- Accumulated depreciation	0	0	8,712	-8,712	0	0
Total	9,096,945	160,753,570	-38,374	141,034	-169,953,175	0
8. Net disposals:						
- Book value	-200,014	-27,674,945	-454,851	-44,393	-161,557	-28,535,760
- Accumulated depreciation	148,128	23,664,179	446,000	44,222	0	24,302,529
Total	-51,886	-4,010,766	-8,851	-171	-161,557	-4,233,231
9. Depreciation:	-12,291,939	-136,263,913	-2,211,588	-965,116	0	-151,732,556
10. Acquisition business activities (TSO)						
- Book value	24,855,169	55,642,741	75,260	16,696,801	3,143,434	100,413,405
- Accumulated depreciation	-3,494,206	-23,341,757	-27,696	-8,682,650	0	-35,546,309
Total	21,360,963	32,300,984	47,564	8,014,151	3,143,434	64,867,096
11. Grants						
- Book value	0	-14,172,721	0	0	0	-14,172,721
- Accumulated depreciation	0	0	0	0	0	0
Total	0	-14,172,721	0	0	0	-14,172,721
13. Balance B)	29,040,961	122,660,346	692,675	8,670,880	-6,912,116	154,152,746
BALANCE AT DEC. 31 2005 (A + B)						
14. Historical cost	521,069,485	5,909,696,560	41,875,459	30,630,016	373,063,586	6,876,335,106
15. Revaluations	60,377,597	849,175,575	147,220	24,109	0	909,724,501
16. Book value	581,447,082	6,758,872,135	42,022,679	30,654,125	373,063,586	7,786,059,607
17. Accumulated depreciation	-223,300,671	-3,510,745,875	-29,307,505	-20,215,047	0	-3,783,569,098
D) BALANCE AT DEC. 31 2005	358,146,411	3,248,126,260	12,715,174	10,439,078	373,063,586	4,002,490,509

The changes occurring in the year, in addition to the ordinary year-on-year variations referring to capital expenditure (€ 259.4 million), disposals (€ 4.2 million) and depreciation (€ 151.7 million), also record the acquisitions of tangible assets occurring further to the acquisition of the TSO business activities from GRTN.

With regard to the caption “Land and buildings” (€ 358.1 million) the increases chiefly refer to the building located in the municipality of Rome in via Palmiano, offices of the National Electricity Control Centre, and those purchased in the municipalities of Naples, Venice and Turin.

The caption “Plant and machinery” (€ 3,248.1 million) includes the electricity transmission grid, transforming stations and centralized systems for the remote monitoring and control of equipment and the national system of energy control

As regards “work in progress and advances”, projects for the development and upgrading of the network with a value of more than € 5 million are indicated below:

Euro

POWER LINES:	
KV 380 Matera - S.Sofia	71,957,534
KV 380 Turbigo - Rho	24,423,239
KV 380 Laino - Feroletto - Rizziconi	10,373,119
KV 150 Sardegna - Corsica	7,284,161
380 KV TRANSFORMING SUBSTATIONS	
Calenzano	14,979,316
Carpi Fossoli	13,310,615
Santa Barbara	12,197,337
Foggia	7,737,451
Fratta	6,868,564
Rumianca	6,280,208
Sorgente	5,652,480
220 KV TRANSFORMING SUBSTATIONS	
Santa Maria Capua Vetere	5,380,735

Changes in tangible assets occurred in the year are summarized below:

The main “capital expenditure” included:

Euro

Capital expenditure	
- Power lines	121,343,002
- Transforming substations	121,676,289
- Other	16,404,867
Total capital expenditure	259,424,158
TSO activities	64,867,097
Depreciation	-151,732,556
Net disposals	-4,233,231
Operating grants relating to new plant in the year	-14,172,721
TOTAL	154,152,746

- 380kV Turbigo - Rho power line (€ 23.8 million)
- 380kV Laino - Feroletto - Rizziconi power line (€ 1.9 million)
- 380kV Matera - S.Sofia power line (€ 7.4 million)
- 150kV Sardegna - Corsica power line (€ 7.3 million)
- 380kV Santa Barbara transforming station (€ 10.9 million)
- 220kV Rumianca transforming station (€ 5.0 million)
- 380kV Sparanise transforming station (€ 4.5 million)

At December 31, 2005, accumulated depreciation accounted for 51.04% of fixed assets subject to depreciation, compared with 51.07% at December 31, 2004.

The increase in tangible assets compared to the previous year (€ 154.2 million) is attributable to the combined effect of the acquisition of the Transmission and Dispatching activities (€ 64.9 million) and the other changes in fixed assets. The latter refer to disposals to the extent of 4.2 million and to new expenditure to the extent of 259.4 million net of operating grants for plant commencing operation in the course of the year (€ 14.2 million).

3) FINANCIAL ASSETS - Euro 299.0 million

Financial assets break down as follows:

Euro	at Dec 31 2005	at Dec. 31 2004	Increases	Decreases	TSO activities
Equity investments:					
- in subsidiaries	288,493,407	300,007,357	33,449,962	44,963,912	0
- in associated companies	4,570,765	0	2,866,457	0	1,704,307
- in other companies	0	2,866,457	-2,866,457	0	0
Total equity investments	293,064,172	302,873,814	33,449,963	44,963,912	1,704,307
Receivables from subsidiaries	0	6,012,074	0	6,012,074	0
Receivables from others:					
- tax advance on employee termination indemnities (Law662/1996)	1,494,887	2,377,637	225,392	1,108,142	0
- loans to employees and other items	4,421,725	3,490,447	2,787,207	2,686,427	830,498
Total receivables from others	5,916,612	5,868,084	3,012,599	3,794,569	830,498
TOTAL	298,980,784	314,753,972	36,462,562	54,770,555	2,534,805

Equity investments

During 2005 the value of equity investments experienced a net decrease (€ 11.5 million) due to the combined effect of the two factors stated below:

- € 44.9 million decrease in the value of the equity investment held in TSN further to exercise of the redemption right, on the part of Terna SpA, on 175 million preferential shares redeemable by the parent company (unit redemption value of R\$ 0.94108);
- Purchase, with effect from Oct. 10, 2005, from the company Acea SpA of a 100% stake in Acea Trasmissione SpA, later renamed RTL SpA (€ 33,4 million).

The shares of both the foreign subsidiaries have been pledged to Banco Nacional de Desenvolvimento Economico e Social (BNDES) as collateral for the loans granted by said bank. Terna however retains the voting and dividend rights.

Equity investments in associated companies

Equity investments in associated companies, which amount to € 4.6 million, refer to the company Cesi SpA and represent a 24.4% interest in the company's share capital.

This company operates in the construction and management of laboratories and plant for experimental tests, trials, studies and research concerning electrotechnics in general and technical and scientific progress in this field. Compared to the previous year the equity investment has increased (€ +1.7 million) owing to acquisition of the TSO business activities which were added to the 15% interest already held by Terna, leading to reclassification of the item from the caption “equity investments in other companies” to the caption “equity investments in associated companies”.

The table below provides a summary of the equity investments in subsidiaries and associated companies:

Name/ Registered Office	SHARE CAPITAL		Shareholders' equity at Dec. 31 2005 (€/000,000)	Net income/ loss at Dec. 31 2005 (€/000,000)	% Ownership	Book value (€/000,000)	Value as per art. 2426 point 4 C.C. (€/000,000)	Difference
	(€/000,000)	(R\$/000,000)						
SUBSIDIARIES								
Transmissora Sudeste Nordeste S.A.		250.0	145.7	16.8	100.0%	113.1	65.6	47.5
- Rio de Janeiro								
Novatrans Energia S.A.		373.1	177.7	18.8	100.0%	141.9	133.4	8.5
- Rio de Janeiro								
RTL SpA	20.6		33.2	-0.8	100.0%	33.4	33.4	0
- Rome								
ASSOCIATED COMPANIES								
CESI SpA	8.6		26.1	0.7	24.4%	4.6	1.8	2.8
- Milan								

Shareholders' Equity of the investee companies TSN and Novatrans refers to the amounts stated in the respective financial statements converted at the year-end rate of exchange and is net of R\$ 48,465,312 and R\$ 27,645,407 respectively, which the respective Boards decided to distribute in 2006 as provided by Brazilian law.

Receivables from subsidiaries

Compared to the previous year this item has a balance of zero following payment (€ -6 million on Mar. 24, 2005) by the subsidiary Novatrans Energia SA of the interest accrued on the Shareholder Loan Agreement taken over by Terna when it acquired its interest in the company.

Receivables from others

Withholding taxes on employee termination indemnities, paid pursuant to the provisions of law and

remunerated at the rate used to adjust employee termination indemnities, declined by € 0.9 million, attributable to the normal employee turnover and to revaluation for the year.

The item also carries the amounts relating to loans extended to employees, remunerated at current market rates, which were disbursed for first-home purchase or for serious family necessity and will be repaid by employees according to pre-established amortization schedules. The increase compared to the previous year (€ 0.8 million) is chiefly attributable to loans pertaining to the employees of the TSO business activities.

C) CURRENT ASSETS - Euro 1,070.6 million

1) INVENTORIES - Euro 17.8 million

Inventories of raw materials include stocks of materials and equipment to be used in the operation, maintenance and construction of plant (€ 7.2 million). The € 2.9 million decrease is chiefly attributable to routine plant maintenance requirements. Stocks include some company property stored at suppliers' premises before being assigned its final destination.

Contract work in progress (€ 10.6 million) refers to long-term work carried out by Terna for various clients. Projects include: work done for Ferrovie dello Stato SpA (the state railway company) involving the upgrading and renovation of transmission plant (€ 2.4 million); work for SEAP Srl regarding the installation of an electric bus system in Chieti (€ 1.5 million); and work for Energia Molise involving the construction of the 380kV Termoli-Larino power line (€ 1.5 million)

Euro	At Dec.31 2005	At Dec.31 2004	Change
Raw materials	7,175,173	10,039,942	-2,864,769
Contract work in progress	10,641,957	22,612,806	-11,970,849
Total	17,817,130	32,652,748	-14,835,618

2) RECEIVABLES - Euro 1,037.0 million

A breakdown of receivables by maturity within and exceeding five years is shown in the table at the end of asset section of the notes.

Trade receivables - Euro 978.7 million

Trade receivables amount to € 978.7 million and feature a considerable increase (+ € 839.6 million) compared to 2004 attributable to the electricity dispatching activity performed by the company in its new capacity as owner and operator of the National Transmission Grid further to acquisition of the transmission and dispatching activities from GRTN SpA with effect from the month of November 2005.

The table below provides a breakdown of receivables according to their nature:

Euro	At Dec.31 2005	At Dec.31 2004	Change
Remuneration NTG	170,167,031	118,555,672	51,611,359
Receivables for energy items	754,068,733	-	754,068,733
Other receivables	54,501,585	20,557,890	33,943,695
Total	978,737,349	139,113,562	839,623,787

Receivables pertaining to the CTR tariff component refer to remuneration to be paid to the Company for usage of the company- owned portion of the NTG by electricity distributors (resolution 5/04 article 17 and subsequent amendments) and producers (resolution 5/4 article 19 and subsequent amendments). Specifically, in compliance with resolution 5/04, the aforesaid receivables mainly consist of usage fees for the last two months of 2005, falling due in January and February 2006. Receivables for energy items mostly report receivables relating to the so-called “let-through revenues” pertaining to the activity of energy dispatching and which for the company do not contribute to margin. Also included are receivables for considerations, due from market operators as remuneration of the activity of dispatching, (DIS tariff component - resolution 237/04) and metering (MIS tariff component - resolution 05/04). Through the dispatching activity Terna guarantees safety of supplies ensuring adequate resources to meet demand and continuous balance in real time between energy needs and available resources, while the metering activity refers to the reading and recording of the measurements of energy introduced by the production units to the NTG.

Other trade receivables also include receivables due from Enel Group companies, and in particular from

Enel Distribuzione (€ 4.6 million) for operating and maintenance activity on HV lines owned by the same and from the company Enel.Net (€ 7.0 million) for the laying of fiber optic lines, and their operating, maintenance and development.

Receivables from subsidiaries - Euro 27.6 million

This item consists of financial receivables from the two Brazilian companies, Transmissora Sudeste Nordeste S.A (TSN) and Novatrans Energia S.A (NVT) and trade receivables from the subsidiary RTL. The former refer to the interest on equity, a particular form of return on internal funds, which was approved by TSN (€ 13.4 million) and NVT (€ 13.8 million) in compliance with some local conditions and authorizations, and shall be paid to the Parent Company during 2006.

The trade receivables (€ 0.4 million) due from the company RTL refer to services arising from the management fees contract and from the contract for operation and routine maintenance of the power lines owned by said company.

Receivables from associated companies - Euro 0.1 million

This item consists of trade receivables from the company Cesi SpA

Receivables from the Parent Company

At December 31, 2005, this item has a zero balance. Last year's figure related to a financial receivable and represented the balance of the intercompany current account held with the former Parent Company Enel SpA and entirely repaid on September 15, 2005.

Other receivables - Euro 30.5 million

The balance of this item consists mainly of deferred tax assets (€ 12.1 million), tax receivables (€ 5.2 million) and credits with the Greek revenue authorities for indirect taxes (VAT - € 9 million) in relation to the activities carried out by the Terna branch in Greece and to the adjustment in the company's favor pertaining to the acquisition of the TSO activities from GRTN (€ 2.0 million).

Tax receivables refer to the advance payment of VAT effected in December (€ 1.9 million), to receivables for tax paid abroad (in Greece € 1.8 million and in Brazil € 0.1 million), which can be deducted in the tax-return in Italy. Specifically, the taxes withheld by the Brazilian subsidiaries refer to the payment of receivable

interest accrued vis-à-vis Novatrans (repayment of the Shareholder Loan).

The adjustment relating to the acquisition of the TSO business activities from GRTN arises from comparison between the initial balance at Dec. 31, 2004, used for determination of the sales price, and the final transfer balance reported at Dec. 31, 2005.

Further minor items chiefly refer to advances disbursed to employees and third parties for various accounts.

The changes in deferred tax assets, determined in accordance with tax rates in force (33% Ires (Corporate Income Tax) - 4.43% average - Irap (Regional Business Tax), are shown below:

The decrease is largely attributable to utilization for the period concerning temporary items.

In millions of Euro	At Dec. 31 2005	At Dec. 31 2004	Change recorded in the Income Statement
Provision for early retirement incentive expense	3,164,700	1,605,450	1,559,250
Provisions for risks and charges	7,231,114	12,994,380	-5,763,266
Other components:			
- <i>contract renewal</i>	391,363	0	39,363
- <i>registration duties acquisition TSO activities</i>	1,044,039	0	1,044,039
- <i>depreciation of buildings not used in operations</i>	274,105	237,339	36,766
	12,105,321	14,837,169	-2,731,848

4) CASH AND CASH EQUIVALENTS - Euro 15.8 million

Cash and cash equivalents at Dec. 31, 2005 amount to € 15,8 million, of which € 15.7 million represent available funds on bank current accounts and € 0.1 million cash held by the company's eight operating facilities in Italy.

D) ACCRUED INCOME AND PREPAID EXPENSES - Euro 29.4 million

Euro	At Dec.31 2005	At Dec.31 2004	Change
Accrued income	13,151,142	10,008,219	3,142,923
Prepaid expenses			
- discount on loans	3,000,331	3,169,817	- 169,486
- other	13,277,762	8,043,301	5,234,461
Total	16,278,093	11,213,118	5,064,975
TOTAL	29,429,235	21,221,337	8,207,898

Accrued income refers exclusively to interest income accrued on derivative contracts (swaps) entered into against bond issues effected in the year and EIB loans established in previous years.

Prepaid expenses pertain to energy items (€ 5.6 million), the issue discount (€ 3.0 million) and expenses (€ 3.6 million) relating to the aforesaid bond issue and distributed over its life and to prepaid insurance premiums (€ 2.3 million).

Specifically, the prepaid expenses pertaining to energy items refer to the charges for subscription to the ETSO - CBT (European Transmission System Operators - Cross Board Trade) agreements concerning the compensation of costs relating to energy transit on foreign electricity grids. With its resolution 15/2005 AEEG (the Italian Regulatory Authority for Electricity and Gas) in fact guaranteed coverage of said charges, establishing that the procedures for refund are to be defined by specific order.

The table below provides a breakdown of receivables and accrued income by maturity:

	Within 1 years	From 2 to 5 years	Over 5 years	Total
LONG-TERM FINANCIAL RECEIVABLES				
Receivables from others	834,862	1,760,771	3,320,978	5,916,612
Total long-term financial receivables	834,862	1,760,771	3,320,978	5,916,612
CURRENT RECEIVABLES				
Trade receivables	978,737,349			978,737,349
Receivables from subsidiaries	27,599,843			27,599,843
Receivables from associated companies	120,000			120,000
Tax receivables	5,158,894			5,158,894
Pre-paid tax receivables	12,105,321			12,105,321
Receivables from others	3,812,526	9,435,046		13,247,572
Total current receivables	1,027,533,933	9,435,046	0	1,036,848,979
Accrued income	13,151,142			13,151,142
TOTAL	1,041,519,937	11,195,817	3,320,978	1,055,916,733

The table below provides a breakdown of receivables by geographical area:

	Receivables f/customers	Receivables f/subsidiaries	Receivables f/associates	Other receivables	Total
Italy	975.4		0.1	21.4	996.9
UE	0.4			9.1	9.5
Extra-UE	2.9				2.9
North America					
Central/South America		27.6			27.6
Total	978.7	27.6	0.1	30.5	1,036.9

LIABILITIES AND SHAREHOLDERS' EQUITY

A) SHAREHOLDERS' EQUITY - Euro 1,866.0 million

The changes in Shareholders' Equity are as follows:

Euro	Share capital	Legal reserves	Other reserves	Retained earnings	Net income	Total
BALANCE AT DEC. 31, 2002	2,036,050,000	73,910,747	256,111,172	215,292	88,119,868	2,454,407,079
Allocation of 2002:						
- To Legal reserve		4,405,993			-4,405,993	
- To Other reserves (accelerated depreciation)			39,614,690		-39,614,690	
- To Retained earnings				120,505	-120,505	
- To Dividends					-43,978,680	-43,978,680
Net income for 2003					123,489,605	123,489,605
BALANCE AT DEC. 31, 2003	2,036,050,000	78,316,740	295,725,862	335,797	123,489,605	2,533,918,004
Allocation of 2003:						
- To Legal reserve		6,174,480			-6,174,480	
- To Other reserves (accelerated depreciation)			36,907,614		-36,907,614	
- To Retained earnings				187,140	-187,140	
- To Dividends					-80,220,371	-80,220,371
Share capital reduction	-1,596,050,000		396,050,000			-1,200,000,000
Interim dividends					-90,000,000	-90,000,000
Net income 2004					674,263,935	674,263,935
BALANCE AT DEC. 31, 2004	440,000,000	84,491,220	728,683,476	522,937	584,263,935	1,837,961,568
Allocation of 2004:						
- To Legal reserve		3,508,780			3,508,780	
- To Retained earnings				440,755,155	440,755,155	
- To Dividends: balance 2004					140,000,000	-140,000,000
Interim dividends 2005					100,000,000	-100,000,000
Net income 2005					268,044,434	268,044,434
BALANCE AT DEC. 31, 2005	440,000,000	88,000,000	728,683,476	441,278,092	168,044,434	1,866,006,002

Share capital - Euro 440.0 million

The share capital of Terna Spa is represented by 2,000,000,000 ordinary shares of nominal value € 0.22 each, held as follows:

- By Cassa Depositi e Prestiti (CdP - government controlled public financing agency), for a stake equal to 29.99% of share capital (599,999,999 shares) further to transfer of shares owned by Enel SpA effected on September 15, 2005, in implementation of authorizing order no. 14542 of August 4, 2005 issued by the Italian Anti-Trust Authority;
- By Enel SpA to the extent of approximately 6.142%; said stake, as a result of maturity, in December, of the right to allocation of free shares (so-called bonus shares) to subscribers to the IPO of Terna shares in June 2004, has at today's date been further reduced to approximately 5%;
- The remaining shares equal to approximately 64.90% have been parceled out on the market further to the Public Sale Offer addressed to public and institutional investors (June 2004) and to the subsequent accelerated book building transaction targeted at Italian and foreign institutional investors (March 2005).

Allocation of Net Income for 2004

On April 2, 2005, the Ordinary Shareholders' Meeting unanimously approved the Financial Statements and Report on Operations for 2004 and allocated net income as follows:

- € 3,508,779.75 to Legal Reserve up to 20% of share capital;
- € 90,000,000.00 to cover the interim dividend up for payment on October 21, 2004;
- € 140,000,000.00 as settlement of dividends in the amount of € 0.07 per share (2,000,000,000 ordinary shares), paid out on May 26, 2005;
- € 440,755,155.16 as retained earnings.

Legal Reserve

This item is equal to € 88.0 million and represents 20% of Share Capital. Accordingly, upon allocation of the net income for 2004 the Reserve reached full appropriation.

Other Reserves

Other reserves, which retain the same balance as at Dec. 31, 2004, amount to € 728.7 million and include accruals made in previous years, net of relative contributions, exclusively for tax purposes (€ 332.6 million) and the portion of share capital reduction (€ 396.1 million) following resolution of the Shareholders' Meeting of January 28, 2004, to reduce the share capital from € 2,036.1 to € 440 million by way of refund to the shareholder Enel SpA of € 1,200 million.

Retained Earnings

Retained earnings record a € 440.7 million increase compared to the balance at Dec. 31, 2004 (€ 0.5 million) further to the allocation of net income referred to above.

Interim dividend 2005

On September 9, 2005, The Board of Directors, having consulted the independent auditors KPMG pursuant to Article 2433-bis of the Italian Civil Code, passed a resolution to distribute an interim dividend for 2005, as the requirements for said distribution were present.

The table below provides a breakdown of the single items of the Shareholders' Equity at year end, with specification of their origin, possible utilization, and extent to which they may be distributed.

The non-distributable portion refers to the accelerated depreciation reserve made up of income from previous years for which taxation has not been paid off (€ 332.6) and to most of the retained earnings (€ 431.9), referring to allocation of net income 2004.

Euro	Amount	Possible utilization	Available amount
Share capital	440,000,000		
Legal Reserve	88,000,000	B	
Other Reserves:			
- of Capital	396,066,445	A,B,C	396,066,445
- of Income	332,617,031	A,B	332,617,031
Retained earnings	441,278,092	A,B,C	441,278,092
Interim dividends	-100,000,000		
Net income 2005	268,044,434		
Total			1,169,961,568
Non-distributable portion			764,527,970
Remaining distributable portion			405,433,598

A: for capital increase
 B: for covering losses
 C: for distribution to shareholders

In previous years utilizations of the reserves for hedging losses or for other purposes have not been recorded.

B) PROVISION FOR RISKS AND CHARGES - Euro 494.2 million

Euro	At December 31, 2005	At December 31, 2004	Accruals	From RTL	TSO business activities	Utilization
Provision for retirement benefits	1,704,973	717,399	942,184		575,170	529,780
Deferred tax liabilities	456,849,516	463,968,279	8,306,340			15,425,103
Others:						
- litigation	13,767,705	13,446,398	931,277	20,972		630,942
- sundry risks and charges	12,317,412	21,779,398	9,972,507	109,011		19,543,504
- early retirement incentives	9,590,000	4,865,000	7,163,000			2,438,000
Total	35,675,117	40,090,796	18,066,784	129,983		22,612,446
TOTAL	494,229,606	504,776,474	27,315,308	129,983	575,170	38,567,329

Provision for retirement benefits - Euro 1.7 million

The provision includes accruals for indemnities in lieu of notice and additional monthly payments accruing to personnel.

Deferred tax liabilities - Euro 456.8 million

The following table shows changes in deferred tax liabilities, by type of temporary difference, determined in accordance with prevailing tax rates (33% Ires; 4.43% average Irap):

Euro	At Dec. 31,2005	At Dec. 31,2004	AMOUNTS RECORDED IN INCOME STATEMENT		
			Ordinary changes	Change in rate	Total
Additional depreciation	455,001,903	463,737,336	-9,449,422	713,989	-8,735,433
Other components	1,847,613	230,943	1,616,670		1,616,670
Total	456,849,516	463,968,279	-7,832,752	713,989	-7,118,763

Compared with 2004 the provision records a decrease of € 7.1 million due to the combined effect of the following events:

- allocations made against additional depreciation compared to the depreciation rates appropriated in the year (€ 6.1 million) and write-downs on receivables (€ 1.6 million);
- adjustment to the initial provision (+0.7 million) in accordance with the average IRAP tax rate in force (4.43%);

- utilization (€ 15.4 million) attributable to reabsorption of depreciation exceeding the deductible quota. This has increased considerably due to recent tax legislation on depreciation (Article 102-bis of the Consolidation Act on Income Tax) for assets included in the homogeneous categories of the electricity sector as determined by AEEG.

Provision for litigation - Euro 13.8 million

The provision, broadly unchanged from the previous year, is intended to cover potential liabilities in respect of litigation or other disputes relating to company activity, assessed on the advice of external and internal counsel. It does not include provisions for litigation for which a positive outcome is expected, nor provisions for which a potential charge cannot reasonably be quantified. The latter are described under "Off-balance-sheet items".

Provision for sundry risks and charges - Euro 12.3 million

Compared to the previous year, the provision has undergone a € 9.5 million decrease attributable to algebraic effect of accruals (€ 10.0 million) and utilization (€ 19.5 million) for the period, as follows:

- Release (€ 15.0 million) of the accruals made in previous year for network fees for the years 2002/03/04 referring to the prevailing dispute with the auto-producers of Cip 6 energy; this litigation was settled during the year further to the events specified below:
 - in 2005 the Council of State delivered various judgments by which it ruled that the GRTN's credit claim against owners of the so-called Cip 6 production plants relating to the service of electricity transportation was inexistent;
 - iAEEG then specified the procedures for covering said costs, thus causing Terna's claims against GRTN to become certain and collectible.
- Release (€ 1.5 million) of the accruals for contractual penalties to be paid in 2004 to Enel Distribuzione referring to the contract for maintenance of the HV lines owned by the latter, no longer necessary insofar as the counterparty has waived said item within the scope of renewal of said maintenance contract;
- Accrual referring to the long-term incentive plan (LTI) in favor of senior managers not included in the stock option plan (€ 3.7 million);
- Utilization for premiums linked to the options exercised by senior management on Enel shares (€ 2.6 million);

- Accrual (€ 6,0 million) referring to the “Projects for urban and environmental redevelopment” aimed at compensating the environmental impact of the construction of power lines.

Provision for early retirement incentives - Euro 9.6 million

The provision for early retirement incentives represents the estimated value of the extraordinary expenses related to the early consensual termination of employment of staff members who are entitled to a pension.

C) EMPLOYEE TERMINATION INDEMNITIES - Euro 75.7 million

The changes in the balance in 2005 are shown below:

Euro

Balance at Dec. 31, 2005	60,424,427
Accruals	9,631,218
Pension fund contributions	-2,330,712
Indemnities paid and other transactions	-8,356,153
Acquisition TSO activities	15,868,251
Acquisition/sale of contracts	504,830
Total	75,741,861

The provision represents the accrued entitlement of employees for termination indemnities, net of advances and contributions to the pension funds. The amount is carried net of the 11% flat withholding tax on the revaluation of employee termination indemnities, pursuant to Legislative Decree 47/2000.

The sharp increase (€ 15.3 million) compared to the previous year is essentially due to the resources acquired with the TSO activities.

D) PAYABLES - Euro 2,892.5 million

A breakdown of payables by maturity within and exceeding five years is included in a separate schedule at the end of the liabilities section of the Notes. The table below instead provides a breakdown of the global position of financial indebtedness by maturity of the single loans:

Long-term payables - Euro 1,800.0 million

In millions of Euro	Repayment period	Dec. 31, 2005	Current portion	Non-current portion	2007	2008	2009	2010	Beyond
B.I. 2014	2014	600.0	0.0	600.0	0.0	0.0	0.0	0.0	600.0
B.I. 2024	2024	800.0	0.0	800.0	0.0	0.0	0.0	0.0	800.0
EIB n. 20271	2014	61.4	6.8	54.5	6.8	6.8	6.8	6.8	27.3
EIB n. 21159	2016	238.6	22.7	215.9	22.7	22.7	22.7	22.7	125.0
EIB n. 22947	2020	100.0	0.0	100.0	0.0	0.0	4.6	9.1	86.4
Total		1,800.0	29.5	1,770.5	29.5	29.5	34.1	38.6	1,638.6

Bond issues - Euro 1,400.0 million

During 2004 the Company released two bond issues, the terms of which are provided below:

Ten-year bond 2004-2014:

- Nominal amount € 600 million;
- Issue price 99.968;
- Issue discount € 192 thousand;
- Life from October 28, 2004 to October 28, 2014;
- Fixed rate of 4.25% p.a. with 365/365 divisor;
- Payment annual coupon;
- Lump-sum repayment at maturity;

Twenty-year bond 2004-2024:

- Nominal amount € 800 million;
- Issue price 99.624;
- Issue discount € 3,008 thousand;
- Life from October 28, 2004 to October 28, 2024;
- Fixed rate of 4.90% p.a. with 365/365 divisor;
- Payment annual coupon;
- Lump-sum repayment at maturity;

With regard to the bond issues, considering the hedging by derivative instruments, 81.3% of the twenty-year Bond and 53.3% of the ten-year Bond is quantified at fixed rate.

Medium/long term bank loans - Euro 400 million

The total value of this item is € 400 million and refers to three EIB loans denominated in euro and includes a debt with San Paolo/IMI for a prime rate loan (granted by the Val d'Aosta Independent Region) equal to € 31 thousand.

The first EIB loan was granted on October 22, 1999 for the "Italy-Greece electricity network interconnection" project, with an initial value of € 75 million, and has the following terms:

- Floating interest rate with a ceiling equal to 3m Euribor + 0.15% (2.44% at the end of 2005);
- Interest payments made on a half-yearly basis (March 15 and September 15);
- Repayment of principal: in 22 equal installments paid half-yearly from March 15, 2004 to September 15, 2014.

On March 15, 2005 and September 15, 2005 repayment of the third and fourth installments was effected for a total of € 6.8 million. At Dec. 31, 2005 the residual loan is equal to € 61.4 million and it is completely hedged against fluctuations in interest rate by derivative instruments.

The second EIB loan, of € 250 million, was granted on July 6, 2001 for the design, building and bringing into service of around 200 electricity transmission facilities, and has the following terms:

- Floating interest rate with a ceiling equal to 3m Euribor + 0.24% (2.53% at the end of 2005);
- Interest payments made on a half-yearly basis (June 15 and December 15);
- Repayment of principal: in 22 equal installments paid half-yearly from December 15, 2005 to June 15, 2016.

On December 15 the first installment was repaid for a total of € 11.4 million. The residual loan, equal to 238.6 million, is hedged by interest rate swaps with a nominal value of € 207.6 million, leaving 13% of the total loan exposed to interest-rate risk.

The third EIB loan, of € 100 million, was granted on March 15, 2005 and is part of a € 300 million loan contract signed with EIB, intended to cover part of the expenditure for the expansion scheduled in the company's industrial plan. The remaining € 200 million may be disbursed by the end of 2007 and, as in the case of the other EIB loans, will have a 4-year grace period and an 11-year repayment period. The loan has the following terms:

- Floating interest rate with a ceiling equal to 3m Euribor + 0.27% (2.56% at the end of 2005);
- Interest payments made on a half-yearly basis (March 15 and September 15);
- Repayment of principal: in 22 equal installments paid half-yearly from September 15, 2009 to December 15, 2019.

The loan has not been hedged and is therefore exposed to interest-rate risk.

Short-term bank loans: Euro 55 million.

In order to meet cash requirements, in December two drawdowns were made on the short-term credit lines for a total of € 55 million at an average interest rate of 2.46%: € 25 million was drawn on Banca Popolare di Sondrio with maturity Jan. 16, 2006 and € 30 million on Banca Nazionale del Lavoro with maturity Jan. 20, 2006.

At year end, taking into account the transactions performed in derivative instruments, 66.8% of the entire gross indebtedness and 67.4% of total net payables of Terna SpA is thus quantified at fixed rate.

Breakdown and terms of the Euro 500 million "Facility"

In 2004 the company took up a fifteen-year revolving credit line for € 500 million, organized and managed by Mediobanca, in the capacity of Agent and Bookrunner. In addition to Mediobanca the following banks intervened in the capacity of Mandated Lead Arranger: Banca Intesa, BBVA, BNL, Capitalia, MPS, San Paolo/IMI and UBM. The credit line was subscribed for the purpose of guaranteeing financial hedging of short-term requirements and those ensuing from any extraordinary transactions scheduled in the next 12-18 months. At year end the credit line had yet to be used.

Any utilization shall be remunerated with a margin above Euribor equal to 17.5 base points. This spread may vary according to the company's rating (currently AA- for Standard&Poor's and Aa3 for Moody's).

The non-utilization commission is equal to an annual 30% of the margin. The commission for use is equal to 2.5 basis points if the overall amount of utilization is between 1/3 and 2/3 of the total credit line and 5 basis points for utilization equal to or exceeding 2/3 of the total credit line.

Hedging activity

The table below provides the notional value and the fair value of the hedging instruments present in the portfolio at year end.

In millions of Euro	NOZIONAL VALUE		FAIR VALUE	
	2005	2004	2005	2004
Fixed-rate hedging derivatives on B.I.	1280.0	1200.0	106.1	39.0
Floating-rate hedging derivatives on loans	269.0	285.7	-17.8	-18.9
Other hedging derivatives	850.0	650.0	-11.2	-12.6
Total	2,399.0	2,135.7	77.1	7.5

Advances - Euro 34.9 million

Advances include contributions received for work underway at December 31, 2005 for connections to the network as well as for works for third parties.

A breakdown of advances is provided below:

- Contributions on expected costs of connections to high-voltage network (€ 24.8 million);
- Renewal and upgrading of various plants for RFI (€ 2.4 million);
- Construction of the new Termoli - Larino 380 KV electric power line (€ 1.7 million);
- Construction and upgrade of various plants (€ 5.6 million).

Compared to 2004 (€ 36.2 million) the item records a slight decrease of approximately € 1.3 million, which is chiefly due to the algebraic effect of the € 8.1 million increase arising from new contributions and the € 9.4 million decrease due to completed contracts.

Trade payables - Euro 932.6 million

-Non-energy items - Euro 185.4 million

Trade payables regard invoices received and to be received for contracts, services and purchases of material and equipment. The increase is the result of purchases and services performed during the last period of the year for routine investment and operating activities. The item also reflects payables for services received from Enel Group companies (€ 29.8 million). Lastly it records the payable (€ 0.6 million) relating to adjustment to be paid to ACEA SpA for acquisition of the block of shares in the company RTL.

-Energy items - Euro 747.2 million

This item carries the financial effects relating to the so-called let-through costs, chiefly referred to procurement of energy and to transport fees due to the owners of portions of the NTG.

Payables to subsidiaries - Euro 5.8 million

This item essentially represents the financial debt exposure (€ 4.8 million) relating to the current account held by the Parent Company with the subsidiary RTL. This relationship is governed by the treasury contract drawn up on October 10, 2005 with the subsidiary RTL. The interest rate applied is equal to the arithmetic average of 1 month Euribor, plus/minus a spread of 0.25% calculated on an annual basis (360 days). Interest is paid at the end of each quarter.

Trade payables are also recorded for € 0.9 million for invoices to be received entirely concerning the assessment of network fees for usage of the RTL-owned portion of the NTG applicable only to the last two months of 2005.

Payables to associated companies - Euro 2.6 million

This item records payables to the Company Cesi for services received in relation to the construction and management of laboratories and plants for experimental tests, trials, studies and research concerning electrotechnics in general and technical and scientific progress.

Tax payables - Euro 22.0 million

The tax payables item for 2005 shows the Company's tax liability (€ 136.6 million for Corporate Income Tax (IRES) and 28.6 million in local tax (IRAP)), net of the advances totaling € 150.8 million paid in June and

November 2005. It also includes a payable of around € 4.8 million for withholding tax and payables for registration fees of € 2.8 million pertaining to the contract for acquisition of the TSO activities from GRTN.

Payables to social security institutions - Euro 11.5 million

The item refers to payables to INPS (the national social security institute) for the month of December 2005. It also includes contributions paid on staff incentives to be distributed in the following financial year and the portion of estimated contributions pertaining to renewal of the collective bargaining agreement which expired on June 30, 2005.

The € 3.6 million increase compared to the previous year (€ 7.9 million at Dec. 31, 2004) is influenced by the additional staff acquired by Terna with acquisition of the TSO activities and the company RTL SpA

Sundry payables - Euro 28.0 million

The table below provides a breakdown of sundry payables:

Euro	At Dec. 31, 2005	At Dec. 31, 2004	Change
Payables to employees	21,381,742	12,173,262	9,208,480
Payables to third parties for amounts withheld from employees' pay	381,810	316,045	65,765
Other payables	6,198,190	259,206	5,938,984
Total	27,961,742	12,748,513	15,213,229

Sundry payables equal to € 28.0 million (€ 12.7 million at December 31, 2004) chiefly reflect the payables to employees for staff termination indemnities, to be paid out to by December 31, 2005 in addition to the staff incentives that will be distributed in 2006. The sharp increase recorded, equal to €15.2 million, is largely attributable to debit items entrusted to Terna further to transfer of the TSO business activities, chiefly referring to sundry payables to staff and to the recording of guarantee deposits securing contractual obligations of the electricity market operators for dispatching contracts.

E) ACCRUED LIABILITIES AND DEFERRED INCOME - Euro 227.0 million

Accrued liabilities and deferred income consist of the following:

Euro	At Dec. 31, 2005	At Dec. 31, 2004	Change
Interest payable on loans	23,194,610	18,389,060	4,805,550
Other accrued liabilities	712,069	636,139	75,930
Deferred income on loans	2,830,938		2,830,938
Capital contributions	161,934,584	161,187,666	746,918
Deferred income on energy items	23,545,141		23,545,141
Deferred income on safety plan	14,256,449		14,256,449
Other deferred income	555,724	572,850	- 17,126
Total	227,029,515	180,785,715	46,243,800

This item shows an increase on the previous year (€ 46.2 million), partly attributable to interest payable on loans (€ 4.9 million), which reflects the charges related to the bond issues as well as to the transactions in hedging derivatives.

The further € 41.4 million increase concerns items arising with the acquisition of the TSO business activities:

- € 14.3 million, as deferral of revenues destined to cover future costs within the Safety Plan. Mention is made of AEEG resolution 05/04 which established that costs pertaining to the NTG safety plan are to be remunerated by a portion of the CTR tariff component. Hence the deferral in question refers to the aforesaid portion of the CTR tariff component that will contribute to remuneration of future costs to be incurred in optimizing NTG safety;
- € 14.2 million as "Consideration for usage rights of the transmission capacity";
- € 2.4 million as "Guarantee of the foreign interconnection capacity";
- € 6.4 million as "CD component" as remuneration of the production capacity net of the sums already paid to producers.

The last three deferrals shall be recorded in the balance sheet and income statement when AEEG defines the allocation and/or relative beneficiaries. A final component of the increase posted is the collection of the last portion of the contribution for the Italy-Greece interconnecting power line (€ 9.7 million), which occurred in the 1st half-year.

The following table provides a breakdown of payables and accrued liabilities by maturity.

Euro	Within 1 year	From 2 to 5 years	Over 5 years	Total
FINANCIAL PAYABLES TO THIRD PARTIES				
Payables to third parties for bonds	0	0	1,400,000,000	1,400,000,000
Payables to banks				
- for medium/long term loans	29,545,454	131,818,181	238,667,430	400,031,065
- for short term loans	55,000,000	0	0	55,000,000
Total financial payables	84,545,454	131,818,181	1,638,667,430	1,855,031,065
OTHER PAYABLES				
Advances	10,269,356	24,608,077	0	34,877,433
Trade payables				
- non-energy items	185,011,370	431,091	0	185,442,461
- energy items	747,201,164	0	0	747,201,164
Total other trade payables	932,212,534	431,091	0	932,643,625
Payables to subsidiaries	5,807,996	0	0	5,807,996
Payables to associated companies	2,622,625	0	0	2,622,625
Tax payables	22,042,794	0	0	22,042,794
Social security payables	11,472,724	0	0	11,472,724
Other payables	24,976,287	2,985,454	0	27,961,741
Total other payables	1,009,404,316	28,024,622	0	1,037,428,938
Accrued liabilities	23,906,679	0	0	23,906,679
TOTAL	1,117,856,450	159,842,803	1,638,667,430	2,916,366,683

The table below provides a breakdown of payables by geographical area.

	Bonds	Bank loans	Third party advances	Non-energy items	Energy items	Payables to subsidiaries	Payables to ass.d co.s	Other payables	Total
Italy	444.0	55.0	34.9	178.8	743.9	5.7	2.6	64.2	1,529.2
EU	798.0	400.0		6.5	0.4				1,204.9
Non-UE	70.0			0.1	2.9				73.0
North America	46.0								46.0
Central/South America									
America	0.0					0.1			0.1
Asia	6.0								6.0
Others	36.0								36.0
Total	1,400.0	455.0	34.9	185.4	747.2	5.8	2.6	64.2	2,895.1

COMMITMENTS

Commitments include amounts relating to guarantees, risks and other commitments, as detailed below:

Euro	At Dec. 31, 2005	At Dec. 31, 2004	Change
GUARANTEES GRANTED:			
Guarantees given to third parties	5,582,716	13,899,077	- 8,316,361
Equity participations pledged to third parties	255,043,446	300,007,357	- 44,963,911
Total	260,626,162	313,906,434	- 53,280,272
OTHER COMMITMENTS:			
Hedging derivatives	2,398,977,274	2,135,681,818	263,295,456
Commitments with suppliers for purchase of:			
- Sundry supplies	663,630,287	219,080,840	444,549,447
- Contract work	820,590,545	164,496,455	- 7,536,197
Total	820,590,545	383,577,295	437,013,250
TOTAL	3,480,193,981	2,833,165,547	647,028,434

The guarantees given refer to shares of the subsidiaries TSN and Novatrans, owned by Terna, pledged to the banks (BNDES - IDB) providing loans for the investments in Brazil and to the guarantees granted to third parties in respect of contracts for works and services rendered by the company.

The notional value of the financial interest-rate derivatives is recorded in commitments and risks and emerges as positive by € 77 million at December 31, 2005. Specifically, hedging on the EIB loans feature a negative value of €17.8 million, while hedging on the bond issues record a current positive value of € 94.9 million.

The commitments to suppliers refer to the total of commissioned orders/contract work, net of supplies and services already invoiced.

OFF-BALANCE SHEET ITEMS

Environmental litigation

Environmental litigation relates to the installation and operation of electrical plant, and, especially, the effects of electrical and magnetic fields.

Terna is a defendant in a number of civil and administrative proceedings requesting the relocation of power lines or changes in operational conditions. The claims are based on the alleged health hazards posed by the power lines, even though they have been installed in full compliance with regulatory requirements. Only a

very limited number of suits have been filed against the company seeking damages for personal injury caused by electromagnetic fields.

On July 8, 2003, a Prime Ministerial Decree was enacted to complete the implementation of General Law 36 of February 22, 2001. It establishes values for three parameters (exposure limits, thresholds of concern and quality targets) that electrical plant must meet. The decree had a favorable impact on pending disputes, because the scope of the framework law was limited to laying down general principles only.

Only a few adverse rulings have been issued against the company in this area, and these have all been appealed (the cases are still pending). No claim for damages for personal injury has ever been upheld.

Legislation concerning electrical and magnetic fields

The relevant general law, enacted on February 22, 2001, entrusts the state with the task of defining, through specific orders, the reference parameters (exposure limits, thresholds of concern and quality targets) with which electrical plant must comply.

Attention is drawn in this regard to the general law on reclamation which establishes a mechanism for recovery of related expenses according to criteria defined by the Authority for Electricity and Gas, pursuant to Law no. 481/95, given that costs are incurred for common benefit.

On August 29, 2003 the Prime Ministerial Decree of July 8, 2003 for the “Definition of exposure limits, thresholds of concern and quality targets for the protection of the population from exposure to electrical and magnetic fields at network frequency (50 Hz) generated by power lines”, which established the values for the three parameters provided by the general law, was published in the Official Gazette of the Italian Republic.

On regional legislation level, some regional governments have formulated bills governing the matter, which establish more restrictive limits compared to those prescribed by Prime Ministerial Decree 1992, and by the more recent Prime Ministerial Decree of July 8, 2003.

However it must be noted that judgment no. 307 of the Constitutional Court of October 7, 2003 declared some regional laws on the matter of electromagnetic fields to be constitutionally unlawful (amongst which the law of the Campania regional government no. 13 of November 24, 2001). It also established the principle that derogation from the state law is not permitted, even where this may involve higher standards being implemented by regional laws, as public health must be uniformly guaranteed throughout Italian territory.

Litigation relating to the GRTN business activities

It must be specified that, as far as litigation referring to events occurring up to the date of transfer and pertaining to the GRTN business activities of transmission and dispatching of energy ("Business Activities") according to the provisions of Article 1 of Prime Ministerial Decree of May 11, 2004, and to the transfer contract stipulated between Terna and GRTN on February 28, 2005, said litigation has not been transferred and hence every ensuing or related responsibility, charge or liability remains the concern of GRTN.

Terna, in its capacity as holder of the concession for transmission and dispatching activities from November 1, 2005, has been summoned in some trials appealing against orders of the AEEG and/or of the Ministry of Productive Activities and concerning the matters mentioned above. The Company has entered proceedings only in the cases in which the plaintiffs not only claim flaws in the opposed orders, but also Terna's alleged breach of the regulations issued by the aforesaid Authorities.

Other pending litigation

A number of legal disputes are pending in relation to urban planning and environmental issues associated with the construction and operation of a number of transmission lines. Adverse rulings could have repercussions, but since the impact cannot be quantified at present they have not been included under the provisions for litigations.

For a limited number of cases it is not possible to completely preclude unfavorable rulings of which the consequences could include not only the payment of damages but also the costs involved in modifying power lines and the temporary unavailability of the lines. In any case, an adverse outcome would not jeopardize the operation of the power lines.

An assessment of the aforesaid suits, which included taking advice from external legal counsel, suggests that unfavorable rulings are however remote.

By way of Memorandum no. 63 of May 6, 2005, INPS ordered, with retroactive effect from 1999 onwards, that privatized state-owned industrial enterprises performing industrial activities be obliged to pay CIG, CIGS, DS and mobility contributions, which give rise to a burden in the region of € 24.8 million. Given the complexity of the matter, Terna and the other companies operating in the electricity sector first applied to the administrative court, requesting the annulment of the act, subject to prior suspension. The administrative court denied having jurisdiction, observing that the matter exclusively concerned rights rather than law. Hence Terna has now applied to the ordinary courts for declaratory judgment on the

obligation to pay the contributions. The hearing has been set for October 3, 2006. Meanwhile INPS itself has deemed it necessary to request the opinion of the Council of State, suspending the payment of the contributions until said opinion has been delivered.

Stock options plans

On May 9, 2005, the Board of Directors of the Parent Company passed a resolution to implement the first corporate stock option plan for senior managers of Terna Spa and/or of its subsidiaries, pursuant to Article 2359 of the Italian Civil Code, who fulfill the most important functions in terms of achievement of the company's strategic results.

On December 21, 2005, the Board of Directors, on the basis of proposals submitted by the Remuneration Committee also passed a resolution to implement a 2006 stock option plan for senior managers of the Terna Group, who fulfill the most important functions in terms of achievement of the company's strategic results. In keeping with the international practices adopted by the major Italian listed companies, these plans aim to provide the Terna Group with a means of ensuring management incentive and loyalty. The stock options will allow the Group to encourage a sense of company loyalty in key resources while at the same time ensuring they constantly strive to create value, thus determining convergence between shareholders' interests and those of management.

Information on the terms and conditions of the stock options plans 2005 and 2006 can be found in the report on operations at December 31, 2005. The table below provides the residual useful life of the stock options at December 31, 2005 and the relative fair value:

	Options assigned (at December 31, 2005)	Maturity of options	Fair value determined at assignment date (euro)	Strike price
2005 PLAN				
	1,169,700	2006	0.183	2.098
	1,169,700	2007	0.183	
	1,559,600	2008	0.181	
	3,899,000			
2006 PLAN				
	2,997,600	2007	0.126	2.072
	2,997,600	2008	0.121	
	3,996,800	2009	0.115	
	9,992,000			

At December 31, 2005 the options assigned by these remuneration plans are all outstanding and none are exercisable at said date.

	2005 Plan	2006 Plan
Held at Jan. 1		
Assigned during the year	3,899,000	9,992,000
Not opted during the year	3,899,000	9,992,000
Exercised during the year		
Matured during the year		
Held at year end	3,899,000	9,992,000
Exercisable at year end		

Lastly it is specified that the year-end price of the stock was equal to € 2.084 and the relative volatility equal to 14.000%.

INCOME STATEMENT

A) VALUE OF PRODUCTION

The item comprises the following:

1) REVENUES FROM SALES AND SERVICES - Euro 1,605.7 million

They include the following:

Euro	At Dec. 31, 2005	At Dec. 31, 2004	Change
MARGIN REVENUE ITEMS:			
CTR grid usage component	786,782,978	810,779,378	-23,996,400
MIS metering component	1,643,793	0	1,643,793
DIS dispatching component	5,286,520	0	5,286,520
Total margin revenue items	793,713,291	810,779,378	- 17,066,087
LET-THROUGH ENERGY REVENUE ITEMS:			
Within Exchange perimeter	605,687,175	0	605,687,175
Outside Exchange perimeter	135,086,606	0	135,086,606
Total l/t energy revenue items	740,773,781	0	740,773,781
Other sales and services	71,231,695	62,789,292	8,442,403
TOTAL	1,605,718,767	873,568,670	732,150,097

Revenue from sales and services amount to € 1,605.7 and record a sharp increase (+732.2 million) compared to 2004 attributable to the “energy” sales produced by the company in its new capacity as owner and operator of the National Transmission Grid following acquisition of the TSO activities from GRTN SpA with effect from November 2005.

In particular:

- The revenues for the so-called margin items chiefly refer to remuneration (CTR tariff component) due to the Company for usage of the national transmission grid and also include, referring to the two months of integration, the further share of the CTR tariff components (AEEG resolution no. 15/2005) recognized to Terna with the acquisition of the TSO activities. However said revenues record a downturn (-4.0 million) attributable to the adjustment of the percentage ownership of the National Transmission Grid (€ -2,7 million) and to the effect of the variations introduced on the time-bands (AEEG resolution no. 5/2004) from the month of April 2004 which strongly privileged revenues pertaining to the first quarter of the previous year. The other “margin” components record total revenues for € 6.9 million and refer respectively to the consideration due from the operators for the metering activity (MIS component) and to the consideration recognized for operation of the dispatching service (DIS component).

- The revenues referring to the so-called let-through items present a balance which elides with the “let-through” energy costs (commented in the next paragraph of these notes), hence they do not record a margin to the benefit of Terna and refer exclusively, as do the relative costs, to the exercise of the activity of dispatching of energy. A breakdown is provided below:

Euro	At Dec.31, 2005	At Dec.31, 2004	Change
REVENUES WITHIN EXCHANGE PERIMETER:			
Energy sale on DAEM, RTE, MDS and other minor markets	106,198,096	0	106,198,096
Imbalancing and other minor revenues	266,200,188	0	266,200,188
MDS resources procurement	221,604,781	0	221,604,781
Other items (Income, CBT)	11,684,110	0	11,684,110
Total revenues within Exchange perimeter	605,687,175	0	605,687,175
REVENUES OUTSIDE EXCHANGE PERIMETER:			
CTR revenues other owners and GRTN cip/6 quota	16,921,879	0	16,921,879
Revenues other components of no.168/04-237/04	93,241,699	0	93,241,699
Other items	24,923,028	0	24,923,028
Total revenues outside Exchange perimeter	135,086,606	0	135,086,606
TOTAL	740,773,781	0	740,773,781

The item other sales and services amounts to € 71.2 million and refers to revenues arising from diversified specialist activities in the field of high and very high voltage that the Company provides to third parties customers. Specifically, the aforesaid amount features:

- Revenues accrued for contract work in progress which was completed and tested during the year for € 21.9 million;
- Maintenance on third-party owned HV plant for € 5.6 million;
- Various kinds of specialist HV services for approximately € 11.5 million;
- Revenues pertaining to the maintenance contract for the HV lines owned by Enel Distribuzione SpA for ? 20.5 million (€ 27.1 million in 2004);
- Revenues for the laying of fiber optic lines on Terna plant and the maintenance and development of the same for € 11.3 million (€ 11,7 million invoiced in 2004) invoiced to Enel.Net Srl;
- Services for the benefit of the subsidiary RTL SpA referring to the period October-December 2005 for HV line maintenance and management fees (€ 0.4 million).

3) CHANGE IN CONTRACT WORK IN PROGRESS - Euro 12.0 million

The change in contract work in progress is the net result of work still pending at December 31, 2005 (€ 3.1 million) and work completed and tested in the year (-€ 15.1 million).

The main increases include the following works:

- Termoli-Larino 380kV power line on behalf of Energia Molise (+0.2 million);
- Construction of HV leads S. Barbara power station on behalf of Enel Power (+0.7 million);
- HV lines at San Giuliano Milanese on behalf of FS (state railway company) (+0.8 million);

The main decreases include:

- Adjustment of the SCTI control system on behalf of GRTN (-12.3 million);
- Supply of reactance Rome South and Rome North HV stations for GRTN (-5.1 million);
- Upgrade/renewal HV plant in Pisa on behalf of FS (-0.7 million);
- Supply HV/MV station for EOS Windenergy (-0,5 million);
- Delivery point Busachi wind power plant for Enel Produzione (-0.6 million).

4) INCREASE IN CAPITALIZED EXPENSES FOR INTERNAL PROJECTS - Euro 26.5 million

Capitalized costs refer to labor costs (€ 13.1 million) and the consumption of materials and machinery (€ 13.4 million). The item records a € 3.9 million increase on last year which is largely attributable to the consumption of materials.

5) OTHER INCOME AND REVENUES - Euro 55.2 million

Other income and revenues are detailed below:

Euro	At Dec.31, 2005	At Dec.31, 2004	Change
Grants from third parties for HV connections	10,242,884	15,262,356	-5,019,472
Other revenues	5,666,793	6,653,570	-986,777
Extraordinary income	39,258,418	6,800,999	32,457,419
Total	55,168,095	28,716,925	26,451,170

Compared to 2004 the item records a decrease of approximately € 5.0 million in capital grants received from third party customers. The other revenues (€ 5.6 million) refer to rent receivable, insurance repayments

for damage to plant, contractual penalties to suppliers and sundry sales. The extraordinary income specifically arises from the following phenomena:

- Positive adjustments from GRTN SpA on network fees referring to prior years (2002/2004) for a total of € 19.9 million;
- Release to revenues of a portion of risk provisions recorded in previous years pertaining to CTR tariff considerations of doubtful collectibility on account of the litigation brought by auto-producers of cip/6 energy (€ 15.0 million) as noted in the relative liability item.

B) OPERATING COSTS

6) RAW MATERIALS - Euro 643.7 million

This item mainly records the electricity purchased on the electricity market and necessary to dispatching requirements. The total amount is to be set against the relative revenues deriving from sales on the electricity market.

It exclusively refers to the two months of effect of the acquisition of the TSO activities.

Euro	At Dec.31, 2005	At Dec.31, 2004	Change
ENERGY PURCHASES			
On DAEM and RTE markets	63,973,341	0	63,973,341
For provision of dispatching service	450,243,714	0	450,243,714
For imbalancing	44,546,081	0	44,546,081
On foreign markets – importation	37,211,864	0	37,211,864
Other energy purchases	26,749,116	0	26,749,116
Total energy purchases	622,724,116	0	622,724,116
Sundry purchases and supplies other than energy	21,019,151	21,670,140	-650,989
TOTAL	643,743,267	21,670,140	622,073,127

The item “sundry purchases and supplies” records costs incurred for the purchase of various materials and equipment used for the operation and maintenance of facilities. It remains essentially in line with last year.

7) SERVICES - Euro 194.0 million

The item consists of the following:

Euro	At Dec.31, 2005	At Dec.31, 2004	Change
Purchase of electricity market-related services	98,949,857	0	98,949,857
Other non-energy services	95,002,199	102,935,197	-7,932,998
Total	193,952,056	102,935,197	91,016,859

Purchases of electricity market-related services chiefly comprises:

- Assignment transport capacity usage rights to EMO;
- Remuneration of interruptible service;
- Remuneration of the availability of production capacity;
- Assignment of transport capacity usage rights on bilateral contracts.

The item “other non-energy services” records a decrease (€ -7.9 million) largely attributable to costs for listing the Company on the Stock Exchange (approximately € 10 million) incurred last year. If this item is excluded service costs are more or less in line with 2004. On a more specific level the item third-party contracts, for routine activities of operation, maintenance and repairs necessary to maintaining plant efficiency, records a decrease (€ -2.2 million) as do the telephone and telecommunication services and special projects for plant (Wind SpA € -2.1 million). Lastly the item records costs incurred for remuneration of the members of the Board of Directors and the Board of Statutory Auditors summarized in the table below.

The schedule has been drawn up with reference to the length of office and on an accruals basis.

Surname	Name	Office held	Period of office	Expiry of office	Office emolument	Bonuses and other incentives	Total
Roth	Luigi	Chairman/Director	nov-dec.05	Approval Fin. Statements2007	12,083.33		12,083.33
Cattaneo	Flavio	Chief Executive Officer	nov-dec.05	Approval Fin. Statements2007	(***)		
De Paoli	Luigi	Director	nov-dec.05	Approval Fin. Statements2007	7,916.67		7,916.67
Garaffo	Mario	Director	nov-dec.05	Approval Fin. Statements2007	12,916.67		12,916.67
Macri	Carmine	Director	nov-dec.05	Approval Fin. Statements2007	7,916.67		7,916.67
Maranesi	Piero Giuseppe	Director	nov-dec.05	Approval Fin. Statements2007	7,916.67		7,916.67
Ponzellini	Massimo	Director	nov-dec.05	Approval Fin. Statements2007	9,166.67		9,166.67
Smurro	Franco	Director	nov-dec.05	Approval Fin. Statements2007	7,916.67		7,916.67
Machi	Salvatore	Director	jan-dec.05	Approval Fin. Statements2007	42,450.00		42,450.00
Romano *	Massimo	Director	jan-dec.05	Approval Fin. Statements2007	28,750.00		28,750.00
Conti *	Fulvio	Chairman/Director	jan-nov.05		20,833.33		20,833.33
Mobili	Sergio	Managing Director	jan-nov.05		350,000.00	341,390.00**	691,390.00
Arnaboldi	Luca	Director	jan-nov.05		34,133.33		34,133.33
Cantarella	Paolo	Director	jan-nov.05		38,300.00		38,300.00
Croff	Davide	Director	jan-nov.05		38,700.00		38,700.00
Machetti *	Claudio	Director	jan-nov.05		34,533.33		34,533.33
Ruzzini*	Paolo	Director	jan-nov.05		34,133.33		34,133.33
Sardo*	Salvatore	Director	jan-jun.05		12,500.00		12,500.00
Total Directors' remuneration					700,166.67	341,390.00	1,041,556.67
Ferreri	Giovanni	Chair. Board of Stat. Aud.	jan-dec.05	Approval Fin. Statements2007	55,000.00		55,000.00
Corvace	Giancarlo	Auditor	jan-dec.05	Approval Fin. Statements2007	45,000.00		45,000.00
Tasca	Roberto	Auditor	apr-dec.05	Approval Fin. Statements2007	33,750.00		33,750.00
Franceschetti	Bruno	Auditor	jan-apr.05		20,250.00		20,250.00
Total Auditors' remuneration					154,000.00		154,000.00
FINAL TOTAL					854,166.67	341,390.00	1,195,556.67

* For the offices held the relative emoluments, for a total amount of Euro 130,750 were attributed to Enel SpA

** This amount refers to a variable part of the fees referring to the year 2005, approved and disbursed in the course of 2005

*** Consideration has not yet been defined

8) LEASE AND RENTALS - Euro 31.9 million

Euro	At Dec. 31, 2005	At Dec. 31, 2004	Change
Rental to NTG owners	12,148,693	0	12,148,693
Rental to GRTN	4,773,186	0	4,773,186
Rental to ETSO-CBT grid owners	2,177,927	0	2,177,927
Other non-energy lease and rentals	12,767,111	12,370,444	396,667
Total	31,866,917	12,370,444	19,496,473

This item includes rental to be paid to the owners of sections of the NTG and rental to be paid to GRTN to cover recognized costs (AEEG resolution no. 15/05). It also includes rental owed to the European TSO, within the ETSO-CBT agreement, for the regulation of cross-border trading of electricity. In accordance with specific AEEG provisions, this charge is counterbalanced by revenues in order to be considered let-through.

Other non-energy lease and rentals primarily consist of property rent payable (€ 6.4 million), leasing costs (€ 4.1 million), costs for crossing fees and miscellaneous fees (€ 2.3 million).

Figures are in line with those recorded in 2004.

9) PERSONNEL - Euro 176.9 million

Personnel costs record a € 13.7 million increase chiefly attributable to:

- The higher cost (approximately € 8 million) ensuing from the inclusion of human resources pertaining to the TSO “transmission and dispatching” activities acquired from GRTN on November 1, 2005;
- The charges for the long-term incentive plans (LTI) of approximately € 4 million;
- The higher unit cost.

The total also includes the additional costs sustained in the period for staff incentives as provided by the sector’s collective agreement.

Euro	At Dec. 31, 2005	At Dec. 31, 2004	Change
Wages and salaries	126,915,881	115,662,916	11,252,965
Social security contributions	33,427,051	31,392,130	2,034,921
Employee termination indemnity	9,631,218	8,981,616	649,602
Other costs	6,944,042	7,133,873	- 189,831
Total	176,918,192	163,170,535	13,747,657

Both the average number of employees by category of employment and their number at December 31, 2005 are shown in the table below, with comparison to the previous year:

	Average number 2005	Number at Dec. 31, 2005	Number at Dec. 31, 2004
aSenior management	43	74	34
Middle management	248	403	221
Office staff	1,532	1,813	1,467
Workers	1,143	1,098	1,149
Total	2,966	3,388	2,871

Compared to 2004 the company staff increased by +517 employees (taking into account the 586 coming from GRTN SpA as from November 1, 2005 and the 34 coming from RTL SpA as from October 1, 2005).

10) AMORTIZATION, DEPRECIATION AND WRITE-DOWNS - Euro 157.5 million

Amortization of intangible assets:

This item records the amortization applied for the year and calculated on the basis of the expected useful life of the assets.

Depreciation of tangible assets:

This item includes accruals for the year (€ 151.7 million) calculated on the basis of the depreciation rates representing the remaining useful life of the company's plant (in 2004: € 143.5 million).

Write-downs of assets:

These amount to € 0.1 million and refer to the release of work in progress and advances for abandoned projects.

11) CHANGES IN INVENTORIES - Euro 2.9 million

This shows the net negative change in inventories during the year.

12) PROVISIONS FOR RISKS - Euro 0.9 million

These include accruals made at December 31, 2005, as described in greater detail in the section on the provision for risks and charges.

14) OTHER OPERATING COSTS - Euro 21.3 million

This item records a sharp decrease (€ -7.5) compared to 2004 due to adjustments payable on network usage fees for the year 2002/2003 (€ 14.8 million).

It also includes local indirect taxes (€ 3.9 million), registration fees for the acquisition of the TSO activities (€ 2.8 million), taxes paid abroad not deductible in Italy (€ 4.3 million), ordinary losses for disposal of power lines (€ 3.3 million) and discounts on electricity supplied to retired personnel (€ 2.3 million).

C) FINANCIAL INCOME AND EXPENSE - Euro -9.9 million

Other financial income

A breakdown of other financial income is provided below:

Euro	2005	2004	Change
Income from investments	10,316,279	4,882,457	5,433,822
Other financial income	127,863	191,324	-63,461
Interest on current account with former Parent Company	3,301,032	4,353,182	-1,052,150
Interest on loans to subsidiaries	0	11,598,170	-11,598,170
Interest on equity from subsidiaries	28,939,342	13,863,391	15,075,951
Interest on bank c/a and short-term loans	1,758,302	0	
Total	44,442,818	34,888,524	9,554,294

Financial income from subsidiaries records an increase in dividends paid by TSN (+5.4 million) and in particular in the item "Interest on Equity", a specific form of return on internal funds, provided for by prevailing Brazilian legislation, and passed by both the subsidiaries TSN and Novatrans (+15.1 million), for this year.

Interest and other financial expense

A breakdown of interest and other financial expense is provided below:

Euro	2005	2004	Change
Interest and expense on loans from former Parent Company Enel SpA	0	25,661,302	-25,661,302
Interest on EIB financing	8,861,480	7,036,272	1,825,208
Financial expense on derivatives (swaps)	-15,474,187	2,552,143	-18,026,330
Interest on Bond Issue	64,700,000	11,521,918	53,178,082
Other interest and financial expense	613,712	395,213	218,499
Profit and loss on foreign exchange trading	-4,358,814	-23,254	-4,335,560
Total	54,342,191	47,143,594	7,198,597

This item specifically records financial expense pertaining to the bond issues (+53.2 million against the 2004 figure which accounted for only 2 months), and the EIB loans (+1.8 million) which have risen as a result of variations in interest rates.

The expense pertaining to said loans is mitigated by the positive effects generated by the hedging instruments in the portfolio. The profit and loss on foreign exchange trading are linked to the general appreciation of the R\$ during the year which gave rise to said positive differences particularly upon repatriation of capital from Brazil.

E) EXTRAORDINARY ITEMS - Euro 7,6 million

This item records a negative balance of € 7,6 million. Extraordinary income derives from excess income taxes recorded in the previous year in relation to the liability actually recognized in the company's tax return (€ 5.6 million) as well as from prior year gains referring to higher tax credits deductible proving in Italy for withholdings effected in the previous year in Brazil (€ 1.9 million).

Extraordinary expense totaled € 15.2 million and entirely refers to early retirement agreements implemented during the year with employees and senior management who are entitled to pension.

22) INCOME TAXES - Euro 160.8 million

Income taxes which account for 37.50% (39.52% in 2004) of the pre-tax profit have decreased by a total of € -4.4 million.

Euro	At Dec.31, 2005	At Dec.31, 2004	Change
Current taxes:			
- IRES	136,644,804	85,139,673	51,505,131
- IRAP	28,566,500	19,358,816	9,207,684
Prepaid taxes	2,731,848	7,457,414	-4,725,566
Deferred taxes	-7,118,763	53,291,673	-60,410,436
Total	160,824,389	165,247,576	-4,423,187

Current taxes have increased by € 60.7 million, chiefly due to the effects of law no. 266 of Dec. 23, 2005 (the so-called Finance Act for 2006) which introduced, amending the Consolidation Act on Income Tax (TUIR), with effect from Jan. 1, 2005, Article 102-bis. This article limits, compared to previous years, the deductibility of depreciation of tangible assets used in some regulated activities, such as the management of the national electricity transmission grid.

The breakdown of prepaid taxes is represented by provisions for:

- Tax recovered amounting to € 8.2 million, due to the use/release of risk provisions taxed in previous years;
- Tax prepayments relating to temporary differences of € 5.5 million that emerged in the year for accruals to the risk provision for litigation and the provisions for future risks and charges.

Deferred taxes relate to:

- The portion of depreciation in excess of the ordinary depreciation rate, accrued for tax purposes and the allocation to the bad debt provision, also for tax purposes (€ 7.7 million), as permitted by Article 109 of the TUIR;
- The utilizations arising from the taxation of depreciation exceeding, in previous years, the deductible limit (€ 15.5 million);
- The realignment of deferred taxes to the new average IRAP rate (€ +0.7 million), quantified on the basis of the tax rate in force in the years in which reversal will take place.

Changes in corporate income tax (IRES) from the previous year are shown in the reconciliation between the expected and the effective income taxes as below:

In millions of Euro	2005
Pre-tax profit	428.9
- Additional depreciation	-16.2
- Take-back of depreciation exceeding deductible portion	41.5
- Changes in risk provisions	-10.6
- Dividends and IOE from subsidiaries - exempt portion	-39.3
- Other increases/decreases	9.7
TAXABLE INCOME (IRES)	414.0
Tax expense (33%) for the year	136.6

The reconciliation between the expected and the effective local business tax (IRAP) is instead shown below:

In millions of Euro	2005
Difference value of production and operating costs	446.4
- <i>Personnel</i>	176.9
- <i>Additional depreciation</i>	-16.2
- <i>Take-back of depreciation exceeding deductible portion</i>	41.5
- <i>Changes in risk provisions</i>	-16.6
- <i>Other increases/decreases</i>	12.8
TAXABLE INCOME (IRAP)	644.8
Tax expense (average 4.43%) for the year	28.6

TRANSACTIONS WITH RELATED PARTIES

Related parties have been identified with reference to the provisions of Article 2 of the CONSOB Issuers' Regulations pursuant to CONSOB resolution no. 14990 of 14 April 2005, as well as to the international accounting standard IAS 24 concerning financial reporting on transactions with related parties.

In view of the transactions implemented by the Company this year, the related parties are represented by transactions with the subsidiaries and with the associated company Cesi SpA.

The transactions implemented by Terna with the related parties RTL SpA and Cesi SpA essentially concern the provision of services governed by specific contracts stipulated between the parties in accordance with the market conditions that would have been applied between two independent parties.

Specifically the contracts with the subsidiary that generate expenses for Terna refer to:

- Rental due from the Parent Company, in its capacity as operator of the national transmission grid, for usage of the portion of NTG owned by the subsidiary;
- Management and coordination of all the transactions associated with the administration of both the financial resources and requirements and the treasury services and of every other related transaction (so-called treasury contract).

While the contracts generating revenues refer to:

- Services for routine activities of operation and maintenance of the HV lines owned by RTL SpA for the purposes of maintaining plant efficiency;
- Assistance and advice in the administrative, financial, legal/corporate, tax field as well as strategic policy-making and industrial coordination functions (so-called Management Fee contract).

With the associated company Cesi Spa the contracts generating expenses chiefly refer to technical consultation, study and research, planning and experimentation services received by Terna, while the relations generating revenues essentially relate to rental of laboratories and other similar structures for specific uses.

As far as the Brazilian subsidiaries Novatrans Energia SA and Trasmissora Nordeste Sudeste SA are concerned, the economic relations and the relative credit balances existing at Dec. 31, 2005, derive from the so-called Interest on Equity (IOE), the financial income due to the Parent Company by way of remuneration of the invested capital and paid periodically upon specific authorization of the local financing banks (BNDES - IDB) and the Brazilian Central Bank.

The following table shows, in millions of euro, expenses and revenues for the year as well as receivables and payables outstanding at year-end.

	ECONOMIC RELATIONS			FINANCIAL BALANCES			
	Revenues	Costs for the year	Investment costs	Receivables	Payables	Guarantees	Doubtful debt prov. Loss on receivables
RTL SpA	0.4	0.9		0.4	5.7		
Cesi SpA	0.2	1.7	1.6	0.1	2.6	0.8	
Novatrans Energia SA	14.7			13.8			
TSN Transmissora Sudeste Nordeste SA	14.3			13.4			
Total	29.6	2.6	1.6	27.7	8.3	0.8	

Guarantees refer to those received on the expense generating contracts stipulated.

Information on the stock option plans and the remuneration of the members of the Board of Directors and the Board of Statutory Auditors in the year at December 31, 2005, can be found in previous paragraphs of this document. Information on the shares held by Directors and Auditors can instead be found in the company's Report on Operations at December 31, 2005.

OTHER INFORMATION

Pension fund expense

The charge taken in respect of the extraordinary contribution due upon the suppression of the Electricity Sector Employee Pension Fund with Law 488 of December 23, 1999 (the Finance Act for 2000), which was originally recognized as an intangible asset, has been nil since 2002 because the company opted to amortize it in income over three years (2000, 2001 and 2002), in accordance with the provisions of the same law. If the company had opted to amortize the charge over 20 years, which was also an option under the law and in line with reference accounting standards, intangible assets would have shown an additional liability of around € 70 million at December 31, 2005 (about € 75 million at December 31, 2004).

More detailed information on the activity performed by the company and description of the significant post-year end events can be found in the relevant sections of the Report on Operations at December 31, 2005.



REPORTS

REPORT OF THE BOARD OF STATUTORY AUDITORS TO THE SHAREHOLDERS OF TERNA SPA

**PURSUANT TO ARTICLE 2429, PARAGRAPH 2, OF THE ITALIAN CIVIL CODE AND ARTICLE 153
OF LEGISLATIVE DECREE 58/1998**

To the Shareholders' Meeting of Terna SpA

Shareholders,

pursuant to Article 153 of Legislative Decree 58/1998, we inform you that in the year ended December 31, 2005, we performed the supervisory activity required by the law, in accordance with the code of practice recommended for statutory auditors by the National Board of Chartered Accountants.

In particular:

- We attended the meetings of the Board of Directors and were regularly informed by the Directors of the activities performed and of the major economic, financial and equity transactions carried out by the Company, and are satisfied that the resolutions were not only implemented but also complied with the provisions of law and the bylaws and were not patently imprudent, risky, in potential conflict of interest or at variance with the resolutions passed by the Shareholders' Meeting;
- We examined the development and conclusion of the process for unification of the ownership and management of the National Transmission Grid, implemented pursuant to Law 290/03;
- We gathered information and monitored, as far as our authority permitted, the organisational structure, observing the adequacy of the same, also in view of the modifications implemented following the procedure for integration of the activities acquired with the TSO ("Transmission System Operator") business segment, sold off by GRTN SpA;
- we monitored the administrative and accounting system, assessing the reliability of the latter in providing a true and fair view of operations and also monitored compliance with sound management practices. These activities were conducted both through direct observation and information gathered from management;
- We held meetings, pursuant to Article 150 of Legislative Decree 58/98, with the Independent Auditors, for the purpose of mutual exchange of information and data. Over the course of the various meetings no facts worthy of mention in this report emerged;

- We assessed and monitored the existing internal control system through information received from management, including specific regular reports issued by the head of the internal control department. No facts worthy of mention in this report emerged, thus proving the adequacy of the existing control system;
- We monitored the adequacy of the instructions issued by the Parent Company to the subsidiaries TSN and Novatrans in relation to the reporting obligations provided by the law;
- We verified, through direct inspections and through information obtained from the Independent Auditors, compliance with the provisions of law regarding the preparation of the financial statements, with a particular focus on the formats adopted, content and accounting policies applied. In this regard we report that the Company, in accordance with the options offered by Legislative Decree 38/2005, opted not to use the international accounting standards in drawing up the financial statements 2005. We also verified the completeness of the Report on Operations prepared pursuant to Article 2428 of the Italian Civil Code and the adequacy of the same in describing the transactions with related parties implemented in 2005.

The only other aspects, relating to the financial statements, that the Board of Statutory Auditors believes to be of significance are the following:

- The economic and financial effects arising from the process of unification of the ownership and management of the National Transmission Grid, with particular regard for the recording, under intangible fixed assets, of the concession to exercise on an exclusive basis the activity of transmission and dispatching of electricity. The value of the aforesaid concession is equal to the difference between the price paid for acquisition of the TSO activities from GRTN SpA and the book value of the assets and liabilities acquired;
- The decrease in the value of equity investments due to the algebraic sum of the negative effect deriving from the decrease in value of the equity investment held in the Brazilian company TSN due to the exercise of the right of redemption of redeemable shares on the part of Terna, and of the increase in value of the equity investments associated with the acquisition of the entire share capital of RTL SpA;
- The change in composition of deferred taxes as a result of the effect of the new tax legislation on amortisation and depreciation, set forth in Article 102-bis of the Consolidation Act on Income Taxes, for assets falling under the homogeneous categories of the electricity sector, determined by

the Italian Authority for Electricity and Gas, which defined longer useful lives than those previously recognised;

- The ordinary contingent assets resulting from positive adjustments determined by GRTN for the years 2002/2004 and from the release of provisions for risks relating to the CTR consideration ("Transmission service consideration") of which collection is doubtful owing to the dispute brought by auto-producers of CIP/6 energy.

No objections are raised in the Independent Auditors' Report on the Financial Statements 2005, but attention is drawn to the following aspects:

- The reporting of the extraordinary charge ensuing from suppression of the Electricity Sector Social Security Fund;
- The drawing up of the Group consolidated financial statements.

The Board has no remarks to make with regard to the above-mentioned aspects. In the course of the monitoring activity described above and, on the basis of information obtained from the Independent Auditors and from the Managers of Terna, no omissions, reprehensible facts or irregularities necessitating report to the appropriate authorities or mention hereunder have emerged.

We also report that:

- The Board of Directors, of which the composition was changed on November 2, 2005, met 9 times and the Board of Statutory Auditors attended all the meetings. During 2005 the Board of Statutory Auditors met 7 times;
- During 2005 the Board of Statutory Auditors issued two opinions pursuant to Article 2389, paragraph 3, concerning the fees for the members of both the Remuneration Committee and the Internal Control Committee and concerning the remuneration of the Chief Executive Officer. Instead the Independent Auditors issued a single opinion for the distribution of interim dividends, pursuant to Article 2433-bis of the Italian Civil Code;
- No report pursuant to Article 2408 of the Italian Civil Code was received, nor was any complaint filed by third parties;

- The Company has adopted a Corporate Governance system consistent with the recommendations contained in the Self-Disciplinary Code provided by Borsa Italiana SpA

Furthermore, and once again in line with the provisions set forth by Borsa Italiana, the Company has adopted:

- an adequate Code of Conduct for handling and disclosing to the market information relating to transactions of financial instruments (“Code”), issued by Terna or by its subsidiaries, performed by persons vested with the relevant decisional powers within the corporate framework and with access to price sensitive information;
- adequate internal Regulations setting forth provisions relating to the management and handling of confidential information (“Regulations”) and describing the procedures to be observed in disclosing documents and information concerning the Company and its subsidiaries to external parties, with particular regard for the price sensitive information referred to in Article 114, paragraph 1, of Legislative Decree 58/98.

The Code was subject to revision following new legislation concerning market abuse. The entry into force of the updated Code was scheduled for April 1, 2006.

Lastly to comply in full with the recommendations set forth in Consob notice of April 6, 2001, and subsequent amendments and integrations, we report the following:

1. During 2005 no irregular or unusual transactions were implemented with related companies or with third parties;
2. With reference to routine transactions with related parties (subsidiaries and associated companies), these primarily relate to the supply of institutional assistance or consulting services (management fee contract), the supply of services for routine activities of operation and maintenance of HV lines, transactions of a financial nature and treasury services, income from the rental of laboratories and other similar structures for specific uses and the receipt of technical consulting services, study and research services and rental payable for the use of portions of the National Transmission Grid. On the basis of sample checks carried out by the Board of Statutory Auditors and of disclosures received, these transactions prove to be in line with the interests of the Company.

As far as the economic effects of the aforesaid transactions are concerned, these generated total revenues equal to € 29.6 million and total costs equal to € 2.6 million.

As specifically documented, in addition to the auditing assignment, KPMG provided the following services:

- assignment for the audit of the IFRS reconciliation tables of Terna and its subsidiaries, for an amount equal to € 30,000, plus € 1,270 as refund of expenses;
- assignment for the issue of an opinion pursuant to Article 2433-bis of the Italian Civil Code, for an amount equal to € 30,000, plus € 1,295 as refund of expenses.

Other than the activities listed, from the information in our possession, further assignments do not appear to have been entrusted to subjects associated with the Independent Auditors.

In view of the foregoing, the Board of Statutory Auditors, as far as its authority permits, finds no impediment to the approval of the Financial Statements 2005 prepared by the Board of Directors

Rome, April 11, 2006

THE BOARD OF STATUTORY AUDITORS

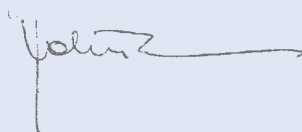
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(Translation from the Italian original which remains the definitive version)

Report of the auditors in accordance with article 156 of legislative decree no. 58 of 24 February 1998

To the shareholders of
 Terna S.p.A.

- 1 We have audited the financial statements of Terna S.p.A. as at and for the year ended 31 December 2005. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audit.
- 2 We conducted our audit in accordance with the auditing standards recommended by Consob, the Italian Commission for Listed Companies and the Stock Exchange. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement and are, as a whole, reliable. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

Reference should be made to the report dated 11 March 2005 for our opinion on the prior year figures which are presented for comparative purposes as required by law.

- 3 In our opinion, the financial statements of Terna S.p.A. as at and for the year ended 31 December 2005 comply with the Italian regulations governing their preparation; therefore they are clearly stated and give a true and fair view of the financial position and results of the company.
- 4 We draw your attention to the following disclosures that the directors have provided in the notes to the financial statements:
 - 4.1 The notes to the financial statements show the effects on the financial statements of the application of Law no. 488/1999, governing the recognition of the extraordinary expense that arose as a result of the suppression of the Electricity Sector Employee Pension Fund.



Terna S.p.A.
Report of the auditors
31 December 2005

- 4.2 The company holds controlling interests in a number of companies and, in accordance with current legislation, has prepared consolidated financial statements. Such statements are presented in addition to its own financial statements in order to furnish adequate information on the financial position and results of both the company and the group. We have audited the consolidated financial statements and these (with our audit report thereon) are presented together with the statutory financial statements.

The notes disclosed the effects that would have impacted the financial statements had the company accounted for its investment in subsidiaries using the equity method.

Rome, 11 April 2006

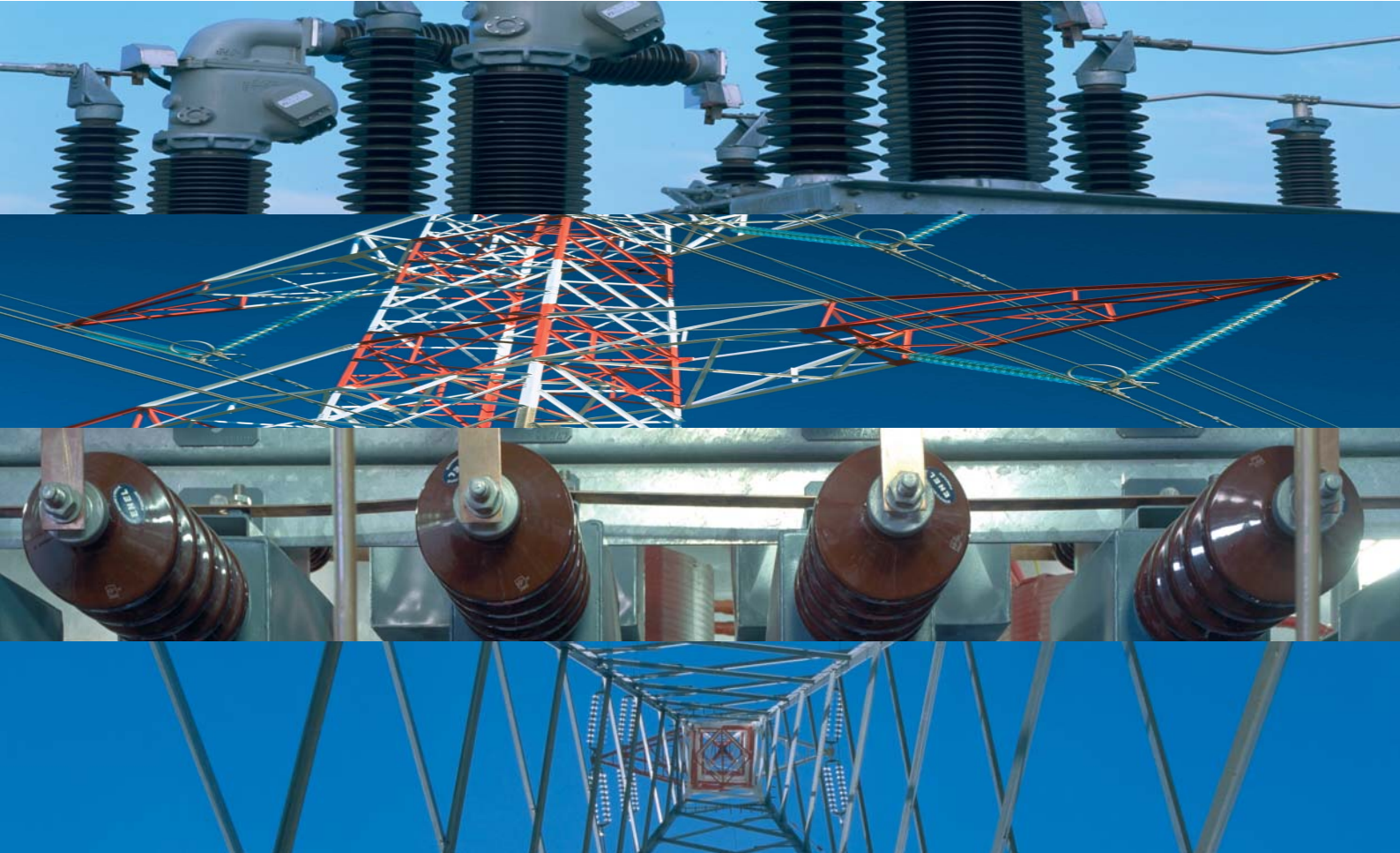
KPMG S.p.A.

(Signed on the original)

Bruno Mastrangelo
Director

HAVING CLEAR POINTS MEANS BETTER MOVING





CONSOLIDATED FINANCIAL STATEMENTS OF THE TERNA GROUP 2005

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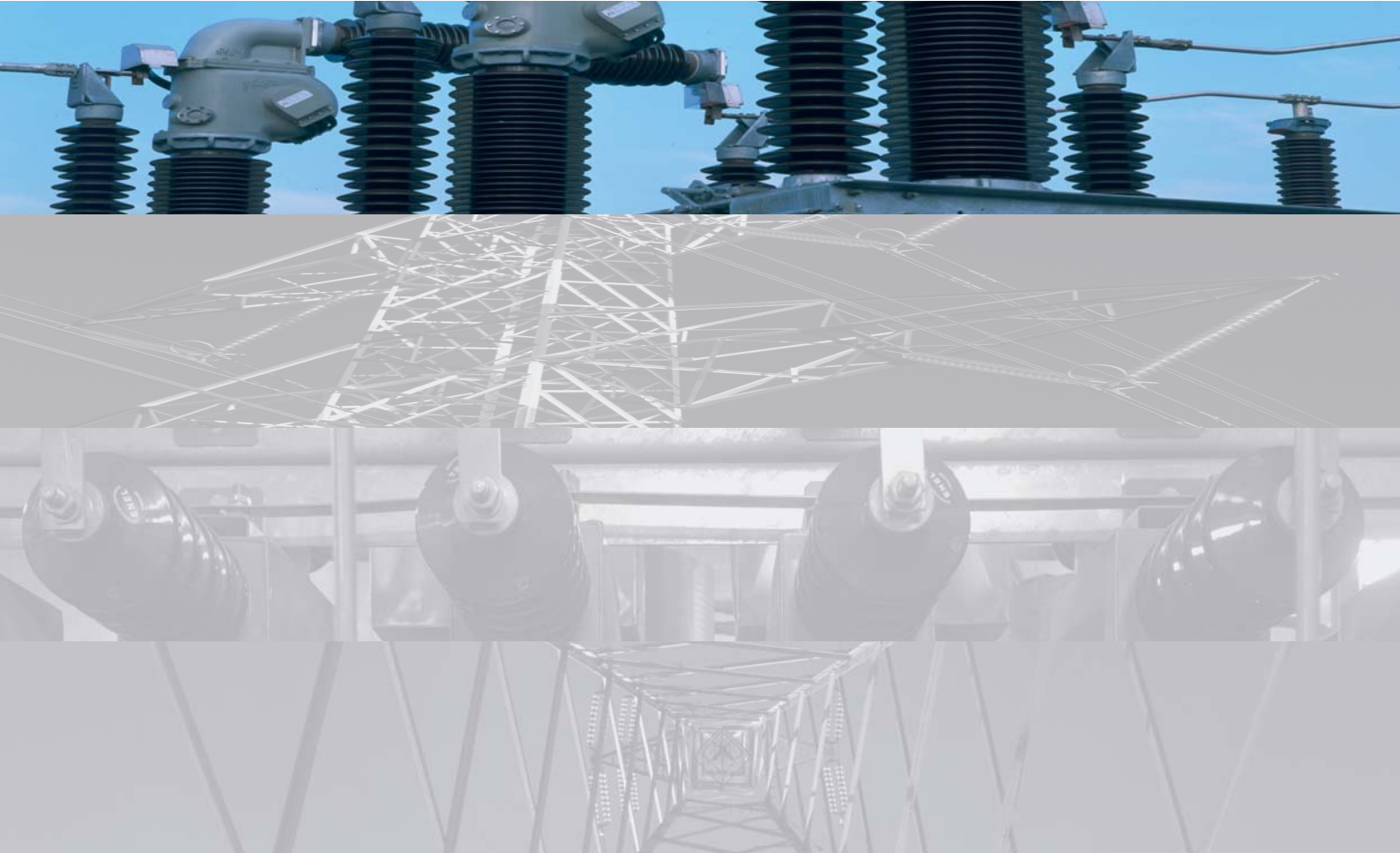
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REPORT ON OPERATIONS OF THE TERNA GROUP

INTRODUCTION

The comparative figures for the 2004 accounting period have been re-determined in accordance with the international accounting standards in these consolidated financial statements.

Pursuant to Article 82 of the CONSOB Resolution No. 11971/1999, the Company availed of the exemption from publishing the quarterly report as of December 31, 2005.

As far as the most significant events in 2005, reference legislation and energy data, Corporate Governance, and other information are concerned, reference should be made to the Report on Operations accompanying the financial statements of Terna SpA.

SCOPE OF CONSOLIDATION

The scope of consolidation includes the wholly-owned subsidiary companies, Novatrans and RTL Spa. CESI SpA, in which an interest of 24.36% is held, is carried at equity.

Brazil

Significant events

On December 15, Transmissora Sudeste Nordeste S.A. ("TSN") signed an agreement with the companies Control Y Montajes Industriales CYMI S.A. and Fluxo Engenharia Ltda for the acquisition of the entire share capital of Munirah Transmissora de Energia S.A. ("Munirah").

Munirah is the concession holder of 106 km transmission lines and two sub-stations in the State of Bahia, operative as from last October, which represent the extension of TSN's 500 kV lines closing the North-North-east circuit.

The price for 100% of the company's share capital was set at Reais 48 million (around € 17 million). The concession, which the company holds, envisaged annual revenues of Reais 18 million (approximately € 6 million).

The closure of the transaction is anticipated for the end of March 2006.

ANEEL resolutions and authorizations

On June 30, 2005 ANEEL established the new values of the Concession Fee (RAP) in force as from July 1, 2005 until June 30, 2006. The TSN and Novatrans fees were respectively set at R\$ 245 million and R\$ 269 million, reflecting the adjustment for inflation (IGPM rate) accumulated between June 2004 and May 2005, equal to 9.0752%. ANEEL also acknowledged an additional one-off increase, to be received in 12 monthly instalments as from July 2005 relating mainly to the adjustment for the additional PIS/COFINS rates paid by the companies up until May 30, 2005, amounting to around R\$ 13 million for TSN and R\$ 14 million for Novatrans.

In August, Aneel authorized the agreement with Transener for the management of the Novatrans lines. On September 12, 2005, having obtained the prior authorization of ANEEL, an extraordinary general shareholders' meeting of TSN was held, which amended the corporate purpose by extending it so as to permit the company to take part in other concessions or in other companies who are electricity grid concession holders.

Payments to Terna

During the accounting period, TSN paid out € 15.2 million in interest on capital and € 9.6 million in dividends to Terna.

Exchange rate performance

During the period, the Brazilian Real appreciated against the US Dollar, and even further against the Euro.

EXCHANGE RATE VALUES AT THE END OF EACH QUARTER

Euro	Jan '05	Mar '05	Jun '05	Sept '05	Dec '05
BRL/US\$	2.62	2.67	2.35	2.22	2.32
BRL/EUR	3.42	3.46	2.85	2.67	2.74
EUR/US\$	1.30	1.30	1.21	1.20	1.18

The appreciation relating to the Real is attributable: (i) to high internal interest rates (the SELIC base rate rose to 19.75% only to then drop at period end to 18.0% on an annual basis); (ii) the improvement in the fundamentals of the Brazilian economy also witnessed by the sharp improvement in the spread between Brazilian and American government securities which fell from 463 basis points at the end of 2004 to 306 basis points at period.

Operations

TSN

During the period, the Sudeste - Nordeste kV 500 transmission line, with an extension of 1,062 km⁽¹⁾, from Serra da Mesa (Goias State) to Sapeaçu (Bahia State), including the intermediate sub-stations of Rio das Eguas, Bom Jesus da Lapa and Ibicoara, was fully operative.

Construction activities

The supply and installation of the TVCs on the primaries of the transformers at the Sapeaçu and Bom Jesus da Lapa stations was carried out. Two additional reserve reactors were supplied and installed.

Service Quality

The ratios relating to availability and fault rate for 2005 are indicated in the table below, excluding external causes and unforeseeable circumstances. The 2004 figures are shown in brackets.

AVAILABILITY AND FAULT RATE

	AVAILABILITY %		FAULT RATE ⁽²⁾	
	2005	2004	2005	2004
Power lines (including reactors)	90.65	99.90	0.00	0.85
Bar reactors	99.98	99.99	0.00	0.00
ATR	99.07	99.94	0.25	0.25
SVC	99.88	99.83	4.01	5.01

⁽²⁾ Number of faults per line (100Km)/component (units)

⁽¹⁾ Length "As Built" of the 500Kv lines (compared to 1,050 km in the concession agreement), in addition to 15 km relating to the 230 kV double-circuit stretches (considering them as two individual circuits) for a total of 1,0

The fault rate on the lines is conditioned by a series of faults affecting the lines reactors, deriving from an oil corrosion problem; the necessary corrective action is currently underway. Shareholders are informed that the line function is considered unavailable in the event of the unavailability of the related reactors even if the line is operative.

NOVATRANS

During 2005, the North-South II kV 500 connection, with an extension of 1,278 km, from Samambaia (Federal District) to Imperatriz (Maranhão State) including the intermediate sub-stations of Serra da Mesa, Gurupí, Miracema and Colinas, was fully operative.

Construction activities

During 2005, activities continued for the creation of the new Ancillary Services of all the stations with a power supply which is independent from Furnas and Eletronorte. The Samambaia and Gurupi generators were started up. Supplies and installations are underway for the MV lines and the MV/lv transformations. Two reserve reactors have been installed at the Samambaia and Serra da Mesa stations. The emergency situation which came about following the presence of corrosive oil in part of the Novatrans and TSN reactors, made it advisable to provisionally install the Samambaia reserve reactor at another station. The emergency satellite link has been installed, permitting communication between the Samambaia, Serra da Mesa and Sapeaçu stations with the Rio De Janeiro offices.

Service Quality

The ratios relating to availability and fault rate for 2005 are indicated in the table below, excluding external causes and unforeseeable circumstances. A comparison with the same period last year is not possible since: (i) some of the plants have become operative during 2004; (ii) since the period of grace for the purposes of Parcela Variavel was applicable during 2004, extraordinary maintenance measures were carried out reducing the availability and increasing the fault rate.

AVAILABILITY AND FAULT RATE FOR 2005

	Availability %	Fault rate ⁽¹⁾
Power lines (including reactors)	99.82	0.24
FSC	99.87	0.67
TCSC	98.12	28.03

⁽¹⁾ Number of faults per line (100Km)/component (units)

Shareholders are informed that the figures relating to the Capacitor Stand functions, both fixed (FSC) and variable (TCSC), are conditioned by a number of project errors made by the supplier which are being corrected by means of measures which have led to extraordinary out-of-service conditions.

Italy

RTL Rete di Trasmissione Locale

As from October 1, 2005 Terna acquired the equity investment in RTL SpA (formerly Acea Trasmissione SpA) from ACEA SpA. This change led to a series of corporate changes described below:

As of September 29, 2005 the letters of resignation of the members of the Board of Directors and the Board of Statutory Auditors were signed, effective as of September 30, 2005.

As of September 30, 2005, Acea Trasmissione general shareholders' meeting resolved;

- The appointment of the Chairman and the members of the new Board of Directors
- The appointment of the Chairman and the members of the new Board of Statutory Auditors
- The amendments to the Articles of Association, in particular the corporate name from Acea Trasmissione SpA to RTL Rete di Trasmissione Locale SpA.

Subsequently and once again on September 30, 2005 a Board Meeting was held which resolved on:

- The appointment of the Chief Executive Officer;
- The appointment of the Secretary to the Board;
- The structure of powers within the corporate sphere;
- The transfer of the registered offices to Via Arno, 64 Rome.

Operations

Up until September 30, 2005 RTL SpA had directly ensured the control, maintenance and development of the overhead power lines conferred, including the portion of the National Transmission Grid which it availed of, whilst with regards to the underground power lines forming part of the same National Transmission Grid, these activities have been carried out under service agreements by ACEA Distribuzione.

At the same time, ACEA Trasmissione ensured the control and maintenance of the entire network of high voltage overhead power lines owned by this company, equal to approximately 409 Km, under service agreements carried out by ACEA Distribuzione.

As a result of the transfer of the shareholding from Acea SpA to Terna, these agreements have been concluded. As from October 1, 2005, by contrast Terna was entrusted, under a specific contract, with the operating activities (with the exclusion of the running) and the ordinary maintenance activities in relation to the power lines belonging to RTL, and more specifically comprising: (i) inspections and checks; (ii) emergency service activities; (iii) processing and implementation of plans for conventional work and that carried out on line equipment; (iv) handling of the interferences; (v) handling of unavailability and operating events; (vi) ordinary maintenance measures; (vii) damage to the assets of RTL..

Another two new contracts have been stipulated with the subsidiary RTL also disciplined on the basis of current market conditions or with reference to the improvements made in relation to the cost anticipated proportionate to the product/service quantity used.

These contracts include;

- The General Services Contract, which involves Terna guaranteeing strategic policy and industrial co-ordination functions, the supply, directly or indirectly, in the interests of the company, of services of corporate interest, also taking steps to see to: (i) the administrative and financial co-ordination of the company, including therein the layout and management of the financial activities of the same and (ii) the supply of other services in favour of the company in areas of specific corporate interest;
- A Cash Management Contract by means of which Terna ensures the management and co-ordination of all the transactions from time to time associated with the management of both the financial resources and the requirements and the cash management services as well as the performance of any other related transaction.

Once again as of October 1, 2005 all the blue and white-collar staff were transferred from RTL to Terna SpA. Therefore, as of December 31, 2005 the company had just one Executive on the workforce. The consolidation of the economic results of the company concerns the last three months of the 2005 accounting period.

THE TERNA GROUP'S OPERATING AND FINANCIAL REVIEW

The consolidated financial statements as of December 31, 2005 closed with net income of € 297.9 million, after having provided amortization and depreciation on fixed assets totalling approximately € 175.1 million, net financial expense of € 82.0 million, and income taxes amounting to € 169.0 million.

Revenues amounted to around € 1,087.4 million, of which € 957.8 million referring to the payment for the use of the National Transmission Grid. More specifically, fees for grid usage have been assessed for the parent company for a total of around € 786.8, involving a decrease of around € 24.0 million (- 3.0%) when compared to the same period in 2004. The contribution of the subsidiary companies comes to € 169.8 million (of which € 88.8 million for Novatrans and € 81.0 million for TSN).

Operating costs amounted to approximately € 365.2 million, of which € 201.7 million relating to staff and € 118.8 to services.

Income taxes for the year, amounting to € 169.0 million, include € 159.8 million relating to the parent company, € 0.6 million to Novatrans, € 8.4 million to TSN and € 0.2 million to RTL.

The balance sheet discloses net tangible fixed assets amounting to € 4,965.9 million, net employed capital of € 4,170.9 million covered by shareholders' equity amounting to € 1,902.2 million (45.6%, compared to 48.2% as of December 31, 2004) and net financial debt of € 2,268.7 million (54.4%, compared to 51.8% as of December 31, 2004).

The reclassified income statement of the Terna SpA Group, for 2005 and 2004 is summarized in the following table, obtained by classifying the data presented in the income statement.

Income statement

TERNA GROUP BALANCE SHEET

In millions of Euro	As of Dec. 31, 2005	As of Dec. 31, 2004	Change	%
REVENUES				
NTG usage fees	957.8	929.1	28.7	3.1
Other energy items	6.9	0.0	6.9	0
Other sales and services	59.1	64.8	-5.7	-8.8
Other sundry revenues and income	63.6	26.1	37.5	143.7
Total revenues	1,087.4	1,020.0	67.4	6.6
OPERATING COSTS				
Payroll and related costs	201.7	178.2	23.5	13.2
Services and use of third-party assets	118.8	129.8	-11.0	-8.5
Materials	25.4	20.1	5.3	26.4
Other costs	45.8	63.6	-17.8	-28.0
Capitalized costs	-26.5	-22.5	-4.0	17.8
Total operating costs	365.2	369.2	-4.0	-1.1
Gross Operating Margin	722.2	650.8	71.4	11.0
Amortization and depreciation	175.1	156.3	18.8	12.0
OPERATING INCOME	547.1	494.5	52.6	10.6
Net financial income (expense)	-82.0	-99.9	17.9	-17.9
Income/(expense) deriving from the valuation of equity investments using the equity method	1.8	0.0	1.8	100.0
INCOME BEFORE TAXATION	466.9	394.6	72.3	18.3
Income taxes for the period	-169.0	-163.5	-5.5	3.4
NET INCOME PERTAINING TO THE GROUP AND TO MINORITY SHAREHOLDERS	297.9	231.1	66.8	28.9
GROUP NET INCOME	297.9	231.1	66.8	28.9

Revenues for 2005, amounting to € 1,087.4 million (€ 915.5 million for the parent company, € 1.5 million for RTL and € 170.4 million for the Brazilian subsidiaries), disclosed an increase of € 67.4 million (+ 6.6% with respect to the € 1,020.0 million in 2004). The net increase in revenues essentially derives from:

- The higher fee for the use of the grid amounting to around € 28.7 million including:
 - a decrease amounting to around € 24 million for the parent company, essentially attributable to the tariff process (zone effect, Cross Border Trade and adaptation of the NTG ownership percentage) for approximately € 37 million offset by an increase of around € 10 million for the payment deriving from the activities pertaining to the acquisition of the GRTN business segment;
 - an increase for the Brazilian companies of around € 51.4 million, essentially attributable to the rise in amounts for the completion of the power lines of Novatrans in Spring 2004 (€ 23.4 million), and the effect of the appreciation of the average exchange rate in 2005 when compared to 2004 (€ 28 million);

- an increase of around € 1.3 million (referring to the last quarter of 2005) for RTL, which was not present in 2004;
- The increase in other energy items by around € 7 million, attributable to the parent company and deriving from the Dispatching and Gauging activities acquired together with the GRTN business segment, which were not present in 2004;
- Fewer other sales and services essentially attributable to the parent company and deriving from fewer services provided to Enel Group companies, referring in particular to the maintenance contract for the high voltage power lines belonging to ENEL Distribuzione;
- An increase in other revenues and income of € 37.5 million, essentially attributable to the parent company, for greater out-of-period income relating to the adjustments on the grid rental fee for the years 2002/2004 (approximately € 20 million) and the freeing up of provisions for risks and charges set aside in previous years (around € 16.5 million).

Operating costs amounted to € 365.2 million (€ 322.8 million for the parent company, € 0.3 million for RTL and € 42.1 million for the foreign subsidiaries) and decreased by 1.1% (- € 4.0 million) on 2004 (€ 369.2 million), as a result of:

- Higher payroll and related costs by around € 23.5 million essentially attributable to:
 - the additional cost (around € 8 million) consequent to the inclusion of the human resources forming part of the GRTN “transmission and dispatching” business acquired in November 1, 2005;
 - the charges pertaining to the year for the long-term incentive plan (LTI) for around € 4 million and the additional redundancy incentive costs totalling approximately € 5 million;
 - the additional cost for actuarial charges and other non-recurring costs;
- Greater consumption of materials for approximately € 5.3 million (€ 3.9 million for the parent company, € 1.2 for the Brazilian companies and € 0.2 for RTL);
- Lower costs for services and other costs, for a total of about € 15 million, essentially attributable to the parent company and essentially identifiable in the lower out-of-period income for grid usage fees (€ 15 million), higher costs incurred in 2004 for the stockmarket listing of the Company (€ 10 million), additional costs for taxes relating to the acquisition of the business segment from GRTN (€ 2.8 million) and for taxes paid abroad which are not deductible in Italy (€ 4.3 million) and additional costs for services amounting to around € 3.0 million;
- A rise in capitalized costs by around € 4 million, attributable to the Parent Company.

The **EBITDA** (gross operating margin) came to € 722.2 million, disclosing an increase of € 71.4 million when compared to the € 650.8 million in 2004 (+ 11%). The Brazilian subsidiaries contributed € 128.2 million, compared to € 83.3 million in 2004.

EBIT (operating income) came to € 547.1 million and was up by € 52.6 million (+ 10.6%) when compared to € 494.5 million in 2004. The benefit of the growth in the EBITDA is reduced by the substantial increase (€ 18.8 million) in the item “amortization/depreciation” of which around € 13.9 million attributable to the parent company (€ 5.6 million for intangible fixed assets and € 8.3 million for tangible fixed assets essentially attributable to the acquisition of the TSO business segment from GRTN), and around € 4.5 relating to the Brazilian subsidiaries (€ 1.8 million for additional amortization/depreciation and € 2.7 million due to the exchange effect). The portion pertaining to RTL amounts to around € 0.4 million.

Net financial expense of € 82.0 million, including approximately € 50.0 million for the parent company, underwent a decrease of 17.9% (- € 17.9 million) and derives from:

- An increase in interest income and other revenues amounting to about € 28.6 million, essentially attributable to the parent company (+ € 25.7 million) due to the adjustment of the fair value on FVH hedging derivatives (+ € 25.1 million);
- An increase in interest expense and other charges of around € 42.3 million, of which € 16.9 million attributable to the parent company and € 25.4 million to the Brazilian companies (€ 3.9 million for TSN and € 21.5 million for Novatrans) due to the effects of the interest on medium and long-term loans (€ 29.5 million) which in 2005 had been present for the entire year, with particular reference to the bond issue and the Novatrans debt. There was also a decrease in the charges relating to trading derivatives by around € 7.8 million;
- An increase in exchange gains of approximately € 31.6 million (of which € 1.7 million realized). This increase comprises € 4.4 million attributable to the parent company, € 3.2 million attributable to TSN and € 24 million attributable to Novatrans and essentially concerns the appreciation of the Real against the Euro and the US dollar.

Income taxes for the year came to € 169.0 million, representing 36.2% of the pre-tax income.

Net income amounted to € 297.9 million (up by 28.9% when compared to the figure of € 231.1 million in 2004) after having provided for income taxes of € 169 million (€ 9 million referring to the Brazilian companies and € -7.2 million for net deferred taxes). Income taxes for the year represented 36.2% of the pre-tax income.

Balance sheet

The Terna Group's balance sheet for 2005 and 2004 is summarized below, obtained by reclassifying the balance sheet balances.

In millions of Euro	2005	2004	Change
NET FIXED ASSETS			
Tangible and intangible	4,952.5	4,440.3	512.2
Long-term financial assets	13.4	9.3	4.1
Total	4,965.9	4,449.6	516.3
NET WORKING CAPITAL			
Trade receivables	1,026.2	157.9	868.3
Inventories	21.2	19.6	1.6
Other assets	20.9	18.2	2.7
Net tax payables	16.9	7.2	9.7
Trade payables	975.0	183.6	791.4
Other liabilities	255.4	205.4	50.0
Total	-179.0	-200.5	21.5
Gross capital employed	4,786.9	4,249.1	537.8
Sundry provisions	616.0	597.5	18.5
Net capital employed	4,170.9	3,651.6	519.3
Shareholders' equity	1,902.2	1,759.1	143.1
Net financial debt	2,268.7	1,892.5	376.2
Total	4,170.9	3,651.6	519.3

Net financial debt is analysed as follows:

In millions of Euro	2005	2004	Change
Bond issue	1,498.40	1,434.70	63.7
EIB loans	400	318.2	81.8
BNDES/IDS loans	468.9	378.9	90
Short-term loans	55	0	55
Bank balances and cash	-76.6	-231.8	155.2
Derivative financial instruments in portfolio	-77	-7.5	-69.5
Total financial debt	2,268.70	1,892.50	376.2

Net tangible and intangible fixed assets amounting to € 4,965.9 million, rose by € 512.2 million, of which:

- around € 189.2 million for intangible fixed assets attributable to the value of the concession totalling € 134.5 million, net of the amortization set aside in the income statement, which came about as the difference between the equity acquired and the price paid for the business segment; around € 16.5 million for costs incurred for the development of the applications software developed internally or acquired as part of the creation of programmes for the development and evolution of the systems; around € 37.2 million due to the adjustment of the value to the period end exchange rate relating to the valuation of the goodwill; the difference concerns other intangible investments in progress;
- around € 323.0 million for tangible fixed assets, including approximately € 80.3 million relating to the algebraic effect between investments, depreciation and disposals during the year; € 146.1 million due to the appreciation of the R\$/Euro exchange rate which as of December 31, 2004 fell from 3.61 to 2.74 R\$ per Euro as of December 31, 2005; around € 70 million for the fixed assets of the former GRTN business segment and € 26.6 million due to changes in the scope of consolidation (RTL).

Long-term financial assets rose by € 4.1 million, essentially attributable to the parent company with particular reference to the equity investment of the associated company Cesi SpA from the TSO business segment acquired from GRTN. Following this acquisition, the ownership percentage in CESI reached 24.4% and it was therefore classified among Equity investments in associated companies.

The **net working capital** amounted to € -179.0 million and disclosed a decrease on 2004 of € 21.5 million. Shareholders are informed that the considerable increase in the items Trade receivables and Trade payables is attributable to the new dispatch activities; these are of a transitory nature, but determine considerable volumes of financial transactions.

The **increase in provisions** by around € 18.5 million, is nearly entirely attributable to the parent company and mainly reflects the increase in the employee termination indemnity provision (€ 15 million) being the consequence of the staff included in the TSO business segment.

The **net invested capital** therefore amounted to € 4,170.9 million, disclosing an increase of € 519.3 million which as already mentioned essentially reflects the net tangible and intangible fixed assets.

Investments in tangible fixed assets

The breakdown of investments made in 2005 by plant type is presented as follows:

In millions of Euro	2005	2004
Power lines	121.3	154.1
Transformer stations	121.7	110.9
Leasehold improvements and other	18.9	12.8
Brazil	9.4	25.4
Total	271.3	303.2

Plant and equipment

The Group's plant is illustrated in the table below:

	TERNA		TSN		NOVATRANS		RTL	
	N°	Km	N°	Km	N°	Km	N°	Km
Stations	302		5					
Transformers	572		14					
Bays	3,947		29		10			
Lines		35,129		1,077		1,278		539
Double circuit lines	1,953	38,976	12	1,077	5	1,278	35	700

The main changes during 2005 resulted from:

For TERNA

In relation to the number of stations, the two new 150 kV stations at Celle S. Vito and Ulassai came onto stream.

With regards to the number of transformers, there was a total increase of 3 units due to the following changes:

- The installation of a new 220 / 132 kV 160 MVA auto-transformer at the Biella East station;
- The installation of a new 380 / 132 kV 250 MVA auto-transformer at the Rondissone station;
- The installation of a new 380 / 150 kV 250 MVA auto-transformer at the Rome east station;
- The installation of a new 380 / 150 kV 250 MVA auto-transformer at the Taranto North station;
- The demolition of a 220 / 150 / 15 kV 100 MVA auto-transformer at the Codrongianos station.

Overall, the total transformation capacity rose from 108,749 MVA at the end of 2004 to 109,968 MVA, involving a total increase of 1,559 MVA.

As far as power lines were concerned, an increase was seen in the overall length of the double-circuit lines by around 280 km when compared to December 31, 2004. This increase was mainly due to the bringing onto stream of the following new connections:

- 380 kV double - circuit power line (around 42 km) for interconnection with Switzerland (S. Fiorano - Robbia);
- 150 kV Taloro 3 - Taloro 2 and Taloro 2 - Taloro 1 lines (for an approximate total of 14 km);
- 380 kV Altomonte - Feroletto line (approximately 105 km);
- 380 kV Feroletto - Rizziconi line (approximately 67 km);
- 150 kV Celle S. Vito – Montefalcone line (approximately 21 km);
- 380 kV SET - S. Maria Capua Vetere line (approximately 3 km).

The plant and equipment of the Brazilian companies remained unchanged, while there was an increase for RTL in the total length of the double-circuit lines by around 1 km when compared to December 31, 2004.

The increase was mainly due to the following connections:

- The doubling of the 150 kV Collarmele ACEA sec. LS - S. Angelo power line into two stretches named Collarmele ACEA sec. LS - Brulli Cucullo and Brulli Cucullo - S. Angelo, involving an increase of 0.72 km of power line and 1.40 km of double-circuit line;
- The partial burying of the 150 kV Flaminia Nomentana power line involving a reduction of around 0.38 km of power line and double-circuit line.

Financial flows

Net financial debt (€ 2,268.7 million) as of December 31, 2005 and the related maturities are as follows:

In millions of Euro	Dec. 31, 2005	Dec. 31, 2004	Change
A) MEDIUM/LONG-TERM DEBT			
Bond issue	1,498.4	1,434.7	63.7
EIB loans	370.5	300.0	70.5
Brazil loans	440.2	350.1	90.1
Financial derivative instruments	-77.0	-7.5	-69.5
Total	2,232.1	2,077.3	154.8
B) SHORT-TERM DEBT (LIQUIDITY)			
EIB loans	29.5	18.2	11.3
Brazil loans	28.7	28.8	-0.1
Other loans. Italy	55.0	0.0	55.0
Net position with banks and liquidity - Italy	-15.8	0.0	-15.8
Net position with banks and liquidity - Brazil	-60.8	-87.9	27.1
Net cash position with intercompany current account	0.0	-143.9	143.9
Total	36.6	-184.8	221.4
TOTAL A + B	2,268.7	1,892.5	376.2

Economic results by geographic area and sector of activities

The breakdown of the essential highlights of the Group's results for the activities in Italy and in Brazil and by sector of activities, are analysed in a specific section of the explanatory notes, to which reference should be made.

RESEARCH & DEVELOPMENT

As far as research and development activities which require specific professional skills were concerned, Terna essentially avails of the collaboration of CESI SpA in which it holds a 25% equity investment; during 2005, collaboration was also started up with the University of Bologna.

These activities are always aimed at improving the efficiency of the processes with particular reference to the realization and maintenance of the plants.

The projects of greatest interest developed during 2005 concerned:

- The extension and optimisation of the expert system supporting the power line and station maintenance and overhaul activities, entitled MBI, which besides being a technical database, supports the proposals and the handling of the maintenance operation plans;
- The search for new diagnostic methods for power line insulators and station equipment;
- The realization of a number of on-line transformer monitoring systems;
- The structural design of power line supports;
- The setting up of innovative solutions for reducing electromagnetic fields.

During the latter part of the year, activities were also continued, as launched in 2005 by GRTN and acquired within the TSO business segment, relating to the dispatch activities (which mainly involved CESI SpA, the University of Pisa and qualified consulting firms).

These activities can be summarized as follows:

- Restarting Plan: simulations under dynamic conditions;
- Review of load Lighting Plan;
- Prototype of new Automatic load Disconnection system (EDA);
- Implementation of new models of continual current connections for the grid simulator;
- New grid monitoring system for the detection and study of grid transients;
- Voltage Regulation System design;
- Realization of Operator Training System.

The related costs incurred by the Terna Group during the year, nearly all of which attributable to the parent company, for the collaboration with CESI amounted to around € 3.4 million (of which € 1.6 capitalized).

The following activities are planned for 2006:

- Application and experimentation in the field of on-line diagnostic systems for power line insulators;
- Analysis and experimentation in the field of innovative solutions for reducing electromagnetic fields;
- Further extension with implementation of new functions for the MBI maintenance management system;
- The setting up of additional diagnostic techniques and experiments in the field.

During 2006, in relation to the Dispatching sector, the activities already launched in 2005 will be developed, possibly integrated by further initiatives necessary for the completion of the Defence Plan and the improvement of the simulation instruments.

Innovation

Other activities more fully directed towards practical application for optimising and improving the efficiency of the processes, carried out mainly by means of internal work groups, include:

- Field experimentation and standardization of new work methods under live conditions for power lines: replacement of protection cables, also with fibre optics, and insulator cleaning;
- Experimentation and introduction of work methods under live conditions at electricity stations;
- Experimentation and introduction of work on power lines using helicopters;
- Installation and setting up of innovative systems for the on-line detection of the temperature of conductors aimed at the best use of the same;
- Executive design and supply of materials for the realization of an experimental section of line with conductors featuring a greater transport capacity;
- The search for innovative methods for underground HV cable diagnostics;
- Experimentation on an operative power line of detection methods using helicopter-borne laser systems for monitoring power lines;
- The search for new plant engineering solutions for the construction of electricity stations;
- The search for and set up of HV compact equipment systems;
- The set-up of new criteria for the control of power lines and stations, with the introduction of newly conceived methods, and optimisation of the review criteria for the main station electrical equipment for improving the operating efficiency.

New system

During 2005, significant measures were carried out within the sphere of the computerized information systems so as to deal with three main requirements:

- Integration between the GRTN business segment (TSO) acquired and Terna;
- Support for the core processes and system safety;
- Support for the operating processes of the company.

Integration between the GRTN business segment (TSO) acquired and Terna

In order to reduce the operative impact of the integration and guarantee the running efficiency, various projects were realized, the most important being:

- Standardization of the administrative and management processes by means of the adoption and the extension of the SAP system, used for some time now within Terna, to TSO as well.
- Integration of the settlement systems for TSO energy with the SAP system for the purpose of the integrated and uniform handling of the economic items relating to the energy within the administrative processes.
- Creation of a new institutional internet site which integrates the information contents of the integrated parties.

Support for the core processes and system safety

As far as the core processes are concerned, significant measures have been carried out for improving the efficiency, safety and efficacy of the operating processes:

Dispatching and Running

- Start up of the System for the Control and the Remote Integrated Running of the electricity grid (SCTI) for the Dispatching process, with benefits for the safety of the grid and the integration of the processes;
- The technical/operating improvement of the computerized information systems supporting the market processes with particular regard to the processes/systems for the planning of the requirement and the assessment of the safety (Forecast), the dispatch of the services for the tertiary regulation of the energy (command system), the settlement of the energy items (settlement, metering, Eneforbil);

- The structural enhancement of the basic technological infrastructure by means of the realization of specific superabundance on the systems and the business continuity logic telecommunications and the continuation of the disaster recovery projects whose completion is anticipated during 2006.

Plant maintenance

- Improvement of the system (Equipment management) for the classification of the equipment by Operating Groups, collation of references and norms for the management, scheduling of the maintenance measures (legal, anticipated by the manufacturers, envisaged by Terna);
- Integration of the geo-referencing system of the National Electricity Grid (GIS) with SAP for all the operating activities and with the database of the Ministry for the Environment for national mapping. This solution introduced during 2005 will be optimised by means of new functions during 2006.

Grid design

- Completion of the Advanced Station Design System (SDSA) integrated by means of activities for estimating and acquiring external resources with the libraries of the design models of the three voltage levels 380 - 220 - 150kV; this creation will be operatively introduced during the first few months of 2006.

Support for the operating processes of the company

During the year, projects were realized with the purpose of improving the company's control capacity over technical/economic aspects and the efficiency of the purchases, specifically:

- An advanced system was created for supporting the process for the purveying of external resources integrated with SAP and with SDSA systems. The new system was used on three pilot projects during 2005 with a positive outcome and will therefore be extended as from the first few months of 2006;
- The system for the estimation and analysis of the final balances of the plant maintenance and overhaul activities was improved, involving integrations with SAP, MBI, and the Service Quality Observatory.
- The System for the Analysis and Reporting of the Maintenance Budget was developed.
- The new Planning System was launched for the management of the corporate budget structured on all the Business units on a consistent basis with the analysis and reporting system of the Maintenance Budget.
- The system for the management and monitoring of the control activities on supplies (MOQ) was created, which includes the scheduling, activity balance, non-compliance handling, preventive action and corrective action phases.

HUMAN RESOURCES

New organizational structure

The exit from the Enel Group and the integration with the business segment acquired from GRTN, determined the need to carry out organization, operational and managerial changes aimed at ensuring the autonomy and full operational functioning of the Company, continuing to guarantee the efficiency, safety and reliability of the national electricity system.

On a consistent basis with this outlook, during the initial integration stage Terna adopted a structure characterized by:

- The maintenance of the organizational set up of the GRTN business segment converged within the sphere of an organizational unit (Dispatching Division) set up for this purpose under the Chief Executive Officer;
- The functional dependence of the staff functions of the Dispatching Division on the company staff functions.

On a parallel, so as to seize the synergies deriving from the integration within Terna of the activities of the GRTN, the work groups launched during the previous year continued with the activities for:

- Defining the functioning formalities of the processes, both core and support, with a view to full functioning of said processes;
- Definition of the integration logics and the subsequent rationalization of the organization.

On December 21, 2005, the Board of Directors resolved the new basic organizational structure of the Company, which envisages:

- The establishment of the Italy Operation Division, which is entrusted with responsibility for co-ordinating the activities relating to the planning and development of the grid, dispatching, running and maintenance of the plant;
- The enhancement of the staff functions;
- The focusing of a Division and the business development and international activities.

Headcount

The following table shows a breakdown of the workforce by category.

BREAKDOWN OF THE WORKFORCE

	ITALY		BRAZIL		TOTAL		Change
	Dec.31,'05	Dec.31,'04	Dec.31,'05	Dec.31,'04	Dec.31,'05	Dec.31,'04	
Senior management	75	34			75	34	41
Middle management	403	221			403	221	182
Office staff	1,813	1,467	53	58	1,866	1,525	341
Workers	1,098	1,149			1,098	1,149	-51
Total	3,389	2,871	53	58	3,442	2,929	513

The figures for both years are net of leavers as of December 31 (amounting to 25 as of December 31, 2004 and 227 as of December 31, 2003).

The increase in the headcount is due to the inclusion, on October 1, 2005, of 34 individuals (5 middle management, 19 office staff, 10 workers) due to the acquisition of ACEA Trasmissione and the inclusion, as of November 1, 2005, of 586 individuals (36 senior management, 179 middle management, 371 office staff) of the TSO business segment acquired from GRTN. Terna's headcount as of December 31, 2005 net of these inclusions (and related evolution) would have come to 2,782 units, involving a reduction of 89 units when compared to December 31, 2004. The company RTL has just one executive on its workforce.

With regards to the **training and development of resources**, during 2005 efforts were concentrated on the objective of consolidating and increasing the wealth of distinctive skills within the sphere of the core business, by means of intense and targeted specialist training activities addressing line workers, in particular on the contents concerning technological innovations and work methods.

On a parallel, specialist training activities were increased for staff workers, so as to support the requirements for increasing the skills required by the changes underway.

The commitment was also considerable for the training of newly employed workers according to a plan

which developed their organizational abilities (team working, communication, working by objectives, etc.), their business orientation (basic economics), and the technical-professional know-how inherent to the business context in which Terna operates.

As far as managerial training was concerned, alongside a programme for the development of “people management” skills, aimed specifically at line middle management, a plan of personalized initiatives has been launched (managerial development programmes selected from Italian and European Business School prospectuses).

During 2005, 2,878 resources participated in at least one training course (including the post-integration phase with GRTN).

Furthermore, during the first six months of 2005, within the sphere of the initiatives supporting the Terna-TSO business segment integration process, joint training activities on the subject of the Corporate Governance of listed companies were achieved and saw the participation of management and specialists from the two companies.

Again within the sphere of the activities supporting the Terna-TSO business segment integration process, on the subject of **internal communication** a comparative survey was carried out at the start of 2005 into the organizational culture of the two companies, involving all the staff with the aim of furthering maximum participation in the changeover process and identifying spheres of action in order to support the imminent integration process.

The process for the re-definition of policies and action plans (on the subject of professional system, development, education and training, compensation, etc.), on a consistent basis with the changed context, was launched starting off from the activities for the evaluation of the intellectual capital and risk management activities, which also included the preliminary mapping of the distinctive expertise of the company.

Long-term incentive systems

With regards to the managerial incentive systems, alongside confirmation of the extension of the MBO to all middle management, on May 9, 2005 the Board of Directors voted for the adoption of the first stock option plan intended for Terna Spa executives and/or those of its subsidiaries pursuant to Article 2359 of the Italian Civil Code, who cover the most significant functions for the purposes of the achievement of the Company's strategic results.

On December 21, 2005, with reference to the proposals presented by the Remuneration Committee, the Board of Directors also voted for the adoption of the stock option plan for 2006, intended for executives of the Terna Group who cover the most significant functions for the purposes of the achievement of the Group's strategic results. The beneficiaries also include the Chief Executive Officer, since he is an executive of the company.

With regards to the executives not involved in this plan, the implementation of a long-term incentive plan (LTI) was decided, linked to the achievement of challenging long-term objectives, whose specific content matter (objectives, parameters and result/bonus correlation curves) were established during the first few months of 2006.

TRANSACTIONS WITH RELATED PARTIES

With regard to the Terna Group's transactions during the 2005 accounting period, they are represented by transactions with the associated company CESI SpA.

The transactions carried out with the latter mainly concern the provision of services, forming part of the ordinary operations and regulated on an arms'-length basis, in other words at conditions which would be applied between two independent parties.

Lastly, shareholders are reminded that within the sphere of the corporate governance regulations which the Terna Group has adopted and which are detailed in the specific section of the statutory Report on Operations, to which reference should be made, the conditions have been anticipated for ensuring that the transactions with related parties are carried out in observance of the criteria of procedural and substantive correctness.

Transactions with related parties are indicated in the explanatory notes within the commentary to the individual balance sheet items and summarized in the specific section "Transactions with related parties" to which reference should be made.

OUTLOOK FOR 2006 AND OTHER INFORMATION

During the next accounting period the matters anticipated by the Prime Minister's Decree dated May 11, 2004 will continue to be implemented, specifically in relation to the unification of the National Transmission Grid by means of the acquisition of the portions of NTG owned by other operators.

Particular attention will also be paid to the development of the projects which will permit us to seize cost synergies downstream from the integration of the TSO business segment.

Consolidation will also follow of the Company's expertise relating to the development and maintenance of the National Transmission Grid and the Dispatching activities.

The Company will continue to scout, in search of investment opportunities abroad, with particular attention paid to profitability and the limited risk profile.

Such action, which the Company intends to pursue, aims to guarantee and increase the creation of value for the shareholder.

Brazil

During 2006, Terna will continue with the stockmarket listing of the Brazilian subsidiaries with the aim of fully expressing the value of the same, permitting access to the local capital market, extending the future growth possibilities in the country and at the same time reducing the direct exposure to risk of Terna SpA.

Human Resources

During the following accounting period, steps will be taken to complete the intervention programmes on organization, the processes and the systems within the sphere of the Terna - TSO business segment integration process.

Furthermore, the new integrated Resource Management and Development system based on the professional system (divided up into areas, families, tasks) and on the skills model, overhauled in light of the new set-up and the new corporate strategic objectives, will be completed with regards to its layout and then implemented. The focus will be on the maximum valorisation of the Company's Human Capital, with reference to the "distinctive" core business "expertise" and the managerial excellence for the "creation of value".

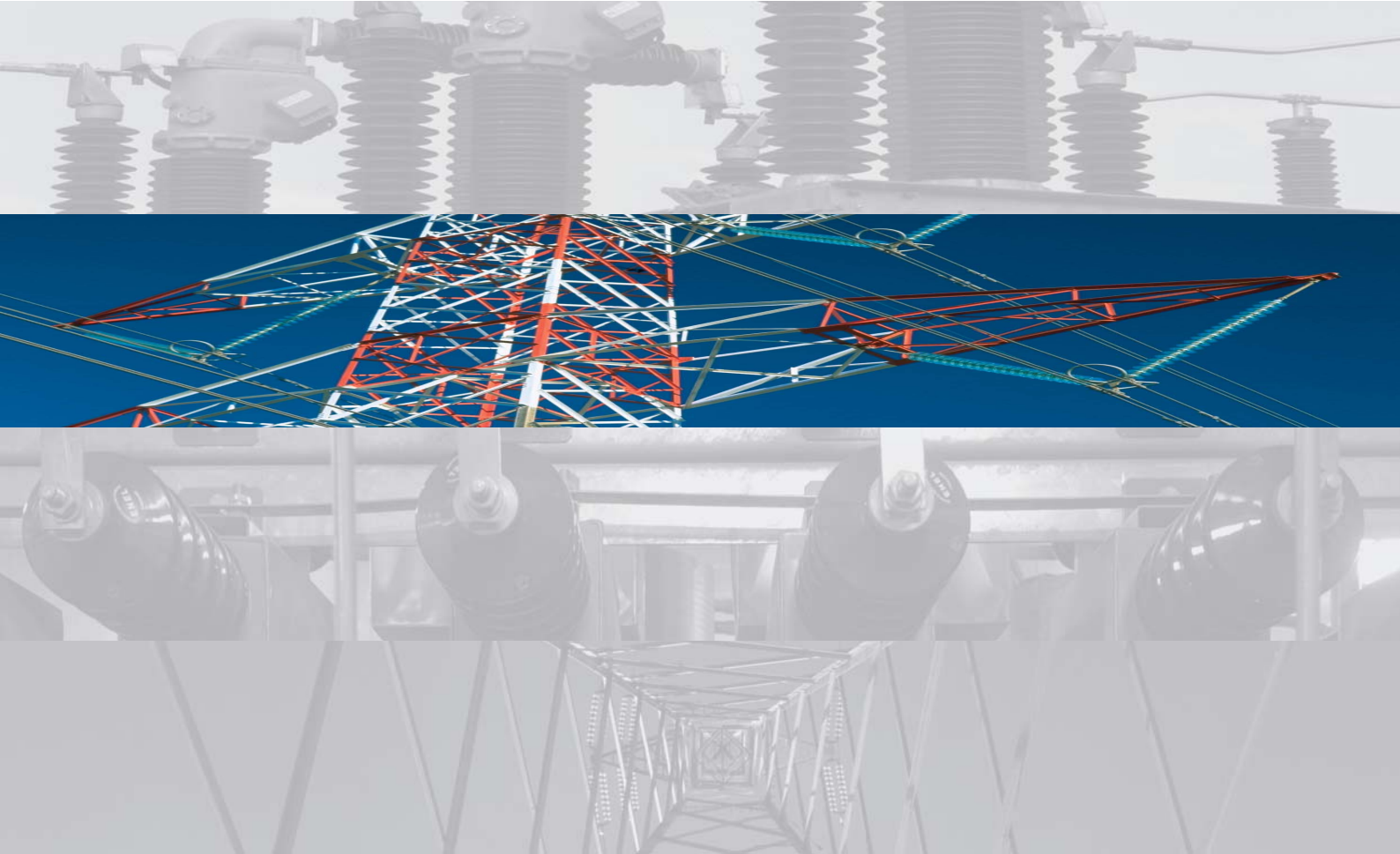
OTHER INFORMATION

Code concerning the protection of personal data (Italian Legislative Decree No. 196 dated June 30, 2003)

During 2003, Terna Spa drew up the Programmatic Security Document in accordance with Italian Presidential Decree No. 318/1999. The document will be updated in compliance with Italian Legislative Decree No. 196 dated June 30, 2003 by the legal deadline anticipated as March 31, 2006.

Own shares

The Company does not hold any own shares or shares in Parent Companies, nor has it acquired or sold any such shares during the accounting period, indirectly or otherwise.



CONSOLIDATED ACCOUNTING SCHEDULES

CONSOLIDATED INCOME STATEMENT

CONSOLIDATED INCOME STATEMENT TERNA GROUP

In millions of Euro	Notes	2005	2004	Change
A) REVENUES				
1) Revenues from sales and services	1	1.023,8	993,9	29,9
2) Other revenues	2	63,6	26,1	37,5
Total revenues		1.087,4	1.020,0	67,4
B) OPERATING COSTS				
1) Raw materials and consumables used	3	25,4	20,1	5,3
2) Services	4	118,8	129,8	-11,0
3) Personnel costs	5	201,7	178,2	23,5
4) Amortisation, depreciation and write downs	6	175,2	157,0	18,2
5) Other operating costs	7	45,7	62,9	-17,2
6) Capitalised costs	8	-26,5	-22,5	-4,0
Total operating costs		540,3	525,5	14,8
A-B OPERATING INCOME		547,1	494,5	52,6
C) FINANCIAL INCOME/(CHARGES)				
1) Financial income/(charges)	9	-82,0	-99,9	17,9
2) Income/(Charges) arising from the valuation of investments using the equity method	10	1,8	0,0	1,8
D) INCOME BEFORE TAXES		466,9	394,6	72,3
E) Taxes for the year	11	169,0	163,5	5,5
F) EARNINGS (LOSSES) FOR THE YEAR		297,9	231,1	66,8
Earnings per share	12	0,149	0,116	0,033
Diluted earning per share	12	0,148	0,116	0,032

CONSOLIDATED BALANCE SHEET

CONSOLIDATED BALANCE SHEET-ASSETS TERNA-GROUP

In millions of Euro	Notes	as at 31.12.2005	as at 31.12.2004	Changes for the period
A) NON-CURRENT ASSETS				
1) Buildings, plants and machinery	13	4.646,3	4.323,3	323,0
2) Goodwill	14	154,7	117,0	37,7
3) Intangible assets	15	151,5	0,0	151,5
4) Prepaid tax assets	16	57,3	51,6	5,7
5) Investments accounted for using the equity method	17	6,4	0,0	6,4
6) Non-current financial assets	18	106,1	41,9	64,2
7) Other non-current assets	21	7,0	6,4	0,6
Total non-current assets		5.129,3	4.540,2	589,1
B) CURRENT ASSETS				
1) Inventories	19	21,2	19,6	1,6
2) Trade receivables	20	1.026,2	157,9	868,3
3) Financial current assets	18	4,4	4,6	-0,2
4) Cash and cash equivalents	22	76,6	231,8	-155,2
5) Other current assets	21	32,9	34,8	-1,9
Total current assets		1.161,3	448,7	712,6
TOTALE ASSETS		6.290,6	4.988,9	1.301,7

CONSOLIDATED BALANCE SHEET CHANGES LIABILITIES AND SHAREHOLDERS' EQUITY

In millions of Euro	Notes	as at 31.12.2005	as at 31.12.2004	Changes for the period
C) GROUP SHAREHOLDERS' EQUITY				
1) Share Capital		440,0	440,0	0,0
2) Other reserves		811,1	1.224,2	-413,1
3) Retained earnings (losses) carried forward		453,2	-46,2	499,4
4) Interim dividend		-100,0	-90,0	-10,0
5) Income for the year		297,9	231,1	66,8
Total Group Shareholders' equity	23	1.902,2	1.759,1	143,1
D) EQUITY ATTRIBUTABLE TO MINORITY INTERESTS		0,0	0,0	0,0
Total D)		1.902,2	1.759,1	143,1
E) NON-CURRENT LIABILITIES				
1) Long-term loans	24	2.309,1	2.084,9	224,2
2) Employee termination indemnity and other provisions for personnel costs	25	168,2	138,3	29,9
3) Provision for risks and charges	26	37,4	40,8	-3,4
4) Deferred tax liabilities	27	467,7	470,0	-2,3
5) Non-current financial liabilities	24	29,0	31,5	-2,5
6) Other non-current liabilities	28	176,2	158,2	18,0
Total non-current liabilities		3.187,6	2.923,7	263,9
F) CURRENT LIABILITIES				
1) Short term loans	24	55,0	0,0	55,0
2) Current shares of long-term loans	24	58,3	47,0	11,3
3) Trade payables	29	951,4	183,6	767,8
4) Income tax payables	29	14,4	12,1	2,3
5) Current financial liabilities	24	16,8	12,9	3,9
6) Other current liabilities	29	104,9	50,5	54,4
Total current liabilities		1.200,8	306,1	894,7
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		6.290,6	4.988,9	1.301,7

STATEMENT OF CHANGES IN CONSOLIDATED SHAREHOLDERS' EQUITY

JANUARY 1, 2004 - DECEMBER 31, 2004

	GROUP SHARE OF CAPITAL AND RESERVES						Group shareholders' equity	Minority interests	Total	
	Share capital	Legal reserve	Foreign currency conversion effects		Retained earnings	Other reserves				Net income for the period
			GOODWILL	OTHER						
Balance as of Jan. 1, 2004	2,036.1	78.3			-40.8	631.3	220.4	2,925.3	0.2	2,925.5
Allocation of 2003 net income:										
a) To legal reserve		6.2					-6.2			
a) To other reserves (acc. depreciation)						36.9	-36.9			
a) To retained earnings					0.2		-0.2			
a) To dividends							-80.2	-80.2		-80.2
Allocation to other reserves						96.9	-96.9			
Conversion of foreign company financial statements			1.5	-13.2				-11.7		-11.7
Share capital reduction	-1,596.1					396.1		-1,200.0		-1,200.0
Other changes					6.1	-21.5 ¹		-15.4	-0.2	-15.6
Net income for the period							231.1	231.1		231.1
Dividend advance							-90.0	-90.0		-90.0
AS OF DEC. 31, 2004	440.0	84.5	1.5	-13.2	-34.5	1,139.7 ²	141.1	1,759.1	0.0	1,759.1

¹ Of which € 2.4 million relating to the 2004 portion concerning the incentive obtained from the Brazilian Ministry of National Integration by the subsidiary TSN and € -5.5 million for the adjustment to the fair value of the derivative cash flow hedge instruments, net of the related tax effect (€ 2.7 million);

² In addition to € 2.4 million for the Brazilian tax incentive as per Note 1, the balance includes € -12.6 million corresponding to the fair value of the derivative cash flow hedge instruments, net of the related tax effect (€ 6.2 million).

DECEMBER 31, 2004 - DECEMBER 31, 2005

	GROUP SHARES OF CAPITAL AND RESERVES						Net income for the period	Group shareholders' equity	
	Share capital	Legal reserve	Foreign currency conversion effect	Retained earnings	Other reserves	Dividend advance			
									GOODWILL
As of Dec. 31, 2004	440.0	84.5	1,5	-13.2	-34.5	1,139.7	-90.0	231.1	1,759.1
Allocation of 2003 net income:									
a) To legal reserve		3.5			-2.4			-1.1	
a) To 2004 Dividend Advance							90.0	-90.0	
a) To 2004 Dividend balance								-140.0	-140.0
Conversion of foreign company financial statements									
			37.2	41.8					79.0
Share capital reduction									
Other changes					422.8	-416.6 ³			6.2
Net income for the period								297.9	297.9
2005 dividend advance							-100.0		-100.0
AS OF DEC. 31, 2005	440.0	88.0	38.7	28.6	385.9	723.1 ⁴	-100.0	297.9	1,902.2

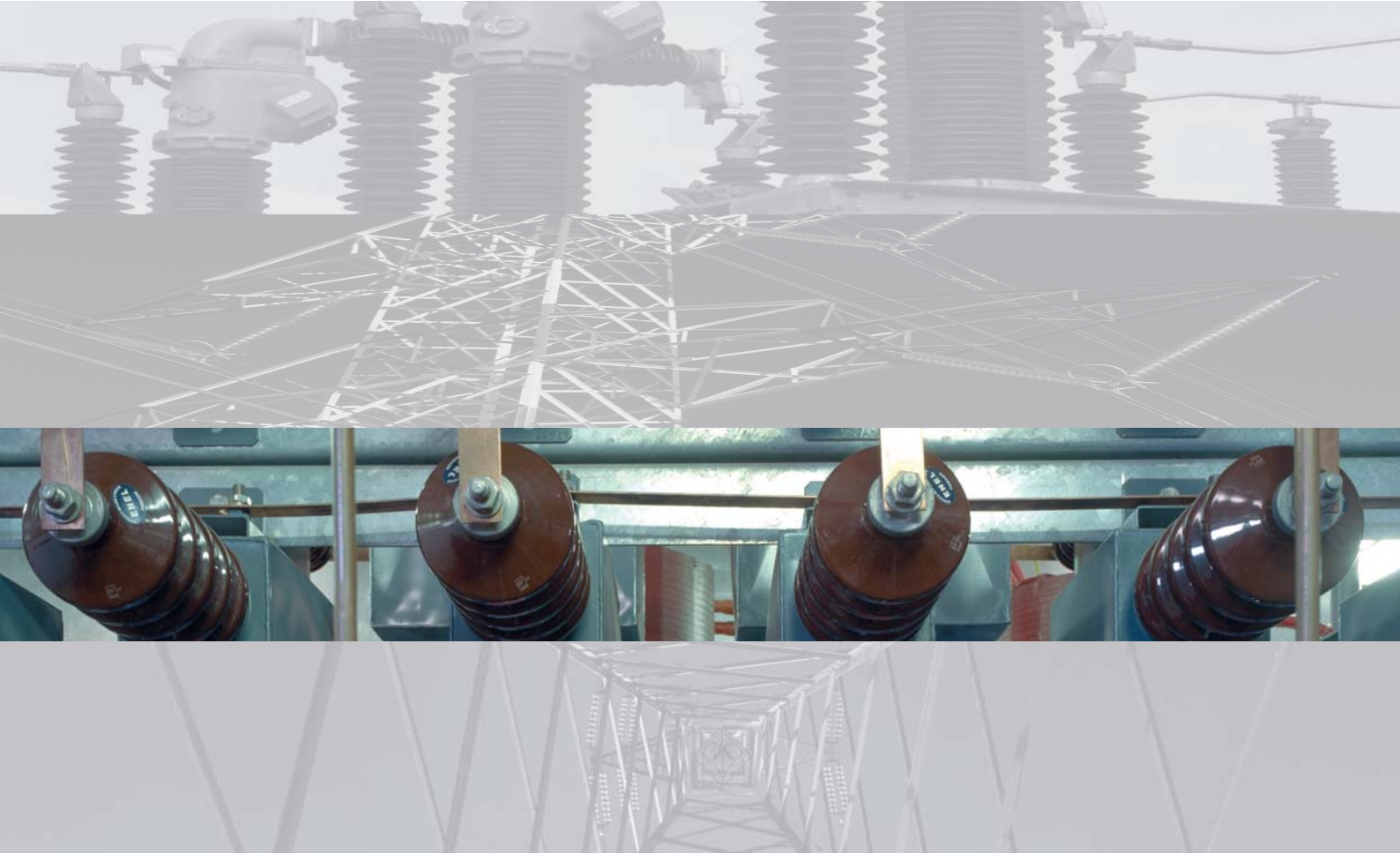
³ Of which € 3.8 million relating to the 2005 portion concerning the incentive obtained from the Brazilian Ministry of National Integration by the subsidiary TSN and € 0.7 for the adjustment to the fair value of the derivative cash flow hedge instruments, net of the related tax effect (€ -0.4 million).

⁴ Includes € 6.2 million for the Brazilian tax incentive as per Note 3 and € -11. million corresponding to the fair value of the derivative cash flow hedge instruments, net of the related tax effect (€ 5.9 million).

STATEMENT OF CONSOLIDATED CASH FLOWS

TERNA GROUP-CONSOLIDATED STATEMENT OF CASH FLOWS

	December 31, 2005	December 31, 2004
Group net income for the period	297.9	231.1
Adjustments for:		
Amortization, depreciation, losses in value/(revaluations) of non-current tangible assets	175.1	157.0
Exchange adjustment effects on foreign currency assets and liabilities (including cash and cash equivalents)	-7.6	12.1
Operating grants credited to the income statement for the period	-10.2	-15.3
Provisions to reserves (including staff fund)	32.8	23.9
Capital (gains) losses on disposals	2.6	5.7
Financial (income)/ expense (excluding exchange differences)	98.8	85.1
Income taxes	169.0	163.5
Cash flow from operations before changes in NWC	758.4	663.1
Decrease in reserves (including staff fund)	-25.1	-96.5
(Increase)/decrease in inventories	-1.6	-4.0
(Increase)/decrease in trade receivables and other current assets	-767.5	118.4
Increase/(decrease) in other non-current liabilities	14.5	107.3
Increase/(decrease) in other non-current assets	-55.0	-0.5
Increase/(decrease) in trade payables and other liabilities	664.8	-131.2
Interest income and other financial revenues collected	61.5	5.3
Interest expense and other financial charges paid	-146.9	-44.3
Taxes paid	-173.8	-85.5
TSO business segment acquisition	154.1	
Change in scope of consolidation	-6.3	
Cash flow from operations [a]	477.1	532.1
Increase in non-current tangible and intangible assets	-272.9	-279.2
Revenue from the sale of non-current tangible assets	1.8	4.4
TSO business segment acquisition and change in scope of consolidation	-225.5	
Change in scope of consolidation	-27.1	
Cash flow from investment activities [b]	-523.7	-274.8
Increase/(decrease) in share capital		-1.596.1
Changes in reserves	7.3	282.2
Changes in medium/long-term financial payables	45.7	1.077.0
Changes in short-term financial payables and term lines of credit (including current portion of medium/long-term loans)	66.3	40.2
Dividends paid	-240.0	-170.2
Cash flow from financing activities [c]	-120.7	-366.9
Exchange effect on cash and cash equivalents [d]	12.1	1.4
Price paid for TSO acquisition	68.3	
Price paid for RTL acquisition	32.8	
INCREASE /(DECREASE) IN CASH AND CASH EQUIVALENTS [A+B+C+D]	-155.2	-108.2
Cash and cash equivalents at the beginning of the period	231.8	340.0
Cash and cash equivalents at the end of the period	76.6	231.8



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

ACCOUNTING POLICIES

Accounting principles

Terna's ("the Company" or the "Parent Company") registered office is in Italy. The Company's Consolidated Financial Statements for the year ended December 31, 2005 include the Company and its subsidiaries (together referred to as "the Group") and the Group's interest in associated companies. The Consolidated Financial Statements were authorized for issue by the Directors on March 15, 2006.

Compliance with IAS/IFRS

Pursuant to EEC Regulation no. 1606/2002 issued by the European Parliament and Council on July 19, 2002, effective from the year 2005, companies listed on markets regulated by the European Union Member States must present their consolidated financial statements in compliance with the International Financial Reporting Standards (IFRS) and its interpretations issued by the International Accounting Standards Board and approved by the European Commission.

The Terna Group has adopted IFRS, as from the year 2005, with transition to the IFRS on January 1, 2004. The last Consolidated Financial Statements presented in accordance with the Italian accounting principles were those relating to the year ended December 31, 2004. The Consolidated Financial Statements have been prepared in compliance with the IFRS in force at the reporting date, including the IFRS recently issued by the International Accounting Standards Board (IASB), the International Accounting Standards (IAS) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and of the Standing Interpretations Committee (SIC), as adopted by the European Commission ("IFRS as adopted"). The note "Transition to the International Financial Reporting Standards (IFRS)" includes, in accordance with the provisions of IFRS 1, the schedules of transition to the IFRS at January 1, 2004 and at December 31, 2004 to ensure comparability with the first IFRS consolidated financial statements.

Basis of presentation

In accordance with the options provided by Legislative Decree 38/2005, the Parent Company Terna SpA opted not to use the IFRS in preparing its Financial Statements at December 31, 2005 which were instead prepared according to the Italian accounting principles. Reconciliation of shareholders' equity at December 31, 2004 and 2005 and of the relative net income of Terna SpA with the corresponding IFRS consolidated figures is illustrated in the annex "Schedules of reconciliation of shareholders' equity and net income of Terna

SpA and consolidated figures". The Consolidated Financial Statements consist of the Balance Sheet, the Income Statement, the Statement of Cash Flows, the schedule of changes in the shareholders' equity and the notes to the financial statements.

The Income Statement is classified on the basis of the nature of costs, while the Statement of Cash Flows is presented using the indirect method.

The Consolidated Financial Statements are presented in euro and all the values are expressed in millions of euro unless otherwise specified.

Concessions

Terna

The concession which the Ministry of Productive Activities assigned free of charge and with effect from November 1, 2005 to the Company for the performance of the activities of transmission and dispatching of electricity in Italy, has a twenty-five year validity and is renewable for a further twenty-five years. In accordance with Articles 18 and 19 of the Decree of the Ministry of Productive Activities of April 20, 2005 in the cases of forfeiture and revocation, and also upon expiry of the concession, the Ministry has the power to redeem the assets directly used in the activity of transmission and dispatching to which the concession refers and owned by the Concession Holder, with the exclusion of plants (lines and stations) which are part of the National Transmission Grid (NTG). In the event of redemption of the Concession Holder's assets, the Ministry shall pay the latter compensation which will be determined by agreement between the parties and based on the most appropriate valuation criteria, averaging the net worth of the redeemed assets and their profitability.

Brazil

Like Terna, the Brazilian companies have been assigned the concessions for use of the portion of the energy transmission grid of which they are owners free of charge. The concessions have a 30 year validity from the assignment date (year 2003) and upon expiry of the concessions the Brazilian companies are not obliged to return the plants (lines and stations) comprising the portion of the transmission grid under their ownership. Upon expiry of the concessions, the plant, the rights and the privileges used in the performance of the concessions must be transferred to the Federal Government subject to payment of compensation commensurate to the portion of the investments that has not yet been amortized referring to the returned assets and effected with the view to ensuring continuity of service.

Accordingly the assets that are directly used in the activities of transmission and dispatching, including the plant (lines and stations) comprising the portion of the Group-owned NTG are classified under property, plant and machinery and amortized throughout their useful life.

Use of estimates

The preparation of the Consolidated Financial Statements in conformity with the IFRS, requires management to make judgments, estimates and assumptions that affect the values of the reported assets and liabilities and the information relating to potential assets and liabilities at reporting date. The estimates and relative assumptions are based on historical experience and other factors considered appropriate to each case and have been adopted to estimate the book value of assets and liabilities which are not readily apparent from other sources. Actual results could differ from these estimates. The estimates are used to report the provisions for credit risks, for obsolete inventory, amortization and depreciation, asset impairments, employee benefits, taxes and other accruals and provisions. The estimates and the underlying assumptions are reviewed on an ongoing basis and the effects of each review are recognized in the period in which the estimate is revised, if the revision affects only that period. If the revision affects both current and future periods, the revision is recognized in the period in which it occurs and in future periods.

Subsidiaries

The consolidation area includes the Parent Company Terna SpA and the companies in which it has the power to govern, directly or indirectly, the financial and operative policies for the purposes of obtaining benefits from its activities. The Financial Statements of subsidiaries are consolidated from the date in which the control is acquired and until that control ceases.

The list of companies included in the consolidation area is provided below:

SUBSIDIARIES

	Registered office	Activity	Share capital	Currency	%
T.S.N. - Transmissora Sudeste Nordeste SA	Rio de Janeiro	Construction and maintenance of electricity transmission grids	250,000,000	R\$	100
Novatrans Energia SA	Rio de Janeiro	Construction and maintenance of electricity transmission grids	373,135,465	R\$	100
R.T.L. Rete Trasmissione Locale	Rome	Construction and maintenance of electricity transmission grids	20,600,000	Euro	100

The only change in the area of consolidation refers to the acquisition of RTL SpA by the Parent Company on October 1, 2005.

Associated Companies

Associated companies are those entities in which the Group has significant influence. They are initially recognized at cost and are subsequently accounted for under the equity method. The consolidated financial statements include the Group's share of the total recognized gains and losses of associates on an equity accounting basis, from the date in which the significant influence commences until the date in which it ceases.

When the Group's share of losses exceeds its interest in an associate, this is cancelled and any excess is recorded in a special provision, if the Group has legal or constructive obligations or made payments on behalf of an associate.

Method of consolidation

All the Financial Statements of the consolidated companies have been prepared at December 31, 2005 and adjusted, where necessary, to ensure uniformity with the accounting standards applied by the Parent Company.

In drawing up the Consolidated Financial Statements, inter-group balances, transactions, revenues and costs are eliminated on a line-by-line basis net of the relative tax effect, if significant.

Unrealized profits and losses made with the associated companies are eliminated to the extent of the Group's interest in the entity. In both cases, unrealized losses are eliminated, if there is no evidence of an impairment.

Translation of foreign currency balances

The Financial Statements of each consolidated company are drawn up in the functional currency used in the economic context in which the companies operate.

In such Financial Statements, all the transactions in currency other than the functional currency are recorded at the exchange rate in force at the transaction date. Monetary assets and liabilities denominated in currency other than the functional currency are subsequently adjusted to the exchange rate in force at balance-sheet

date and the exchange rate differences that may emerge are recognized in the income statement.

Non-monetary assets and liabilities denominated in foreign currency and stated at historical cost are converted using the exchange rate in force at the date of transaction. Non-monetary assets and liabilities denominated in foreign currency and stated at fair value are converted using the exchange rate in force at the date the fair value was determined.

Translation of financial statements denominated in foreign currency

For the purposes of the Consolidated Financial Statements, the profit/loss, assets and liabilities are expressed in euro, this being the functional currency of the Parent Company.

For the purposes of the preparation of the Consolidated Financial Statements, the individual Financial Statements denominated with functional currency other than the euro are converted into euro by applying the exchange rate in force at year-end date to assets and liabilities, including goodwill and adjustments made at the time of consolidation, and the average exchange rates of the period presented to the income statement items which approximate the exchange rates in force at the date of the respective transactions. The related exchange rate differences are directly recognized to the shareholders' equity and are reported separately in a specific equity reserve. This reserve is subsequently released to the income statement at the time of disposal of the investment.

Business Combinations

All business combinations are accounted for using the purchase method where the purchase cost is equal to the fair value at the date of the transactions of the assets acquired, net of the liabilities assumed, including costs directly attributable to the acquisition. This cost is allocated by recording the assets, liabilities and identifiable potential liabilities at the relative fair values. Any positive surplus of purchase cost compared to fair value of the portion of the acquired net assets pertaining to the Group is carried as goodwill or, if negative, taken to the income statement.

Upon first time adoption of the IFRS, the Group chose not to apply IFRS 3 (Business Combinations) retrospectively to the acquisitions effected prior to January 1, 2004. Hence the goodwill arising from the acquisitions made prior to the date of transition to the IFRS is stated at the value recorded in the last Consolidated Financial Statements presented on the basis of the previous accounting principles (December 31, 2003).

Property, plant and equipment

Property, plant and equipment are stated at historical cost, inclusive of accessory costs that are directly ascribable and necessary to starting up the asset for the use which it was purchased for. The cost is increased, in the presence of legal or constructive obligations, by the present value of the estimated cost for the dismantling or removal of the asset. The corresponding liability is recorded in a provision within the provisions for future risks and charges. The financial charges relating to loans associated with the purchase of the assets are recorded in the income statement in the year in which they are accrued. The costs incurred after purchase are recorded as a book increase in the item to which they refer, if it is probable that the future economic benefits arising from the cost incurred will flow to the Group and the cost of the item can be reliably measured. All other costs are recognized in the income statement as an expense as incurred.

Each component of a property, plant and machinery of significant value compared to the total value of the asset of which it is part, is recognized and depreciated separately.

Some assets which had been subject to revaluation as of January 1, 2004 (transition date) or in previous periods, are measured on the basis of the revalued value at the revaluation date considered as substitute cost (deemed cost).

Property, plant and machinery are reported net of the relative accumulated depreciation and of any impairments, determined according to the procedures described below. Depreciation is calculated on a straight-line basis over the estimated useful life of each part of property, plant and equipment, which is reviewed each year and any changes are recognized perspectively. Depreciation of assets under construction commences when the asset is available for use.

The main rates calculated on the basis of the useful life are the following:

DEPRECIATION RATES

Industrial and non-industrial buildings	2.50%	-	4.00%
Power lines	2.50%	-	4.50%
Transforming substations			
- <i>Electrical equipment</i>	2.00%	-	3.00%
- <i>Other electrical equipment</i>	2.80%	-	4.50%
- <i>Automation and control systems</i>	5.00%	-	6.70%
Central systems for management and control			
- <i>Electrical equipment and ancillary plant</i>			5.00%
- <i>Computers</i>			10.00%

Land, whether free from constructions or adjacent to industrial or non-industrial buildings, is not depreciated since it has an unlimited useful life.

Plant, property and equipment acquired under financial lease contracts, by which all the associated risks and benefits are transferred to the Group, are recognized as Group assets at their present value or, if lower, at the present value of the minimum payments due for leasing, including any sum to be paid for exercise of the purchase option. The corresponding liability due to the lessor is classified among the financial payable. The assets are depreciated by applying the above criteria and rates. In the event that there is no reasonable certainty that ownership will be acquired at the end of the lease, the assets are depreciated for the length of the lease or the useful life, if less.

Leases in which the lessor essentially maintains all the risks and benefits associated with ownership of the assets are classified as operating leases. The costs referring to operating leases are recorded on a straight-line basis in the income statement over the duration of the lease contract.

Intangible assets

Intangible assets, all having definite useful life, are stated at cost and recognized net of the relative accumulated amortization and impairment losses, determined according to the procedures described below.

Amortization is calculated on a straight-line basis over the estimated useful life, which is reviewed each year and any change is applied perspectively.

Amortization starts when the asset is available for use.

The estimated useful lives of the main intangible assets are specified in the notes.

Goodwill

Goodwill, arising from the acquisition of subsidiaries, is allocated to each of the cash generating units (hereinafter CGU) identified. After initial recognition, goodwill is not amortized and is reduced by any impairment losses, determined according to the procedures described below. Goodwill relating to equity investments is included in their book value. Negative goodwill arising on an acquisition is recognized directly in the income statement.

Impairments

Tangible and intangible assets with definite life are tested at least once a year for the purpose of identifying any impairments. If there is evidence of impairment, an estimate of their recoverable value is performed.

The recoverable value of goodwill and of intangible assets with indefinite useful life, where present, and that of intangible assets not yet ready for use is estimated on a yearly basis.

The recoverable value is represented by the greater of the net sales price and value in use.

In determining the value in use, the expected future financial flows are actualized using a discount rate gross of taxes which reflects the current market valuation of the cost of money in relation to the period of investment and the risks specific to the asset. For assets which do not generate fully independent financial flows, the recoverable value is determined in relation to the cash generating unit (hereinafter CGU) to which said assets pertains.

An impairment loss is recognized in the income statement when the asset, or the relative cash generating unit to which it is allocated, is carried at a value which is higher than its estimated recoverable value.

The impairments of the CGUs are firstly carried as reduction of the book value of any goodwill attributed thereto and then, as reduction of the other assets in proportion to the book value of each of these. With the exception of goodwill, impairments are reversed where there is evidence that the impairment no longer exists or when there is a change in the assumptions used to determine the recoverable value.

Inventories

Inventories are valued at the lower of cost and net estimated realizable value. The cost configuration used is the weighted average cost which includes pertinent additional charges.

Contract work in progress

Contracts are valued at cost increased by income recognized up to that time net of expected losses and invoices for work progress. The revenues and costs are respectively recorded as revenue and cost in relation to the state of progress of the contract work, where the outcome of a contract may be reliably estimated. The state of progress is determined on the basis of measurements of the work performed. An

expected loss on a contract is immediately carried as reduction of the contract. The contract costs include all the costs that refer directly to the specific contract and the fixed and variable costs incurred by the Group in its normal operating capacity.

Financial instruments

Equity investments in other companies

Equity investments held in other companies are classified as “available for sale” and are valued at fair value with any gains or losses charged directly against the shareholders’ equity. At the time of their disposal such cumulated gains and losses are released to the income statement.

Where the fair value cannot be reliably determined, equity investments in other companies are valued at cost adjusted by impairments, the effect of which is recognized in the income statement.

Said impairments are not reversed.

Financial assets

Financial assets (debt securities) which the company intends or is able to hold to maturity are recorded at the transaction date and initially stated at fair value, inclusive of any transactions costs. Thereafter they are valued at amortized cost, using the effective interest rate method, net of any impairments.

Trade receivables

Trade receivables are entered at amortized cost net of any impairments. Impairments are determined on the basis of the present value of the expected future cash flows, actualized on the basis of the original interest rate. Receivables with maturity within normal commercial terms are not actualized.

Cash and cash equivalents

Cash and cash equivalents include cash instruments, that is, those instruments which are available upon demand or at very short-term notice, favorable outcome and the absence of costs for their collection.

For the purposes of the consolidated Cash Flow Statements, cash and cash equivalents are shown net of bank overdrafts as at year end.

Trade payables

Trade payables are stated at amortized cost.

Financial liabilities

Financial liabilities, other than derivative financial instruments, are recorded on a “transaction date” basis and valued at fair value net of directly attributable transaction costs.

Thereafter, financial liabilities are valued at amortized cost, using the original effective interest rate method.

Derivative financial instruments

The Group holds derivative instruments for the purpose of hedging its exposure to the risk of interest rate variation. In compliance with the chosen strategy, the Group does not implement transactions on derivatives for speculative purposes. However, where transactions do not qualify as hedging transactions for accounting purposes, they are recorded as speculative transactions.

Derivatives are classified as hedging instruments when the relation between the derivative and the hedged instrument is formally documented and the effectiveness of the hedge, which is subject to regular verification is high. Where the hedging derivatives hedge the risk of fair value variation in the hedged instruments (fair value hedge; e.g. hedging of the variability of the fair value of fixed-rate assets/liabilities), they are reported at fair value with the effects booked to the income statement. The hedged instruments are appropriately adjusted to reflect the variation in the fair value associated with the hedged risk. Where the derivatives hedge the risk of variation in the cash flows of the hedged instruments (cash flow hedge; e.g. hedging of the variability in the cash flows of variable-rate assets/liabilities due to interest rate fluctuations), the variations in fair value are initially booked to shareholders' equity and subsequently charged to the income statement consistently with the economic effects produced by the hedged transaction.

Variations in the fair value of derivatives which do not qualify as hedging derivatives are recorded in the income statement.

The fair value is determined by using the official quotations for instruments traded on regulated markets. The fair value of instruments which are not traded on regulated markets is determined by actualizing the expected cash flows to the market interest-rate curve at the reference date and converting the values into currencies other than the euro at year-end exchange rates.

Employee benefits

The liability relating to the benefits recognized to employees and disbursed at the time of or after termination of the employment relationship and relating to defined benefit programs (employee termination indemnities, additional monthly salaries, indemnity in lieu of notice, energy discount, Asem health care and other benefits) or other long-term benefits (loyalty bonuses) for each plan, is recorded net of any assets serving the plan and is determined separately for each plan, on the basis of actuarial assumptions estimating the amount of future benefits accrued by employees at reporting date. The liability is recorded on an accrual basis throughout the period in which the right is accrued. The valuation of the liability is made by independent actuaries.

The actuarial gains and losses at January 1 ,2004, date of transition to the IFRS, were recorded in the balance sheet. If after said date, unrealized gains and losses emerge which exceed 10% of the greater of present value of the benefit obligation and fair value of the assets serving the plan, said difference shall be recorded in the income statement throughout the remaining average working life of the employees subscribing to the scheme. Where this is not the case, actuarial gains or losses shall not be recorded.

Stock option plans

The cost of services provided by employees and remunerated through stock option plans is determined on the basis of the fair value of options granted to employees at the grant date. The fair value of the options granted is recorded under personnel costs, over the vesting period, with corresponding increase of the shareholders' equity, taking into account the best possible estimate of the number of options that will become exercisable. The calculation method used to determine the fair value takes into account the characteristics of the options (duration of the option, price and conditions of exercise, etc.), as well as the price of the Terna share at the grant date, the share volatility and the interest-rate curve at the grant date consistent with the length of the plan. The amount recorded as cost is adjusted to reflect the actual number of stock options accruing, except where failure to achieve the conditions for acquisition of the right is solely due to market conditions.

¹⁾ Additional monthly salary

²⁾ Indemnity in lieu of notice

Provisions for risks and charges

Provisions for risks and charges are recorded when at reporting date there is a legal or implicit obligation, arising from a past event, for which a probable outlay of resources is required, and the amount involved in said outlay can be reliably estimated. If the effect is significant the allocations are determined by actualizing the expected future financial flows at a discount rate gross of tax which reflects the current market valuation of the cost of money in relation to the time and, where applicable, the specific risk applicable to the obligation. When the amount is actualized, the increase in the provision due to the passing of time is recorded as financial expense. If the liability relates to tangible assets, the provision is recorded in a balancing-entry to the asset to which it refers. The expense is recorded in the income statement through depreciation of the tangible asset to which it refers.

Grants

Grants, from both Government and private third parties, are stated at fair value where there is reasonable certainty that they will be received and that the conditions to their attainment will be met.

Grants received for specific expenditure are recorded among other liabilities and are systematically credited to the income statement over the same period in which the related costs accrue.

Grants received for specific assets whose value is recognized among fixed assets are recorded, for property, plant and equipments already in operation at December 31, 2002, among Other liabilities and credited to the income statement over the depreciation period of the related assets. As from the year 2003, for new property, plant and equipments starting operations, the relative grants are recorded as direct reduction of the fixed assets.

Capital grants are fully recorded in the income statement at the time conditions for recognition are met.

Revenues

Revenues are recorded on the basis of the specific criteria stated below, according to the nature of the transaction:

- Revenues from the sale of assets are recorded when the significant risks and benefits of ownership of the assets are transferred to the purchaser;
- Revenues for the provision of services are recorded with reference to the stage of completion of the activities.

Where it is not possible to reliably determine the value of the revenues, they are recorded up to the extent of the incurred costs that are deemed recoverable.

In particular, revenues arising from fees for remuneration of the National Transmission Grid (NTG) are stated according to the tariffs established by the Italian Authority for Electricity and Gas.

The considerations collected on behalf of third parties, such as the remuneration of the other non-Terna Group grid owners and the revenues recorded for the activities of managing the balance of the national electricity system which do not produce an increase in shareholders' equity, are reported net of the relative costs. A breakdown of this items, which reflects the substance of the transactions described, setting off the revenues with the relative costs deriving from the "same transaction", is in any case provided in a specific paragraph in the notes.

Financial income and expense

Financial income and expense is recorded on an accrual basis according to the interest accrued on the net carrying amount of the relative financial assets and liabilities using the effective interest rate method.

Dividends

Revenues are recorded when the shareholders' right to receive dividend is established. Dividends and interim dividends payable to third parties are reported as change in the shareholders' equity at the date in which they are approved, by the shareholders' meeting and by the board of directors respectively.

Income taxes

Current taxes are recorded under tax payables net of advances paid, and are determined on the basis of estimated taxable income and in compliance with tax regulations in force. Deferred tax assets and liabilities are calculated on temporary differences between the values recognized in the Consolidated Financial Statements and the corresponding values recognized for tax purposes, applying the tax rate in force or substantially in force or presumed to be in force at the time the differences are reversed.

Deferred tax assets are carried as receivables when their recovery is probable, that is, when taxable income sufficient to recover the asset is expected to be available in the future. The recoverability of deferred tax assets is reviewed at each year-end.

Risk Management

In performing its activity Terna is exposed to the risk of interest-rate fluctuation. The main source of interest-rate risk arises from the components of net borrowings which generate financial expense. The borrowing strategy is directed towards long-term debt instruments which reflect the useful life of corporate assets and the Group has implemented an interest-rate hedging policy aimed at adapting this approach to fit the regulatory context which establishes the reference cost of the debt within the formula adopted for establishing remuneration of the RAB in four yearly cycles.

Hence the hedging instruments used include, with differing maturities, both derivatives which bring the debt from fixed rate to variable rate (fair value hedge) and derivatives which bring the debt from variable rate to fixed rate (cash flow hedge and soft hedge).

With the intention of reducing total borrowings subject to interest-rate variation and reducing the cost of funding, plain vanilla derivative contracts, such as interest-rate swaps and interest-rate collars, have been used. At year end, taking into account the transactions in derivative instruments, the fixed-rate portion of total gross borrowings of Terna SpA is equal to 66.8% while the fixed-rate portion of net debt is equal to 67.4%. All the derivative contracts have notional value and maturity date which are lower or equal to those of the underlying financial liability, so that each variation in the fair value and/or expected cash flows of said contracts is balanced by a corresponding variation in the fair value and/or expected cash flows of the underlying position.

With regard to the equity investments held in Brazil, the main source of interest-rate risk arises from the indexation of the variable rate to a prime interest rate granted by the Banca BNDES. These borrowings have not been hedged given that the prime rate granted by the BNDES (TJLP) is characterized by low volatility and proves advantageous if compared with domestic short-term rates (CDI) and with similar rate parameters for borrowings of equivalent duration. The Brazilian companies have taken on loans denominated in dollars for which no type of exchange-rate hedging has been implemented in view of the

long-term burden involved and of the natural hedging represented by the mechanism of indexation of the revenues of the companies which presents considerable correlation with trends in the dollar/real exchange rates. As far as the risk associated with the management of liquidity is concerned, given the negative differential that normally exists between the lending rate and the borrowing rate, financial optimization activity has been directed at minimizing the position of liquidity insofar as corporate management requirements allow.

The notional and the fair values of the derivatives existing at December 31, 2005, grouped under current and non-current financial assets and liabilities, are stated in the notes to the Consolidated Balance Sheet.

NOTES TO THE CONSOLIDATED INCOME STATEMENT

REVENUES

1) REVENUES FROM SALES AND SERVICES - Euro 1,023.8 Million

The table below provides a breakdown of revenues for the period:

In millions of Euro	As at Dec.31,2005	As at Dec.31,2004	Change
NTG usage fees	957.8	929.1	28.7
Other energy revenues	6.9	0.0	6.9
Other sales and services	59.1	64.8	-5.7
Total	1,023.8	993.9	29.9

NTG usage fees

These are chiefly attributable (€ 786.8 million) to fees pertaining to the Parent Company for usage of the national transmission grid (NTG). They also include the further share of the CTR components (AEEG resolution no. 15/2005) recognized to Terna following acquisition of the TSO activities and referring to the two months of integration. The revenues generated by the Brazilian companies, equal to € 169.7 million, refer to the fixed local fees established in the concession for operation of power lines issued by the local energy Authority (ANEEL). Also included are the revenues of the subsidiary RTL SpA pertaining to the relative portion of the NTG (€ 1.3 million). The € 28.7 million increase is chiefly due to the following factors:

- Adjustment of the percentage ownership of the NTG and effect of the changes introduced to the time-bands (AEEG resolution no. 5/2004) from the month of April 2004 which strongly privileged the revenues pertaining to the first quarter of the previous year (€ -24.0 million in net revenues for the Parent Company compared to 2004);
- € 51.4 million increase in the revenues attributable to the Brazilian subsidiaries specifically arising from the full capacity operation of the line managed by the company Novatrans and by appreciation of the local currency;
- contribution of revenues from the subsidiary RTL SpA for its portion of NTG (€ 1.3 million).

Other energy revenues

These refer respectively to the consideration due to the Parent Company from operators for metering activities (MIS component) and to the consideration recognized for acquisition of the resources necessary to meet the costs incurred for the dispatching requirements (DIS component). Both relate to the two months of effective integration of the GRTN activities.

Other energy revenues also record a series of economic revenue and cost items pertaining exclusively to the Parent Company which arise from the electricity purchase and sales transactions which are implemented on a daily basis with the electricity market operators, within the scope of the transmission and dispatching functions taken over from GRTN further to acquisition of the TSO activities. These items refer to the two months in which integration has been effective and relate to activities of a “let-through” nature for the Group. They present a zero balance, due to set-off between the revenues and relative costs, while on the balance sheet the relative credit and debit balances are recorded. The table below provides a breakdown of the components of said transactions:

Euro	2005	2004	Change
Revenues within Exchange perimeter			
- Energy sales on DAEM, RTEM, MDS and other minor markets	106.5	0.0	106.5
- Imbalancing and other minor revenues	266.2	0.0	266.2
- MDS resources procurement	221.6	0.0	221.6
- Other items (Income, CBT)	11.7	0.0	11.7
Total revenues within Exchange perimeter	606.0	0.0	606.0
Revenues components of no.168/04 - 237/04 and others	117.9	0.0	117.9
Revenues CTR other owners and GRTN cip/6 quota	16.0	0.0	16.0
Total revenues outside Exchange perimeter	133.9	0.0	133.9
TOTAL LET - THROUGH ENERGY REVENUES	739.9	0.0	739.9
Energy purchases			
- On the DAEM and RTEM markets	64.0	0.0	64.0
- For provision of dispatching services	450.2	0.0	450.2
- For imbalancing	39.1	0.0	39.1
- On foreign market - imports	39.7	0.0	39.7
- Other items (Income, CBT, EMO)	13.0	0.0	13.0
Total costs within the Exchange perimeter	606.0	0.0	606.0
Purchase of electricity market-related services	117.9	0.0	117.9
Fees to pay to NTG owners, GRTN and others	16.0	0.0	16.0
Total services and fees	133.9	0.0	133.9
TOTAL LET-THROUGH ENERGY COSTS	739.9	0.0	739.9

Other sales and services

Revenues from other sales and services amount to € 59.1 million and relate to revenues generated by various specialist activities in the field of high and very high voltage which the Parent Company provides to third party customers. The above amount specifically shows revenues from Enel Distribuzione SpA (€20.5 million) generated by the contract for maintenance of high-voltage lines owned by the latter and

those invoiced to Enel.net SpA (€ 11.3 million) for the laying of fibre optics on Terna SpA plants and the operation, maintenance and development of the same. The item also includes revenues for maintenance of third party plants and specialized services in the field of high-voltage (€ 17.1 million), the change in “work in progress” pertaining to contracts and a series of minor services.

2) OTHER REVENUES - Euro 63.6 Million

Other revenues

Other revenues are chiefly contributed by the Parent Company and are broken down in the table below:

Euro	2005	2004	Change
Fees for high-voltage connections	10.2	15.3	-5.1
Other revenues	6.4	6.9	-0.5
Prior year gains	39.4	3.1	36.3
Recovery of previous years' excess tax	7.6	0.8	6.8
Total	63.6	26.1	37.5

These generally record rental income, insurance refunds for damage to plants and fees from third parties for connections to the National Transmission Grid. This year they also record income from GRTN for adjustments to network fees referring to previous years (€ 20.0 million) and income for the release of previous years' allocations to the risks provisions (€ 16.5 million). The recovery of excess taxes pertaining to the previous year arises from positive adjustments recorded at the time of submission of the tax return.

OPERATING COSTS

3) RAW MATERIALS AND CONSUMABLES USED - Euro 25.4 Million

Euro	2005	2004	Change
Procurement of stock	10.7	11.8	-1.1
Supply of materials and equipment	9.6	7.0	2.6
Other supplies	2.0	3.0	-1.0
Change in inventories	3.1	-1.7	4.8
Total	25.4	20.1	5.3

This item includes the costs incurred for the purchase of various materials and equipment used in routine operation and maintenance of plants and chiefly attributable to the Parent Company.

4) SERVICES - Euro 118.8 Million

This item primarily records costs for maintenance and repair work relating to contracts and services for routine maintenance activities and upholding of plant efficiency. The decrease of € -11.0 million compared to the previous year relates to the costs incurred for Terna's listing in the previous year.

Euro	2005	2004	Change
Contracts on plants	25.6	29.5	-3.9
Various services	57.7	63.4	-5.7
Remote transmission and telephony	22.0	24.2	-2.2
Lease and rentals	13.5	12.7	0.8
Total	118.8	129.8	-11.0

5) PERSONNEL COSTS - 201.7 Million

A breakdown of the item is provided below:

Euro	As at Dec. 31, 2005	As at Dec. 31, 2004	Change
Wages and salaries	128.4	116.9	11.5
Social security contributions	33.3	30.7	2.6
Other costs	2.9	4.5	-1.6
Directors	1.1	0.7	0.4
Post-employment benefits			
Defined benefit schemes			
- Energy discount	8.8	4.7	4.1
- Asem - acem health care	1.7	1.9	-0.2
Defined contribution schemes			
- Fopen	1.1	1.0	0.1
- Fondel	0.2	0.2	0.0
Benefits due for termination of the employment relationship			
- Retirement incentives	15.2	10.5	4.7
- Employee termination indemnities	8.8	7.1	1.7
Stock options	0.2	0.0	0.2
Total	201.7	178.2	23.5

This item records costs for wages and salaries, social security contributions and other personnel costs, including the burden sustained by the Parent Company for employee retirement incentives and benefits recognized to employees during the employment relationship and after termination of the same as provided by the collective bargaining agreement of the electricity sector which is undergoing renewal. These costs record a € 23.5 million increase attributable to the personnel pertaining to the TSO activities and the additional expense incurred in the year for retirement incentives.

Both the number of employees by category of employment at year-end date and the average number are shown in the table below:

	Average number 2005	Number as at Dec.31, 2005	Number as at Dec.31, 2004
Senior management	44	75	34
Middle management	248	403	221
Office staff	1,585	1,866	1,525
Workers	1,143	1,098	1,149
Total	3,019	3,442	2,929

Compared to 2004 staff has increased by +513 employees (taking into account the 586 coming from GRTN SpA as from November 1, 2005 and the 34 coming from RTL SpA as from October 1, 2005).

6) AMORTIZATION, DEPRECIATION AND WRITE-DOWNS - Euro 175.2 Million

This item totals € 175.2 million and the increase (€ 18.2 million) compared to the previous year is due to the tangible and intangible assets acquired from GRTN with the TSO activities, which account for greater amortization and depreciation to the order of approximately € 14 million, and to new plants entering into operation. The Brazilian subsidiaries also recorded a slight increase in amortization and depreciation equal to approximately € 5 million, while total amortization and depreciation referred to the Parent Company only amounts to € 157.5 million.

7) OTHER OPERATING COSTS - Euro 45.7 Million

Euro	2005	2004	Change
Local taxes and duties	35.0	26.4	8.6
Extraordinary expenditure	4.3	18.6	-14.3
Capital losses from disposal of plants	3.4	6.3	-2.9
Other	3.0	11.6	-8.6
Total	45.7	62.9	-17.2

This item chiefly records sundry local indirect taxes and losses due to disposal of plants and other residual costs. The decrease compared to 2004 arises from the extraordinary expenditure for unfavorable adjustments to the fees for usage of the NTG pertaining to the years 2002 and 2003 (€ 16.7 million) and from the effects of the tax amnesty (€ 2.2 million) recorded in 2004.

8) CAPITALIZED COSTS - EURO 26.5 Million

Capitalized costs refer to labor costs (€ 13.0 million) and to the consumption of materials and machinery (€ 13.5 million) for plants currently under construction and related exclusively to the Parent Company.

FINANCIAL INCOME AND CHARGES

9) NET FINANCIAL INCOME/(CHARGES) - Euro 82 Million

A breakdown of the item is provided below:

In millions of Euro	As at Dec. 31, 2005	As at Dec. 31, 2004	Change
FINANCIAL INCOME			
Interest on c/a with former Parent Company Enel SpA	3.3	4.3	-1.0
Other financial income	11.6	7.1	4.5
Adjustments to Fair Value Hedge derivatives	67.1	42.0	25.1
Positive exchange-rate difference	16.8	0.0	16.8
Total income	98.8	53.4	45.4
FINANCIAL CHARGES			
Interest and other expense due to Enel SpA	0.1	25.9	-25.8
Interest due on m/l term loans	106.6	51.3	55.3
Negative exchange rate differences	0.0	14.8	-14.8
Expenses on trading derivatives	4.8	12.6	-7.8
Adjustment debt (Bond Issue) hedged part	63.4	41.8	21.6
Actualization empl. term. indem. and other empl. funds	5.9	6.9	-1.0
Total charges	180.8	153.3	27.5
TOTAL	82.0	99.9	-17.9

This decrease is the result of a combination of factors, among which the following:

- Increase in financial expense pertaining to medium/long-term debt (€ 29.5 million) attributable to the loans disbursed to the subsidiary Novatrans (year end 2004) and to Terna SpA (release of the Bond Issues at the end of October 2004 and, during the year, a further “tranche” of EIB loans);
- Positive exchange - rate differences referring to the year owing to the appreciation of the Brazilian Real against both the euro and the dollar, compared to the negative exchange-rate differences recorded in the year 2004. The positive effects recorded in the year specifically refer to conversion of the receivable for IOE due to the Parent Company and of the portion of the loans to be paid back by the Brazilian subsidiaries in other currencies (mainly dollars);
- Economic effects of the derivative financial instruments held in the Parent Company's portfolio (the same period of the previous year records only interest-rate hedging derivatives on the EIB loans and on the loans of the former Parent Company Enel SpA).

10) PORTION OF INCOME (CHARGES) ARISING FROM VALUATION OF INVESTMENTS UNDER THE EQUITY METHOD

This item records the adjustment of the investment held in the associated company Cesi SpA valued by the equity method. This adjustment gave rise to positive economic effects equal to € 1.8 million.

11) INCOME TAXES

Income taxes for the year amount to € 169 million and account for 36.2% of the pre-tax profit. In the previous year taxes were equal to € 163.5 million, accounting for 41.4% of pre-tax profit. The decrease recorded in the tax/pre-tax profit ratio (approximately - 5 percentage points) is specifically due to the following factors:

- The different tax treatment applied to the financial components of equity remuneration (interest on equity) disbursed by the company TSN;
- Greater permanent differences pertaining to the Parent Company, charged to the year 2004.

The table below provides a breakdown of the taxes recorded in the period:

In millions of Euro	2005	2004	Change
Current taxes			
- IRES	136.2	85.1	51.1
- IRAP	28.6	19.4	9.2
- Brazilian companies	11.4	8.1	3.3
Emergence of temporary differences			
- Prepaid	-14.2	-13.3	-0.9
- Deferred	32.3	63.7	-31.4
Reversal of temporary differences			
- Prepaid	11.9	10.7	1.2
- Deferred	-37.2	-10.2	-27.0
Total	169.0	163.5	5.5

The increase compared to the previous year essentially arises from the higher current taxes of the Brazilian companies linked to net income. The effects on current taxes of the limitations to the deductibility of amortization and depreciation of assets used in some regulated activities, such as management of the NTG, introduced with effect from the year 2005, have been balanced by a corresponding variation in deferred taxes.

	2005	2004
Theoretical tax rate 33%	154.1	130.2
IRAP	28.2	27.3
Brazil	-16.9	-2.8
Permanent differences and other	3.6	8.9
Effective tax	169.0	163.6
Effective tax rate	36.2%	41.4%

12) EARNINGS PER SHARE

Basic earnings per share are equal to € 0.149 where the numerator and the denominator are equal to € 297.9 million and 2,000 million respectively.

Diluted earnings per share are equal to € 0.148 where the numerator and the denominator, which are affected by the existing stock option plans, are equal to € 297.9 million and 2,014 million respectively.

SEGMENT INFORMATION

The table below provides information by business segment and geographical area:

	REGULATED ACTIVITIES					
	TRANSMISSION				Non-regulated activities	Total
	Italy	Brazil	Dispatching	Metering		
Revenues	837.5	170.4	17.7	1.5	60.3	1,087.4
Segment income	465.1	116.0	-2.3	1.5	26.6	606.9
Non-allocated costs						59.8
OPERATING INCOME						547.1
Financial income/(charges)						-82.0
Portion of charges/income of investments valued by equity method	1.8					1.8
Taxes						169.0
Net profit						297.9
OTHER INFORMATION						
Assets	4,024.0	884.2	1,090.4	2.2	289.7	6,290.6
Liabilities	2,797.6	499.7	837.9	0.0	253.2	4,0388.4
Capital expenditure	260.3	9.4	3.2			272.9
Amortization, depreciation and write-downs	151.3	17.7	6.2			175.2
Other non-monetary costs	1.1					1.1

INFORMATION ON THE CONSOLIDATED BALANCE SHEET

ASSETS

13) PROPERTY, PLANT AND MACHINERY - Euro 4,646.3 million

Tangible assets amount to € 4,646.3 million (€ 4,323.3 million at Dec. 31, 2004).

The table below provides a breakdown of the item by category:

Euro	Land	Accessory land.	Buildings	Plant and machinery	Comm. industr. equipment	Other assets	Leasehold improv.	Work in prog. and advances	Total
Cost at Jan 1, 2005	1.6	18.7	574.0	6,926.9	39.5	12.6	0.0	380.0	7,953.3
Capital expenditure		0.2	12.4	90.1	2.9	1.8	2.5	161.4	271.3
Start-up in the year			9.1	161.6		0.1		-170.8	0.0
Acquisition TSO activities			30.0	55.6	0.1	16.7		3.1	105.5
Change in consolidation area		0.1		37.2				0.8	38.1
Exchange-rate differences			10.4	143.6		0.1			154.1
Disposals			-0.2	-27.7	-0.5			-0.2	-28.6
Other changes				-16.2					-16.2
Reclassifications	0.1		-25.1	25.1					0.1
Cost at Dec. 31, 2005	1.7	19.0	610.6	7,396.2	42.0	31.3	2.5	374.3	8,477.6
Acc. depr. and write-downs at Jan 1 2005			-200.5	-3,391.4	-27.5	-10.6	0.0	0.0	-3,630.0
Depreciation			-13.4	-152.9	-2.2	-1.0			-169.5
Write-downs for losses									0.0
Acquisition TSO activities			-3.5	-23.3		-8.7			-35.5
Change in consolidation area				-11.5					-11.5
Exchange-rate differences			-0.4	-7.6					-8.0
Disposals			0.1	23.7	0.4				24.2
Other changes				-1.0					-1.0
Reclassifications			1.7	-1.7					0.0
Acc. depr. and write-downs at 2005	0.0	0.0	-216.0	-3,565.7	-29.3	-20.3	0.0	0.0	-3,831.3
BOOK VALUE									
At Dec. 31, 2005	1.7	19.0	394.6	3,830.5	12.7	11.0	2.5	374.3	4,646.3
At Dec. 31, 2004	1.6	18.7	373.5	3,535.5	12.0	2.0	0.0	380.0	4,323.3

The item “plant and machinery” includes the electricity transmission network and transforming stations in Italy and Brazil, the centralized systems for the remote monitoring and the national system of energy control. The Brazilian assets include the Northeast - Southeast transmission line, which has a nominal voltage of 500 kV and is about 1,062 km long, beginning at the Serra da Mesa substation, in the state of Goiás, and ending at the Sapeaçu substation, in the state of Bahia, which began operations in March 2003, and the North - South II Transmission line, which has a nominal voltage of 500 kV and is about 1,280 km long, beginning at the Imperatriz substation, in the state of Maranhão, and ending at the Samambaia substation, in the Federal District.

The item “improvements to third-party assets” refers to the lump-sum contribution for upgrading and adjustment of the electricity powered systems of the technological infrastructure of the Wind network.

The table below provides a summary of the changes in tangible assets during the year:

In millions of Euro	2005
Capital expenditure	
- Power lines	121.3
- Transforming substations	121.7
- Leasehold improvements and other	18.9
- Brazil	9.4
Total expenditure	271.3
Depreciation	-169.5
Disposals and other changes	-21.5
Exchange-rate differences	146.1
TSO business activities	70.0
Change in consolidation area	26.6
TOTAL	323.0

In addition to the ordinary year-on-year movements referring to capital expenditure (€ 271.3 million), to grants pertaining to start-up of plants during the year (€ 16.2 million), to disposals (€ 4.4 million) and to depreciation (€ 169.5 million), the changes recorded also refer to acquisition of assets further to acquisition from GRTN of the TSO activities (€ 70 million) and acquisition of the company RTL SpA (€ 26.6 million). The main capital expenditure effected during the year by the Parent Company relate to the Turbigo - Rho (€ 23.8 million) and Matera - S. Sofia (€ 7.4 million) power lines and to the construction of the Santa Barbara transforming station (€ 10.9 million).

As far as work in progress and advances are concerned attention is drawn to the following works for development and upgrading to the network worth more than € 5 million:

Euro	2005
KV 380 Matera - S. Sofia	71,957,534
KV 380 Turbigo - Rho	24,423,239
KV 380 Laino - Feroletto - Rizziconi	10,373,119
KV 150 Sardegna - Corsica	7,284,161
380 KV TRANSFORMING SUBSTATIONS	
Calenzano	14,979,316
Carpi Fossoli	13,310,615
Santa Barbara	12,197,337
Foggia	7,737,451
Fratta	6,868,564
Rumianca	6,280,208
Sorgente	5,652,480
220 KV TRANSFORMING SUBSTATIONS	
Santa Maria Capua Vetere	5,380,735

14) GOODWILL - Euro 154.7 million

Goodwill amounts to € 154.7 million (€ 117.0 million at Dec. 31, 2004) and pertains to the Brazilian subsidiaries and to the investee RTL acquired during the year.

The table below provides a breakdown of the item:

In millions of Euro	TSN	NVT	RTL	Total
Balance at Dec. 31, 2004	80.5	36.5		117.0
Change in consolidation area			0.5	0.5
Exchange-rate differences	25.6	11.6		37.2
BALANCE AT DEC. 31, 2005	106.1	48.1	0.5	154.7

The increase in the balance at December 31, 2005 compared to the previous year refers to:

- Adjustment to the year-end exchange rate (€ 37.2 million) of the goodwill recorded further to acquisition of the equity investments in TSN and Novatrans, on December 31, 2003;
- Acquisition of the subsidiary RTL on September 30, 2005 (€ 0.5 million).

Impairment Test

The recoverable value of the Brazilian companies to which goodwill is attributed has been estimated on the basis of value in use. This estimate was performed using the discounted cash flows method for a explicit period of 5 years, equal to the time-span covered by the last approved business plan. Said cash flows have been projected up to the concession termination date (2030) extrapolating the data on the basis of Company assumptions and the macroeconomic scenario of the reference market, estimated by the major banks operating in Brazil. The following main macroeconomic data were considered:

- IGPM (inflation rate basket of industrial goods) to which the revenues and costs are indexed;
- TJLP (cost of loan in Real disbursed by BNDES - Banco Nacional de Desenvolvimento Economico e Social);
- R\$/USD exchange rate.

Said cash flows were actualized using a discount rate indicative of the cost of own means (calculated considering the specific risk of the transmission activities in Brazil), of the cost of third-party means and of the average capital structure of the companies. A 34% tax rate was used. The recoverable value of the goodwill estimated as above is higher than the book value (shown above) for both the CGU. On the basis of the valuations effected, reasonable amendment of the parameters used will not produce significant impact on the results of said valuations and accordingly on the greater value identified.

15) INTANGIBLE ASSETS - Euro 151.5 Million

The table below illustrates changes occurring in intangible assets:

In millions of Euro	Concessions	Other assets	Work in progress and intangible advances	Total
Balance at Dec. 31, 2004	0.0	0.0	0.0	0.0
TSO business activities	135.4	16.0	4.1	155.5
Capital expenditure	0.0	0.0	1.6	1.6
Amortization	-0.9	-4.7	0.0	-5.6
Balance at Dec. 31, 2005	134.5	11.3	5.7	151.5
Situation at Dec. 31, 2004	0.0	0.0	0.0	0.0
Cost	135.4	16.0	5.7	157.1
Accumulated amortization	-0.9	-4.7	0.0	-5.6
Situation at Dec. 31, 2005	134.5	11.3	5.7	151.5

Intangible assets, solely attributable to the Parent Company, amount to € 151.5 million (at Dec. 31, 2004 the item had a zero balance). The increase is mainly due to the acquisition of the TSO business activities from GRTN and chiefly refers to recognition of the concession for exclusive performance of electricity transmission and dispatching activities (€ 134.5 million). The concession for transmission and dispatching of electricity in Italy, including the unified management of the national transmission grid, which was formerly held by GRTN until October 31, 2005, was purchased by Terna on November 1, 2005.

As established by Decree of the Ministry of Productive Activities of April 20, 2005, said concession has a twenty-five year validity commencing from aforesaid date of the effective transfer to Terna of the activities, functions, assets and active and passive legal relationships pertaining thereto.

This intangible asset was initially reported at fair value and subsequently valued at cost. The initial fair value equal to € 135.4 million has been reduced by amortization for the period.

The other intangible assets essentially refer to:

- Development and evolution of software applications for managing the energy billing process;
- Development and evolution of software applications aimed at protecting the electricity system;
- Software applications linked to the development of the electricity exchange with particular regard for the operators' register, consumption units and development of foreign procedures.

Said software applications are amortized over a period representing the residual useful life, generally within three years, given the high obsolescence rate of these assets.

16) PREPAID TAX ASSETS - Euro 57.3 million

Prepaid tax assets refer to the following items:

In millions of Euro	As at Dec. 31, 2005	As at Dec. 31, 2004	Change
All. to provisions for risks and charges	10.3	13.2	-2.9
Empl. term. indem. and other personnel expense	28.4	26.4	2.0
Empl. term. indem. and other pers. expense - TSO bus. act.	1.6	0.0	1.6
CFH and trading derivatives	9.6	10.4	-0.8
Amortization/depreciation assets	0.7	1.4	-0.7
Tax losses (RTL NVT)	5.0	0.0	5.0
Other	1.7	0.2	1.5
Prepaid taxes	57.3	51.6	5.7

The net increase (€ 5.7 million), compared to the previous year, is partly attributable to the transfer of personnel, acquired from GRTN further to disposal of the business activities, and to the allocation of prepaid taxes against tax losses recorded by the subsidiaries RTL in the current year (€ 0.5 million) and Novatrans for previous-year losses (€ 4.5 million). With reference to the latter, the allocation was implemented in the previous year insofar as there was reason to deem these recoverable.

The net increase in the item under review (€ 5.7 million), has not been recorded in a balancing entry in the income statement with reference to the tax effects relating to the following events:

In millions of Euro	
Acquisition subsidiary RTL	1.9
Acquisition TSO business activities	1.5
Adjustment of the value of cash flow hedge derivatives	(0.4)
Effects of conversion of Novatrans prepaid taxes	0.4
Total	3.4

There are no unrecorded prepaid tax assets at December 31, 2005.

17) INVESTMENTS ACCOUNTED FOR UNDER THE EQUITY METHOD - Euro 6.4 million

Investments accounted for under the equity method amount to € 6.4 million and refer to the company Cesi SpA and represent a 24.4% stake in share capital.

This company operates in the construction and management of laboratories and plants for experimental tests, trials, studies and research concerning electrotechnics in general and technical and scientific progress in this field. Compared to the previous year equity investments have increased (€ 3.5 million) owing to acquisition of the TSO activities (€ 1.7 million), increasing the 15% interest already held by Terna. Valuation by the equity method has produced a € 1.8 million increase compared to the purchase cost of the investment, corresponding to the adjustment of the value of the investment at the date of acquisition of the entire percentage ownership by € 0.4 million, and to the Group's share of net income generated by the associated company in the last two months (€ 1.4 million).

The table below provides the key figures relating to the associated company:

In millions of Euro	ASSETS		LIABILITIES		Shareholder's equity	Revenues	Net income
	Current	Non-current	Current	Non-current			
Cesi	86.0	72.8	70.5	44.4	26.1	129.7	6.4

18) FINANCIAL ASSETS

The table below provides a comparison, for each category, of the book value and the fair value of the financial assets reported in the consolidated balance sheet

In millions of Euro	BOOK VALUE		FAIR VALUE	
	2005	2004	2005	2004
FVH derivatives	106.1	39.0	106.1	39.0
Cesi equity investment		2.9		
Non-current financial assets	106.1	41.9	106.1	39.0
Deferred assets on FVH derivative contracts	4.4	4.6		
Current financial assets	4.4	4.6		
TOTAL	110.5	46.5	106.1	39.0

The change occurring in Non-current financial assets, due to revenues accrued but not yet collected on financial items, refers to the fair value of the financial hedging instruments, negotiated on the bond issue, determined by actualizing the expected cash flows on the basis of the market interest-rate curve. The criteria for selection of the banking counterparties with which said derivatives were implemented, provide the company with a safeguard against potential credit risks that could arise therefrom. Information on the Cesi equity investment can be found in paragraph 17 on equity investments accounted for under the equity method.

The table below shows the total Group financial assets subject to interest-rate risk, subdivided by category:

In millions of Euro	2005	2004	Maturity	Average interest rate
FVH derivatives	106.1	39.0	2014-2024	2.1%
Total	106.1	39.0		

The FVH derivatives, of which the impact on the income statement balances the impact of the delta fair value of the bond issues, are sensitive to the variations in the euro interest rate. In calculating the fair value, determined by actualizing the expected cash flows on the basis of the market interest-rate curve at the reporting date, the same method used in 2004 has been applied.

19) INVENTORIES - Euro 21.2 million

Inventories include materials and equipment to be used in the operation, maintenance and construction of plants to the order of € 21.2 million (€ 19.6 million at December 31, 2004). The € 1.6 m increase is chiefly attributable to routine plant maintenance requirements.

20) TRADE RECEIVABLES - Euro 1,026.2 million

Trade receivables break down as follows:

In millions of Euro	As at Dec. 31, 2005	As at Dec. 31, 2004	Change
Receivables from customers	266.5	157.9	108.6
Receivables for energy items	759.7	0.0	759.7
Trade receivables	1,026.2	157.9	868.3

Trade receivables amount to € 1,026.2 million and record an increase (€ 868.3 million) compared to 2004 attributable to the electricity transmission and dispatching related activities performed by Terna in its new capacity as owner and operator of the national Transmission Grid further to acquisition of the transmission and dispatching activities from GRTN SpA with effect from the month of November 2005.

Trade receivables do not bear interest and the terms of payment are in line with commercial practices in the business areas to which they refer.

Receivables from Customers - Euro 266.5 million.

These mostly refer to receivables pertaining to the CTR tariff component relating to remuneration to be paid to the Company for use of the national transmission grid by electricity distributors (resolution 5/04 article 17 and subsequent amendments) and producers (resolution 5/4 article 19 and subsequent amendments). Specifically, in compliance with resolution 5/04, the aforesaid receivables mainly consist of usage fees for the last two months of 2005, falling due in January and February 2006. They also include the pertinent portion of fees for operation of the Brazilian lines, part of which invoiced and part of which yet to be invoiced (€ 33.2 million).

With regard to the foreign subsidiaries, receivables are up on the previous year (+ € 23.1 million) chiefly due to appreciation of the R\$/€ exchange rate (€ 7.0 million), to adjustment of the concession fees (RAP) to the inflation rate (IGPM rate) which occurred during the year (€ 1.8 million), to the recognition of higher Pis/Cofins (social contributions) rates paid (€ 3.7 million) and to the recording of receivables due from Enelpower for termination of the EPC contract (€ 5.3 million).

Other receivables from customers also include receivables due from Enel Group companies, and in particular from Enel Distribuzione (€ 4.6 million) for operating and maintenance activity on HV lines owned by the same and from the company Enel.Net (€ 7.0 million) for the laying of fibre optic lines, and their operation, maintenance and development.

Receivables for energy items - Euro 759.7 million

Receivables for energy items mostly report receivables relating to the “let-through items” pertaining to the activity of energy dispatching and which do not contribute to the creation of margins for the company. Also included are receivables for considerations, due from market operators as remuneration of the activity of dispatching, (DIS tariff component - resolution 237/04) and metering (MIS tariff component - resolution 05/04).

Through the dispatching activity Terna guarantees certain supplies ensuring adequate resources to meet demand and continuous balance in real time between energy needs and available resources, while the metering activity refers to the reading and recording of the measurements of energy introduced by the production units to the NTG.

Among receivables relating to energy items, of particular importance are the outstanding charges for subscription to the ETSO-CBT (European Transmission System Operators-Cross Board Trade) agreements concerning compensation of costs relating to energy transit on foreign electricity grids. With its resolution 15/2005 AEEG (the Italian Regulatory Authority for Electricity and Gas) in fact guaranteed coverage of said charges, establishing that the procedures for refund are to be defined by specific order.

21) OTHER ASSETS

In millions of Euro	As at Dec. 31, 2005	As at Dec. 31, 2004	Change
Receivables from others			
- Loans and advances to employees	4.2	3.3	0.9
- Deposits with third parties	1.3	0.7	0.6
- Prepaid empl. term. indem. tax	1.5	2.4	-0.9
Other non-current assets	7.0	6.4	0.6
Tax receivables	11.7	16.4	-4.7
Receivables from others			
- Advances to employees	0.2	0.2	0.0
- Other	21.0	18.2	2.8
Other current assets	32.9	34.8	-1.9

Receivables for non-current assets, a breakdown of which is provided in the table above, record a balance substantially in line with values reported in the previous year.

The item other current assets presents a balance of € 32.9 million (€ 34.8 million at December 31, 2004) chiefly attributable to the following factors:

- Tax receivables for € 11.7 essentially referring to the advance payment of VAT effected in December (€ 1.9 million), to receivables for tax paid abroad (in Greece € 1.8 million and in Brazil € 0.1 million), which can be deducted in the tax-return in Italy, to receivables for taxes pertaining to the foreign subsidiaries

(€ 5.5 million) and to the subsidiary RTL (€ 0.9 million);

- Receivables due from the Greek revenue authorities for indirect taxes (VAT - € 9 million) in relation to the activities carried out by the Terna branch in Greece;
- Adjustment in the company's favor (€ 2.0 million) pertaining to the acquisition of the TSO activities and arising from comparison between the initial balance at Dec. 31, 2004, used to determine the sales price, and the final transfer balance reported at Oct. 31, 2005;
- Outstanding costs relating to prepaid insurance premiums (€ 2.9 million);
- Advances disbursed to employees and third parties for various accounts (€ 3.3 million).

22) CASH AND CASH EQUIVALENTS - Euro 76.6 million

Cash and cash equivalents of the Parent Company at Dec. 31, 2005 amount to € 15,8 million, of which € 15.7 million represent available funds on bank current accounts (yielding an average of 2.3%) and € 0.1 million as cash on hand.

Cash and cash equivalents of the Brazilian subsidiaries at Dec. 31, 2005 amount to € 60.8 million, of which € 47.3 million represent available funds in R\$ held on bank current accounts (yielding an average of 17.6%), € 7.4 million in available funds in USD held on bank accounts (yielding an average of 4.2%) and € 6.1 million as cash on hand.

The cash and cash equivalents of the foreign subsidiaries also refer for € 18.6 million to available accounts and € 42.2 million to fixed-term deposit accounts for project financing purposes.

At Dec. 31, 2005 the Parent Company holds an additional debt capacity equal to € 1,190 million, of which € 200 million is the residual amount of the EIB granted for € 300 million and used for € 100 million, 500 million relating to the 5-year revolving credit facility and the remaining € 490 million to revocable credit lines (short money).

LIABILITIES AND SHAREHOLDERS' EQUITY

23) GROUP SHAREHOLDERS' EQUITY - Euro 1,902.2 million

Share capital - Euro 440.0 million

The share capital of Terna Spa is represented by 2,000,000,000 ordinary shares of a par value of € 0.22 each, held as follows:

- By Cassa Depositi e Prestiti (CdP - government controlled public financing agency), for a stake equal to 29.99% of share capital further to acquisition on the part of CdP of shares owned by Enel SpA, effected during the third quarter 2005, in implementation of authorizing order no. 14542 of August 4, 2005 issued by the Italian Anti-Trust Authority;
- By Enel SpA, to the extent of approximately 6.14%; said stake, as a result of maturity, in December, of the right to allocation of free shares (so-named bonus shares) to subscribers of the IPO of Terna shares in June 2004, has at today's date been further reduced to approximately 5%;
- The remaining shares equal to approximately 63.87% (1,277,400,000 shares) have been parceled out further to the Public Sale Offer addressed to public and institutional investors of June 2004 and to the subsequent accelerated book building transaction targeted at Italian and foreign institutional investors.

Legal reserve - Euro 88.0 million

Legal reserve represents 20% of the share capital of the Parent Company.

Other reserves - Euro 723.1 million

Other reserves have experienced a net variation of € - 416.6 million, as a result of the following movements:

- Reclassification of the reserve pursuant to the Vietti law to retained earnings (€ -421.3 million);
- Adjustment to fair value of the cash flow hedge derivatives net of the relative tax effect (€ 0.7 million);
- Allocation to capital reserve of the portion referring to the year 2005 (€ 3.8 million) of the incentive obtained from the Brazilian Ministry of National Integration on the part of the subsidiary TSN;
- Recording of the cost (€ 0.2 million) relating to the stock option plans described in subsequent paragraphs.

Retained earnings (loss) carried forward - Euro 453.2 million

Retained earnings chiefly refer to the reserve pursuant to the Vietti law (€ 421.3 million) set up at December 31, 2005 among the other reserves and reclassified during 2005 under retained earnings. The other changes in the year essentially refer to the following events:

- Allocation to legal reserve of € 2.4 million supplementing the allocation to said reserve of the excess consolidated net income 2004, after dividend distribution during the first year-half 2005 (€ 140.0 million);
- Increase of the translation reserve (€ 79.0 million) due to differences arising upon consolidation of the foreign subsidiaries and essentially resulting from the reduction in the exchange rate of the Brazilian Real during the year. Accordingly the adjustment of goodwill to the year-end exchange rate produced a € 37.2 million increase in this item;
- Allocation to coverage of retained losses of the portion referring to the year 2005 (€ 1.6 million) of the incentive obtained from the Brazilian Ministry of National Integration on the part of the subsidiary Novatrans.

Interim dividend 2005

On September 9, 2005, the Board of Directors, having consulted the independent auditors pursuant to Article 2433-bis of the Italian Civil Code, passed a resolution to distribute an interim dividend for 2005, to the order of € 100 million. The schedule of reconciliation of the shareholders' equity and net income of the Parent Company at December 31, 2005 with the corresponding consolidated figures is provided in the paragraph "Schedules of separate and consolidated reconciliation". The table below provides a breakdown of the single items of the Shareholders' Equity at year end, with specification of their origin, possible utilization, and extent to which they may be distributed:

NET INCOME

In millions of Euro	Amount	Possible utilization	Available amount
Share capital	440.0		
Legal Reserve	88.0	B	
Other Reserves			
- of Capital	396.1	A,B,C	396.1
- of Income	327.0	A,B	327.0
Retained earnings	453.2	A,B,C	453.2
Interim dividends	-100		
Net income 2004	297.9		
TOTAL			1,176.3
Non-distributable amount			770.9
Remaining distributable amount			405.4

A: for capital increase, B: for covering losses, C: for distribution to shareholders

The non-distributable amount essentially refers to income reserves and retained earnings for which taxation has not been paid off.

Stock Option Plans

On May 9, 2005, the Board of Directors of the Parent Company passed a resolution to implement the first corporate stock option plan for senior managers of Terna Spa and/or of its subsidiaries, pursuant to Article 2359 of the Italian Civil Code, who fulfill the most important functions in terms of achievement of the company's strategic results.

On December 21, 2005, the Board of Directors, on the basis of proposals submitted by the Remuneration Committee also passed a resolution to implement a 2006 stock option plan for senior managers of the Terna Group, who fulfill the most important functions in terms of achievement of the company's strategic results.

In keeping with international practices adopted by the major Italian listed companies, these plans aim to provide the Terna Group with a means of ensuring management incentive and loyalty. The stock options will allow the Group to encourage a sense of company loyalty in key resources while at the same time ensuring they constantly strive to create value, thus determining convergence between shareholders' interests and those of management.

The characteristics of the 2005 and 2006 stock option plans are stated below.

Regulation of the first stock option plan (passed on May 9, 2005)

The plan provided for the offer of 9,950,000 options to be distributed to a total of approximately 20 senior managers of Terna Spa and/or of its subsidiaries, pursuant to Article 2359 of the Italian Civil Code, who fulfill the most important functions in terms of achievement of the company's strategic results. The total number of expected beneficiaries also included some of the senior managers of GRTN who subsequently converged on Terna.

The plan provided for their inclusion, upon unification, under the same terms and conditions, with the exception of the subscription price determined at the time of the offer to senior managers, according to the procedures specified hereunder. As acquisition of the business activities from GRTN only effectively took place on November 1, 2005, the plan was not actually extended to the former GRTN senior manager.

The stock option plan regulations:

- 1 Provided that the strike price (subscription price) of each share is determined as equal to the arithmetic average of the reference prices of the ordinary Terna SpA share recorded by the electronic system of Borsa Italiana SpA in the period between the offer date and the same day of the previous calendar month;
- 2 Defined as conditions to exercise of the option - qualifying as conditions precedent - that:
 - (a) the amount of the Terna SpA Group EBITDA relating to the year of assignment (2005) and stated in the Group budget approved by the Board of Directors is exceeded;
 - (b) the percentage variation between the reference price of the Terna SpA share stated by the electronic system of Borsa Italiana SpA at January 1 of the year in which options were assigned and the average price at December 31 of the same year is higher than the percentage variation recorded in the same period of time by the reference index (50% MIBTEL and 50% FTSE 300 Electricity). In performing this calculation, both the percentage variation of the reference price of the Terna SpA share and the percentage variation of the reference index should be adjusted to take account of the effect of distribution of the respective gross dividends (ordinary and extraordinary including any free share distributions), in a Total Shareholders' Return logic.

The stock option plan regulations provided that both the above conditions to exercise would have to be met in order for the beneficiaries to be allowed to exercise the options.
- 3 Provided that the subscription of the shares at a price equal to the strike price was to be fully borne by the beneficiaries, as the plan did not include any discount in this respect;
- 4 Provided that the options, upon satisfaction of the conditions to exercise, are exercisable (i) to the extent of 30% as from the first year after assignment, (ii) to the extent of 60% as from the second year after assignment and (iii) to the extent of 100% as from the third year after assignment. All the options granted and rendered exercisable should be exercised by March 31, 2010. The options actually proved exercisable only in the open market days falling in the last 10 days of each month, unless these days fell in the 3 open market days prior to the "coupon detachment" or in the two blocking periods, each lasting a month, set in the run-up to approval of the draft financial statements and the half-yearly report on the part of the Board of Directors.

In the first half-year 2005 application of the stock option plan led to the assignment of 3,899,000 options, featuring a strike price equal to ? 2.098, to 9 senior managers of the company.

On March 15, 2005, the Board of Directors, on the basis of information provided by the Remuneration Committee, verified that the second of the conditions to exercise specified in point 2 above had not been met and, hence in accordance with the Stock Option Plan Regulations, it declared the options assigned to be non-exercisable.

Regulation of the 2006 stock option plan (passed on December 21, 2005)

The plan provides for the offer of 10,000,000 options to be distributed to a total of approximately 20 senior managers of Terna Group, who fulfill the most important functions in terms of achievement of the company's strategic results, among whom also the Chief Executive Officer in his capacity as senior manager of the company.

The approved stock option plan regulations:

- 1 Provides that the strike price (subscription price) of each share is determined as equal to the arithmetic average of the reference prices of the ordinary Terna SpA share recorded by the electronic system of Borsa Italiana SpA in the period between the offer date and the same day of the previous calendar month;
- 2 Identifies two performance parameters that must be reached as a condition to exercise of the options and, hence, the right to subscription of the ordinary Terna shares of new issue, and precisely:
 - (a) the amount of the Terna SpA Group EBITDA relating to the year of assignment (2006) and stated in the Group budget approved by the Board of Directors is exceeded;
 - (b) positive assessment of the performance of each beneficiary during the year 2006 by the CEO, with provision for 50% reduction of the options exercisable by each beneficiary in the case of failure to meet the second condition.
- 3 Provides that the options, upon satisfaction of the conditions to exercise, may be exercised by the respective beneficiaries, by March 31, 2010 and within the limits of the following maximum quantities:
 - (i) up to 30% of exercisable options, as from the date to be specified in the notice stating satisfaction of the conditions to exercise, (ii) up to 60% of exercisable options, as from the first day of the

calendar year after the notice stating satisfaction of the conditions to exercise and (iii) up to 100% of exercisable options, as from the first day of the second calendar year after the notice stating satisfaction of the conditions to exercise. The exercise of exercisable options may occur only in the open market days falling in the last 10 days of each month.

The right to exercise the exercisable options will be suspended (i) in the last three open market days prior to the “coupon detachment”; (ii) in the period between the day set for approval of the draft financial statements on the part of the Board of Directors and the same day of the previous month and (iii) the period between the date set for approval the half-yearly report on the part of the Board of Directors and the same day of the previous month.

Application of the Stock Option Plan 2006 gave rise to the assignment, on December 21, 2005, of 9,992,000 options featuring a strike price equal to € 2.072, to 17 of the company’s senior managers. The Board of Directors will verify whether the conditions to exercise have been met at the time of approval of the draft financial statements of the year at December 31, 2006.

At December 31, 2005 the options assigned by said remuneration plans are all outstanding and none is exercisable at said date.

	2005 Plan	2006 Plan
Outstanding at Jan. 1	-	-
Granted during the year	3,899,000	9,992,000
	3,899,000	9,992,000
Exercised during the year	-	-
Matured during the year	-	-
Outstanding at year end	3,899,000	9,992,000
Exercisable at year end	-	-

The table below provides the residual useful life of the stock options at December 31, 2005 and the relative fair value:

2005 PLAN

	Option granted (at May 9, 2005)	Maturity	Fair Value determined at grant date (Euro)	Fair Value option with assigned probability factor (50%)
	1,169,700	2006	0.183	0.092
	1,169,700	2007	0.183	0.091
	1,559,600	2008	0.181	0.091
Total	3,899,000			

2006 PLAN

	Option granted (at December, 21 2005)	Maturity	Fair Value determined at grant date (Euro)	Fair Value option with assigned probability factor (100%)
	2,997,600	2007	0.126	0.126
	2,997,600	2008	0.121	0.121
	3,996,800	2009	0.115	0.115
Total	9,992,000			

The pricing method used is the Cox-Rubinstein which takes account of the value of the Terna share at assignment date, of share volatility, of the interest-rate curve at the assignment date and consistent with the length of the plan. The parameters used for pricing are as follows:

- Closing price (underlying or spot price) of the share at assignment date (source Bloomberg), respectively equal to € 2.068 for the 2005 plan and € 2.058 for the 2006 plan;
- Strike price, respectively equal to € 2.098 for the 2005 plan and € 2.072 for the 2006 plans;
- Tax curve for calculation of the discount factor at the assignment date (source Reuters);
- Historical volatility of the share recorded at the assignment date (source Bloomberg) respectively equal to 20.348% for the 2005 and 14.860% for the 2006 plan.

24) LOANS AND FINANCIAL LIABILITIES

The table below provides a breakdown of the loans and financial liabilities entered in the Consolidated Financial Statements of the Terna Group at December 31, 2005. In particular, it provides a comparison, for each category, of the book value and the fair value of all the financial liabilities entered in the Consolidated Financial Statements of the Terna Group.

In millions of Euro	BOOK VALUE		FAIR VALUE	
	2005	2004	2005	2004
Bonds	1,498.4	1,434.8	1,498.4	1,434.8
Bank loans				
- Italy	370.5	300.0	370.5	300.0
- Brazil	440.2	350.1	436.5	347.6
Total bank loans	810.7	650.1	807.0	647.6
Long-term loans	2,309.1	2,084.9	2,305.4	2,082.4
CFH derivatives	17.8	18.9	17.8	18.9
Trading derivatives	11.2	12.6	11.2	12.6
Non-current financial liabilities	29.0	31.5	29.0	31.5
Short-term loans	55.0		55.0	
Current portions of long-term loans	58.3	47.0	58.3	47.0
S/t loans and s/t portions of l/t loans	113.3	47.0	113.3	47.0
TOTAL	2,451.4	2,163.4	2,447.7	2,160.9

With regard to the bond issue the book value is determined by actualizing the expected cash flows to the market interest-rate curve at December 31, 2005.

The official quotations for the instruments traded on regulated markets are as follows:

- 20 year bond price at Dec. 31, 2004 105.78 and at Dec. 31, 2005 109.68;
- 10 year bond price at Dec. 31, 2004 103.14 and at Dec. 31, 2005 105.43.

Long-term loans

The table below shows the book value of medium/long-term loans and the repayment plan at December 31, 2005, with distinction between types of loans, including the portions maturing within twelve months.

In millions of Euro	Dec 31,2005	Dec 31,2004	Repayment period	Current portion	Non-current portion	2007	2008	2009	2010	Beyond
Bond issue	1,498.4	1,434.8	2014-2024		1,498.4					1,498.4
IDB	48.8	47.3	2016	5.7	43.2	4.8	5.3	5.7	5.1	22.3
Total fixed-rate	1,547.2	1,482.1		5.7	1,541.6	4.8	5.3	5.7	5.1	1,520.7
EIB no. 20271	61.4	68.2	2014	6.8	54.5	6.8	6.8	6.8	6.8	27.3
EIB no. 21159	238.6	250.0	2016	22.7	215.9	22.7	22.7	22.7	22.7	125.0
EIB no. 22947	100.0		2020		100.0			4.6	9.1	86.3
BNDES	420.2	331.6	2016	23.1	397.1	25.5	28.0	30.9	34.1	278.8
Total floating-rate	820.2	649.8		52.6	767.5	55.0	57.5	65.0	72.7	517.4
TOTAL	2,367.4	2,131.9		58.3	2,309.1	59.8	62.8	70.7	77.8	2,038.1

For the bond issues the fair value at Dec. 31, 2005, calculated as above, is shown, as is the repayment of their nominal value at maturity.

For the components of the financial borrowings their nominal value and relative repayment plan are shown. The total value of Terna Group loans at December 31, 2005 is equal to € 2,367.4 million, of which € 2,309.1 million long/medium-term.

The guarantees provided are equal to € 255,0 million and refer to shares of the subsidiaries TSN and Novatrans, owned by Terna, pledged to the banks (BNDES - IDB) providing loans for the investments in Brazil. Terna retains the voting and dividend rights.

The changes occurring during 2005 include, as specified above, the disbursement, on March 15, 2005, of a € 100 million loan to the Parent Company, relating to a contract for a total of € 300 million negotiated with the European Investment Bank (EIB) and aimed at providing coverage of the development investments scheduled in the company's industrial plan. The remaining € 200 million may be disbursed by the end of 2007 and, as in the case of the other EIB loans, will be repaid as from the fifth year with an 11-year repayment period. The loan has the following terms:

- Floating interest rate with a ceiling equal to 3m Euribor + 0.27% (last fixing at Dec. 15, 2005 equal to 2.56% equivalent to 3m Euribor increased by 10 bps;
- Interest payments made on a half-yearly basis (March 15 and September 15);
- Repayment of principal: in 22 equal installments paid half-yearly from September 15, 2009 to December 15, 2019.

The loan has not been hedged and is therefore entirely exposed to interest-rate risk.

The table below shows the medium/long-term borrowings position with distinction by currency and by average interest rate, including the portions maturing within twelve months.

In millions of Euro	Dec.31,2005	Repayment period	Original currency	Current portion	Non-current portion	Average interest rate at Dec.31,2005
Bond issues	1,498.4	2014-2024	Euro		1,498.4	4.62%
IDB	48.8	2016	Usd	5.7	43.2	9.03%
Fixed-rate	1,547.2			5.7	1,541.6	
EIB no. 20271	61.4	2014	Euro	6.8	54.5	2.14%
EIB no. 21159	238.6	2016	Euro	22.7	215.9	2.23%
EIB no. 22947	100.0	2020	Euro		100.0	2.25%
BNDES	420.2	2016	Real	23.1	397.1	13.29%
Floating-rate	820.2			52.6	767.5	
TOTAL	2,367.4			58.3	2,309.1	

With regard to the bond issue the average interest rate, also taking into account the average rate of interest income on the hedging transactions stated in paragraph 18 and the rate of interest expense on the trading derivatives specified below under current liabilities, is equal to 2.9%. As for the two EIB loans hedged against tax fluctuations, taking into account the effect of the derivative instruments valued at cash flow hedge, the cost of which has been specified under current liabilities, the EIB no. 20271 has an average rate of 4.6%, while the EIB no. 21159 an average rate of 4.4%.

The nature of the financial hedging transactions implemented to safeguard the company from the risk of interest-rate fluctuations guarantees limited volatility of the cost of financial loans.

The table below shows the changes in loans which occurred during the year:

Type of debt	Notional debt at Dec. 31,'04	Book value at Dec. 31,'04	Repayments and Capitalizations	New issues	Exchange rate differences	Delta Fair Value Dec. 31,'04 Dec. 31,'05	Notional debt at Dec. 31,'05	Book value at Dec. 31,'05
Listed fixed-rate bonds	1400.0	1434.8	0.0	0.0	0.0	63.6	1400.0	1498.4
Total bonds	1400.0	1434.8	0.0	0.0	0.0	63.6	1400.0	1498.4
Floating-rate bank loans	378.9	378.9	(19.0)	0.0	109.0	0.0	469.0	469.0
Floating-rate BEI loans	318.2	318.2	(18.2)	100.0	0.0	0.0	400.0	400.0
Total bank loans	697.1	697.1	(37.2)	100.0	109.0	0.0	869.0	869.0
TOT. M/L FINANCIAL BORROWINGS	2097.1	2131.9	(37.2)	100.0	109.0	63.6	2269.0	2367.4

Compared to December 31, 2004 the medium and long term loans have on the whole increased by € 235.5 million, due by € 63.6 million to the increase in the fair value of the bond issues, by € 81.8 million to a net increase in the EIB loans owing to the combined effect of the new debt equal to € 100.0 million disbursed to the Parent Company on March 15, 2005 and of the decrease for the repayments scheduled in the amortization plans (€18.2 million). The increase of Brazilian net loan, equal to € 90.0 million, is given by the algebraic sum of:

- Increase due to exchange-rate differences (€ 109.0 million);
- Increase due to capitalization of interest on the BNDES debt for € 12.4 million;
- Decrease due to the repayments scheduled in the amortization plans (€ 21.8 million);
- Decrease of the debts linked to foreign currencies due to appreciation of the Brazilian Real (€ 9.6 million).

Non-current financial liabilities

The table below shows the repayment period and average interest rate of non-current financial liabilities:

NON-CURRENT FINANCIAL LIABILITIES

In millions of Euro	December 31,2005	December 31, 2004	Repayment period	Average interest rate
CFH derivatives	17.8	18.9	2014-2016	2.5%
Trading derivatives	11.2	12.6	2007-2008	0.3%
Total	29.0	31.5		

This item carries the fair value valorization of the cash flow hedge derivatives and the trading derivatives (that is, those derivatives that do not qualify as hedging). In calculating the fair value, determined by actualizing the expected cash flows to the market interest-rate curve at the reporting date, the same method used in 2004 has been applied. The impact of trading derivatives is recognized in the income statement, while the fair value of cash flow hedge derivatives is reported in the balance sheet under financial liabilities and, the same amount with opposite sign is taken to a special equity reserve, without the variations in fair value having any impact on the income statement. The upward turn in the interest-rate curve, in the last months of 2005, generated an increase in fair value equal to € 1.1 million for cash flow hedge derivatives and € 1.4 million for trading derivatives.

Short-term loans

In order to meet cash requirements, in the month of December two drawdowns were made on the short - term credit lines for a total of € 55 million, accounted at the time of negotiations, at an average interest rate of 2.46%: € 25 million with maturity January 16, 2006 and € 30 million with maturity January 20, 2006.

Current financial liabilities

Current financial liabilities have increased by € 3.9 million compared to December 31, 2004 due to the total loan-related financial expense accrued and not yet paid. The table below provides a breakdown of the deferred liabilities according to the nature of the financial liabilities to which they refer:

In millions of Euro	Dec. 31, 2005	Dec. 31, 2004	Change
Deferred liabilities on			
- <i>hedging</i>	0.6		0.6
- <i>trading</i>	0.9		0.9
Total	1.5		1.5
Bond issue			
- 10 year	4.5	4.5	
- 20 year	7.0	7.0	
Total	11.5	11.5	
Loans	3.8	1.4	2.4
TOTAL	16.8	12.9	3.9

25) TERMINATION INDEMNITIES AND OTHER EMPLOYEE BENEFITS - Euro 168.2 Million

The Group awards benefits to its employees during their working life (e.g. loyalty bonus), upon termination of the employment relationship (e.g. employee termination indemnities, additional monthly salaries, allowance in lieu of notice) and after the employment relationship (e.g. energy discount, ASEM health care scheme). The benefits assigned during the working life (loyalty bonus) are awarded to the Group employees employed under the national collective bargaining agreement (CCNL) (including senior management) upon the reaching of set requirements in terms of length of service within the company (25th and 35th year of service). Benefits due upon termination of the employee relationship are awarded to all the subordinate employees (employee termination indemnities), to senior managers engaged or appointed up to the date of February 28 1999 (allowance in lieu of notice) and to employees (workers, office staff and middle managers) employed under the electricity sector CCNL, engaged at July 24, 2001 (additional monthly salaries).

The benefits due after termination of the employment relationship comprise:

- Tariff reduction on energy consumed for domestic uses, which is granted to all the Group employees employed under the electricity sector CCNL, engaged before June 30, 1996 (energy discount);
- Supplementary health care in addition to the national health service provided by the national collective agreement for industrial senior managers (Asem health care).

The table below provides a breakdown of the employee termination indemnities at December 31, 2005 and illustrates changes during the year:

In millions of Euro	Dec.31 2005	Dec. 31 2004	Acquisition TSO activities	Allocations	Utilizations and other changes
BENEFITS DUE DURING EMPLOYMENT RELATIONSHIP					
Loyalty bonus	3.9	4.8	0.6	-1.2	-0.3
Total	3.9	4.8	0.6	-1.2	-0.3
BENEFITS DUE UPON TERMINATION OF THE EMPLOYMENT RELATIONSHIP:					
- Employee termination indemnities	74.6	57.5	15.3	8.6	-6.8
- Additional monthly salaries	9.2	8.8	0.1	1.2	-0.9
Indemnities in lieu of notice and similar	2.3	1.7	1.8	-1.2	0.0
Total	86.1	68.0	17.2	8.6	-7.7
POST-EMPLOYMENT BENEFITS					
Energy discount	63.0	53.2	2.0	10.1	-2.3
ASEM	15.2	12.3	1.5	2.1	-0.7
Total	78.2	65.5	3.5	12.2	-3.0
TOTAL	168.2	138.3	21.3	19.6	-11.0

The items, equal to € 168.2 million at December 31, 2005 (€ 138.3 million at December 31, 2004), feature a € 29.9 million net increase compared to the previous year. This change essentially refers to transfer of the Parent Company for the energy discount (Euro 7,8 milioni).

	Empl. tm. indm	Notice indemnity	Additional mth sal.	Loyalty bonus	A.S.E.M	Electricity discount	Indemnity in lieu of electr.discount	Total
Liabilities								
at December 31, 2004	57.5	1.7	8.7	4.8	12.3	53.2	0.1	138.3
Service Cost	4.4	0.0	0.3	0.2	0.1	0.3	0.0	5.3
Interest cost	2.5	0.1	0.4	0.2	0.5	2.2	0.0	5.9
(Gains)/Losses	1.7	-1.4	0.5	-1.5	1.5	7.5	0.0	8.3
Actual allowances	-6.8	0.0	-0.9	-0.3	-0.7	-2.2	0.0	-10.9
Former GRTN activities	15.3	1.7	0.2	0.5	1.5	2.0	0.1	21.3
Liabilities								
at December 31, 2005	74.6	2.1	9.2	3.9	15.2	63.0	0.2	168.2

The following are the main assumptions used in the actuarial estimate of the liabilities for employee benefits:

	2005	2004
Discount rate	4.0%	5.0%
Labor cost growth rate	2.0% - 4.0%	3.5%
Health care cost growth rate	3.0%	3.5%

26) PROVISION FOR RISKS AND CHARGES - Euro 37.4 Million

	Provision for litigation	Provision for sundry risk and charges	Charges for retirement incentives	Total
Value at Dec. 31, 2004	14.2	21.7	4.9	40,8
Change in consolidation area		0.1		0,1
Accruals	0.9	11.1	7.1	19,1
Utilizations	-0.8	-19.4	-2.4	-22,6
Value at Dec. 31, 2005	14.3	13.5	9.6	37,4

Provision for litigation - Euro 14.3 million

Essentially in line with the previous year, this provision mainly refers to the Parent Company and is intended to cover potential liabilities existing at year end in respect of litigation or other disputes pertaining to company activity, assessed by also taking into account the advice of external and internal legal counsel. It does not include provisions for litigation for which a positive outcome is expected, nor provisions for which a potential charge cannot be reasonably quantified. The latter are described under "Off-balance-sheet items".

Provision for sundry risks and charges - Euro 13.5 million

Compared to the previous year, the provision records an € 8.2 million decrease attributable to the algebraic effect of the accruals (€ 11.1 million) and utilizations (€ 19.4 million) effected during the year:

- Release (€ 15.0 million) of the accruals made in previous year for network fees for the years 2002/03/04 pertaining to the prevailing dispute with the auto-producers of Cip 6 energy. This litigation was settled during the year further to the events specified below:
 - in 2005 the Council of State delivered various judgments by which it ruled that the GRTN's credit claim against owners of the Cip 6 production plants relating to the service of electricity transportation was inexistent;
 - AEEG then specified the procedures for covering said costs, thus causing Terna's claims against GRTN to become certain and collectible;
- Release (€ 1.5 million) of the accruals for contractual penalties to be paid in 2004 to Enel Distribuzione pertaining to the contract for maintenance of the HV lines owned by the latter, no longer necessary insofar as the counterparty has waived said item within the scope of renewal of said maintenance contract;
- Accrual referring to the long-term incentive plan (LTI) in favor of senior managers not included in the stock option plan (€ 3.7 million);

- Utilization for premiums linked to the options exercised by senior management on Enel shares (€ 2.6 million);
- Accrual (€ 6.0 million) referring to the “Projects for urban and environmental redevelopment” aimed at compensating the environmental impact of the construction of power lines;
- Accrual (€ 1.0 million) referring to the foreign subsidiaries for risks associated with the definition of higher indirect taxes.

Provision for early retirement incentives - Euro 9.6 million

The provision for early retirement incentives represents the estimated value of the extraordinary expenses related to the early consensual termination of employment of staff members who are entitled to a pension.

27) DEFERRED TAX LIABILITIES - Euro 467.7 million

The table below shows changes in deferred tax liabilities:

In millions of Euro	Dec.31, 2005	IMPACTS RECOGNIZED IN THE INCOME STATEMENT			
		Dec.31, 2004	Accruals	Utilizations	Other Changes
Accessory land	-3.8	-3.6	-0.2		
Employee benefits	-0.1	-1.0		0.9	
FVH derivatives	-36.0	-13.9	-22.1		
Adoption of Fair Value	34.7	13.8		20.9	
Delta fair value former TSO properties	-2.0				-2.0
Depreciation	-456.9	-464.0	-8.3	15.4	
Financial expense	-3.6	-1.3	-1.7		-0.6
Total	-467.7	-470.0	-32.3	37.2	-2.6

Compared to 2004, the provision records a € 2.3 million decrease chiefly owing to the combined effect of the following events:

- Utilization (€ 15.4 million) attributable to re-absorption of depreciation exceeding the deductible quota. This has increased considerably due to recent tax legislation on depreciation (Article 102-bis of the Consolidated Act on Income Tax) for assets included in the homogeneous categories of the electricity sector as determined by AEEG;

- Utilization of € 20.9 million entirely referring to the release of deferred taxes on the delta fair value at December 31, 2005 of the Parent Company's bond issue;
- Accrual of deferred taxes on the adjustment to year-end fair value on the fair value hedge financial instruments for € 22.1 million;
- Accrual of deferred taxes on the adjustment to fair value of the assets acquired with the acquisition of the TSO activities from GRTN (€ 2.0 million);
- Accruals effected by the Parent Company for € 8.3 million essentially attributable to the additional depreciation over and above the depreciation rates accrued in the year.

28) OTHER NON-CURRENT LIABILITIES - Euro 176.2 million

The increase in this item (€ 18.0 million) is essentially due to:

- € 14.3 million, as deferral of Parent Company revenues destined to cover future costs within the Safety Plan. Mention is made of AEEG resolution 05/04 which established that costs pertaining to the NTG safety plan are to be remunerated by a portion of the CTR tariff component; hence the deferral in question refers to the aforesaid portion of the CTR tariff component that will contribute to remuneration of future costs to be incurred in optimizing NTG safety;
- € 9.7 million referring to collection of the last portion of the contribution for the Italy - Greece interconnecting power line (occurring in the 1st half year) partially offset by the decrease due to the completion and subsequent start-up of the plant to which the contribution refers.

29) CURRENT LIABILITIES

The table below provides a breakdown of current liabilities at December 31, 2005:

CURRENT LIABILITIES

In millions of Euro	Dec. 31, 2005	Dec. 31, 2004	Change
Short-term loans*	55.0	0.0	55.0
Current portions of long-term loans*	58.3	47.0	11.3
Trade payables	951.4	183.6	767.8
Tax payables	14.4	12.1	2.3
Current financial liabilities*	16.8	12.9	3.9
Other current liabilities	104.9	50.5	54.4
Total	1,200.8	306.1	894.7

(*) Information on these items can be found in note 24. LOANS AND FINANCIAL LIABILITIES

Trade payables - Euro 951.4 Million

The table below provides a breakdown of trade payables at December 31, 2005:

In millions of Euro	Dec. 31, 2005	Dec. 31, 2004	Change
PAYABLES TO SUPPLIERS			
Payables to suppliers			
- Non-energy item payables	200.9	183.1	17.8
- Energy item payables	747.2	0.0	747.2
Payables to associated companies - Cesi	2.7	0.0	2.7
PAYABLES FOR CONTRACT WORK IN PROGRESS			
Payables for contract work in progress	0.6	0.5	0.1
Total	951.4	183.6	767.8

Payables to suppliers

- **Non-energy item payables**

Payables due to suppliers regard invoices received and to be received for contracts, services and purchases of material and equipment. The increase on the previous year (€ 17.8 million) is the result of purchases and services performed during the last period of the year for routine investment and operating activities.

The item also carries payables for services received from Enel Group companies (€ 32.6 million). These include the payable due to Enel Power Spa and Enel Power do Brazil equal to € 11.3 million and relating to the EPC contract stipulated with the subsidiaries (TSN and Novatrans).

- **Energy item payables**

This item carries the financial effects relating to the let-through costs, chiefly referring to procurement of energy and to transport fees due to the owners of the portions of the NTG.

- **Payables to associated companies**

This item, equal to € 2.7 million, records payables to the Company Cesi for services received by the Parent Company in relation to the construction and management of laboratories and plants for experimental tests, trials, studies and research concerning electrotechnics in general and technical and scientific progress. At December 31, 2004 this item was equal to € 1.7 million and was classified under payables to third parties insofar as the interest held in Cesi did not qualify it as associated company, as illustrated in paragraph 17. "INVESTMENTS ACCOUNTED FOR UNDER THE EQUITY METHOD".

Commitments undertaken with suppliers for the 2006-2011 period are equal to € 820.6 million and refer to contractual purchase commitments existing at year end and not included in the normal “operating cycle” and for the part not yet ordered.

Payables for contract work in progress

Contract work in progress, equal to € 0.6 million at December 31, 2005, is substantially in line with December 31, 2004, and breaks down as follows:

PAYABLES FOR CONTRACT WORK IN PROGRESS

In millions of Euro	Advances	Contract value	Balance at Dec. 31, 2005	Advances	Contract value	Balance at Dec. 31, 2004
Other	(5.3)	4.7	(0.6)	(4.6)	4.1	(0.5)
Total	(5.3)	4.7	(0.6)	(4.6)	4.1	(0.5)

Tax payables - Euro 14.4 Million

This item records the tax payables for the year (€ 136.6 million for Corporate Income Tax (IRES) and € 28.6 million in local tax (IRAP)), net of the advances totaling € 150.8 million paid in June and November 2005, exclusively referring to the Parent Company.

Other current liabilities - Euro 104.9 Million

A breakdown of other current liabilities is provided below:

In millions of Euro	December 31, 2005	Within the next year	Beyond the next year	December 31, 2004	Change
Advances	25.2	0.7	24.5	16.2	9.0
Other tax payables	14.4	14.4		11.6	2.8
Social Security payables	11.7	11.7		8.1	3.6
Payables to employees	21.9	21.9		12.7	9.2
Other payables	31.7	28.7	3.0	1.9	29.8
Total	104.9	77.4	27.5	50.5	54.4

Advances

This item carries the capital grants collected by the Parent Company for work underway at December 31, 2005. The value at December 31, 2004 was equal to € 16.2 million and the increase recorded during the year (€ 9 million) chiefly refers to grants received from third parties for works performed for connection to the National Transmission Grid.

Other tax payables

Other tax payables equal to € 14.4 million pertain to the extent of € 7.7 million to the Parent Company and essentially concern payables for withholding taxes equal to approximately € 4.9 million and to payables for registration taxes equal to € 2.8 million pertaining to the contract for acquisition of the TSO activities. The remaining portion, equal to € 6.7 million, relates to taxes and withholdings accrued by the subsidiaries TSN and Novatrans.

Social security payables

Payables to social security institutions are equal to € 11.7 million (€ 8.1 million at December 31, 2004) and chiefly refer to payables due from the Parent Company to INPS for the month of December 2005. The € 3.6 million increase compared to the previous year is influenced by the additional staff acquired by Parent Company further to acquisition of the TSO activities and those of the company RTL SpA.

Payables to employees

Payables to employees equal to € 21.9 million (€ 12.7 million at December 31, 2004) chiefly reflect the payables to employees for staff termination indemnities of the Parent Company, to be paid out to leavers by December 31, 2005 in addition to the staff incentives that will be distributed in 2006.

The sharp increase recorded, equal to € 9.2 million, is largely attributable to debit items entrusted to the Parent Company further to transfer of the TSO business activities

Other payables

Other payables, equal to € 31.7 million (€ 1.9 million at Dec. 31, 2004) chiefly refer, to the extent of € 23.5 million to discount items, arising with the acquisition of the TSO business activities, which will be recorded in the balance sheet and income statement when AEEG defines the allocation and/or relative beneficiaries and to the extent of € 3 million to the recording of guarantee deposits securing contractual obligations of the electricity market operators for dispatching contracts.

OFF-BALANCE SHEET COMMITMENTS AND RISKS

Environmental litigation

Environmental litigation relates to the installation and operation of electrical plants and, especially, to the effects of electrical and magnetic fields.

The Company is a defendant in a number of civil and administrative proceedings requesting the relocation of power lines or changes in operational conditions. The claims are based on the alleged health hazards posed by the power lines, even though they have been installed in full compliance with regulatory requirements. Only a very limited number of suits have been filed against the company seeking damages for personal injury caused by electromagnetic fields.

On July 8, 2003, a Prime Ministerial Decree was enacted to complete the implementation of Framework Law no. 36 of February 22, 2001. It establishes values for three parameters (exposure limits, thresholds of concern and quality targets) that electrical plants must meet. The decree had a favorable impact on pending disputes, because the scope of the framework law was limited to laying down general principles only.

Only a few adverse rulings have been issued against the company in this area and these have all been appealed (the cases are still pending). No claim for damages for personal injury has ever been upheld.

Legislation concerning electrical and magnetic fields

The relevant framework law, enacted on February 22, 2001, entrusts the state with the task of defining, through specific orders, the reference parameters (exposure limits, thresholds of concern and quality targets) with which electrical plants must comply.

Attention is drawn in this regard to the framework law on reclamation which establishes a mechanism for recovery of related expenses according to criteria defined by the Authority for Electricity and Gas, pursuant to Law no. 481/95, given that costs are incurred for common benefit. On August 29, 2003 the Prime Ministerial Decree of July 8, 2003 for the “Definition of exposure limits, thresholds of concern and quality targets for the protection of the population from exposure to electrical and magnetic fields at network frequency (50 Hz) generated by power lines” which established the values for the three parameters provided by the framework law, was published in the Official Gazette of the Italian Republic.

On regional legislation level, some regional governments have formulated bills governing the matter, which establish more restrictive limits compared to those prescribed by Prime Ministerial Decree 1992, and by the more recent Prime Ministerial Decree of July, 8 2003.

However it must be noted that on October 7, 2003 judgment no. 307 of the Constitutional Court was published and this declared some regional laws on the matter of electromagnetic fields to be constitutionally unlawful (amongst which the law of the Campania regional government no. 13 of November 24, 2001) It also established the principle that derogation from the state law is not permitted, even where this may involve higher standards being implemented by regional laws, as public health must be uniformly guaranteed throughout Italian territory.

Litigation relating to the GRTN business activities

It must be specified that, as far as litigation referring to events occurring up to the date of transfer and pertaining to the GRTN business activities of transmission and dispatching of energy ("Business Activities") according to the provisions of Article 1 of Prime Ministerial Decree of May 11, 2004, and of the transfer contract stipulated between Terna and GRTN on February 28, 2005, said litigation has not been transferred and hence every ensuing or related responsibility, charge or liability remains the concern of GRTN.

Terna, in its capacity as holder of the concession for transmission and dispatching activities from November 1, 2005, has been summoned in some trials appealing against orders of the AEEG and/or of the Ministry of Productive Activities and concerning the matter mentioned above. The Company has entered proceedings only in the cases in which the plaintiffs not only claim flaws in the opposed orders, but also Terna's alleged breach of the regulations issued by the aforesaid Authorities.

Other pending litigation

A number of legal disputes are pending in relation to urban planning and environmental issues associated with the construction and operation of a number of transmission lines. Adverse rulings could have repercussions, but since the impact cannot be quantified at present they have not been included under the "provisions for litigations."

For a limited number of cases it is not possible to completely preclude unfavorable rulings of which the

consequences could include not only the payment of damages but also the costs involved in modifying power lines and the temporary unavailability of the lines. In any case, an adverse outcome would not jeopardize the operation of the power lines.

An assessment of the suits, which included taking advice from external legal counsel, suggests that unfavorable rulings are however remote.

By way of Memorandum no. 63 of May 6, 2005, INPS ordered, with retroactive effect from 1999 onwards, that privatized state-owned industrial enterprises performing industrial activities be obliged to pay CIG, CIGS, DS and mobility contributions, which give rise to a burden in the region of € 24.8 million. Given the complexity of the matter, Terna and the other companies operating in the electricity sector first applied to the administrative court, requesting the annulment of the act, subject to prior suspension. The administrative court denied having jurisdiction, observing that the matter exclusively concerned rights rather than law. Hence Terna has now applied to the ordinary courts for declaratory judgment on the obligation to pay the contributions. The hearing has been set for October 3, 2006. Meanwhile INPS itself has deemed it necessary to request the opinion of the Council of State, suspending the payment of the contributions until said opinion has been delivered.

BUSINESS COMBINATIONS

Acquisition of TSO business activities

On February 28, 2005 Terna SpA and Gestore della Rete di Trasmissione Nazionale SpA (GRTN) signed the agreement for the transfer to Terna of the TSO business activities, comprising the activities, functions, assets and legal relationships as specified in Prime Ministerial Decree of May 11, 2004. The purpose of the agreement is to integrate the ownership and management of the electricity NTG (National Transmission Grid). The business activities transferred include approximately 586 resources, and comprise the following:

- Dispatching activities, or rather the management of the flows introduced into and withdrawn from the NTG in order to balance electricity supply and demand;
- Planning and development activities, or rather the definition of investment programs for upgrading the NTG.

Transfer of the TSO business activities from GRTN to Terna became effective on November 1, 2005.

The table below shows the amount, for each class of assets and liabilities, of the business activities acquired, immediately prior to combination:

In millions of Euro

Property, plant and machinery	64.9
Intangible assets	20.1
Equity investments	1.7
Non-current assets	0.8
Current assets	1.7
Total assets	89.2
Empl. term. indm and other empl. benefits	16.7
Non-current liabilities	14.5
Current liabilities	127.1
Total liabilities	158.3
SHAREHOLDERS' EQUITY	-69.1

The amount reported at the acquisition date corresponds to the above assets and liabilities valued on the basis of the relative fair value:

In millions of Euro

Net book value	(69.1)
- Concession	135.4
- Land and buildings	5.2
- Employee benefits	4.7
- Tax effects	(0.5)
Acquisition price of the TSO activities	66.3

The buildings acquired were revalued on the basis of an appraisal for a total of € 5.2 million together with the relative deferred tax effect equal to € 2 million. With regard to liabilities, the employee termination indemnities and the other benefits relating to transferred staff, were recorded on the basis of the present value of the obligations, reporting greater liabilities to the order of € 4.7 million. The relative prepaid tax asset calculated on this total was equal to € 1.5 million.

For transfer of the business activities under review the parties initially agreed upon a price equal to € 68.3 million, to be adjusted by approximately € 2 million according to the transfer situation. The difference, equal to € 135.4 million, between the price due from the Parent Company for acquisition of the TSO business activities from GRTN SpA (€ 66.3 million) and the fair value of the assets and liabilities acquired, was attributed to the value of the concession for the transmission and dispatching of electricity in Italy, previously issued by the Ministry of Productive Activities to GRTN and transferred to Terna at the time of acquisition of the TSO activities. As established by the Decree of the Ministry of Productive Activities of April 20, 2005, said concession is valid for twenty-five years.

Lastly it is specified that the costs directly attributable to the business combination refer to the charges for registration tax, equal to € 2.8 million, borne by the company Terna for registration of the transfer deed in question.

Acquisition of RTL

During the year the Parent Company launched the process for unification of the National Transmission Grid as provided by Law 290/2003 on the restructuring of the electricity sector and subsequent Prime Ministerial Decree of May 11, 2004, which led to acquisition of the company Acea Trasmissione, a company wholly owned by Acea, on October 1.

Specifically on August 8 Terna and Acea Spa (Acea) signed the contract for purchase on the part of the Parent Company of the entire share capital of Acea Trasmissione SpA (Acea Trasmissione). The deal was implemented, after approval of the Antitrust Authority was granted, on September 30 with effect from October 1, 2005.

The company took the name of Rete Trasmissione Locale (RTL) SpA and owns approximately 700 km of high voltage lines in Lazio, Umbria e Abruzzo.

The share capital, wholly owned by the Parent Company, is equal to ? 20.6 million represented by 20,600,000 ordinary shares of € 1 each.

The table below shows the amount, for each class of assets and liabilities, of the company under review, at the acquisition date:

In millions of Euro

Tangible and intangible assets	26.5
Non-current assets	1.9
Current assets	8.6
Total assets	37.0
Empl. term. indm and other empl. benefits	-0.7
Non-current liabilities	-0.4
Current liabilities	-3.0
Total liabilities	-4.1
SHAREHOLDERS' EQUITY	32.9

For transfer of the investment in Acea Trasmissione the parties agreed on a consideration equal to € 33.4 million. The difference between the price paid for acquisition of RTL and the fair value of the assets and liabilities acquired, equal to € 0.5 million, was attributed to goodwill.

It is specified that the amount of the income that may be consolidated with effect from the acquisition date (October 1, 2005) is equal to € 0.6 million.

TRANSACTIONS WITH RELATED PARTIES

With regard to the transactions implemented by the Terna Group this year, the related parties are represented by transactions with the associated company Cesi SpA.

The transactions implemented with the company Cesi SpA essentially concern the provision of services governed by specific contracts stipulated between the parties in accordance with the market conditions that would have been applied between two independent parties.

Specifically, the contracts generating expense chiefly refer to technical consultation, study and research, planning and experimentation services received by Terna and by the foreign subsidiaries, while the relations generating revenues essentially relate to rental of laboratories and other similar structures for specific uses.

The following table shows, in millions of euro, expenses and revenues for the year as well as receivables and payables outstanding at year-end.

In millions of Euro	ECONOMIC RELATIONS			FINANCIAL BALANCES		
	Revenues	Costs for the year	Investments costs	Receivables	Payables	Guarantees
Cesi SpA	0.2	1.8	1.6	0.1	2.7	0.8
Total	0.2	1.8	1.6	0.1	2.7	0.8

Guarantees refer to those received on the expense generating contracts stipulated.

Relations with the members of the Board of Directors and the Board of Statutory Auditors of the Parent Company in the year ending December 31, 2005 are shown in the table below:

Surname	Name	Office held	Period of office	Expiry of office	Office emolument	Bonuses and other incentives	Total
Roth	Luigi	Chairman/Director	Nov-Dec.05	Approval Fin. Statements2007	12,083.33		12,083.33
Cattaneo	Flavio	Chief Executive Officer	Nov-Dec.05	Approval Fin. Statements2007	(***)		
De Paoli	Luigi	Director	Nov-Dec.05	Approval Fin. Statements2007	7,916.67		7,916.67
Garaffo	Mario	Director	Nov-Dec.05	Approval Fin. Statements2007	12,916.67		12,916.67
Macri	Carmine	Director	Nov-Dec.05	Approval Fin. Statements2007	7,916.67		7,916.67
Maranesi	Piero Giuseppe	Director	Nov-Dec.05	Approval Fin. Statements2007	7,916.67		7,916.67
Ponzellini	Massimo	Director	Nov-Dec.05	Approval Fin. Statements2007	9,166.67		9,166.67
Smurro	Franco	Director	Nov-Dec.05	Approval Fin. Statements2007	7,916.67		7,916.67
Machi	Salvatore	Director	Jan-Dec.05	Approval Fin. Statements2007	42,450.00		42,450.00
Romano *	Massimo	Director	Jan-Dec.05	Approval Fin. Statements2007	28,750.00		28,750.00
Conti *	Fulvio	Chairman/Director	Jan-Nov.05		20,833.33		20,833.33
Mobili	Sergio	Managing Director	Jan-Nov.05		350,000.00	341,390.00**	691,390.00
Arnaboldi	Luca	Director	Jan-Nov.05		34,133.33		34,133.33
Cantarella	Paolo	Director	Jan-Nov.05		38,300.00		38,300.00
Croff	Davide	Director	Jan-Nov.05		38,700.00		38,700.00
Machetti *	Claudio	Director	Jan-Nov.05		34,533.33		34,533.33
Ruzzini*	Paolo	Director	Jan-Nov.05		34,133.33		34,133.33
Sardo*	Salvatore	Director	Jan-Giu.05		12,500.00		12,500.00
Total Directors' remuneration					700,166.67	341,390.00	1,041,556.67
Ferreri	Giovanni	Chair. Board of Stat. Aud.	Jan-Dec.05	Approval Fin. Statements2007	55,000.00		55,000.00
Corvace	Giancarlo	Auditor	Jan-Dec.05	Approval Fin. Statements2007	45,000.00		45,000.00
Tasca	Roberto	Auditor	Apr-Dec.05	Approval Fin. Statements2007	33,750.00		33,750.00
Franceschetti	Bruno	Auditor	Jan-Apr.05		20,250.00		20,250.00
Total Auditors' remuneration					154,000.00		154,000.00
FINAL TOTAL					854,166.67	341,390.00	1,195,556.67

* For the offices held the relative emoluments, for a total amount of € 130,750 were paid to Enel SpA

** This amount refers to a variable part of the fees referring to the year 2005, approved and disbursed in the course of 2005

*** Consideration has not yet been defined

All the above transactions were implemented at normal market conditions.

The table below provides a breakdown of the shares of the company Terna SpA directly held by the Parent Company's Directors:

DISCLOSURE ON THE SHARES HELD BY DIRECTORS AND THE STATUTORY AUDITORS

	Company in which interest is held	N. shares held at end of 2004	N. shares acquired in 2005	N. shares sold in 2005	N. shares held at end of 2005	Ownership title ⁽³⁾
Luigi Roth ⁽⁴⁾	Terna SpA	0	0	0	0	-
Flavio Cattaneo ⁽⁴⁾	Terna SpA	0	0	0	0	-
Luigi De Paoli ⁽⁴⁾	Terna SpA	7,805 ⁽⁵⁾			7,805 ⁽⁵⁾	property
Mario Garraffo ⁽⁴⁾	Terna SpA	0	0	0	0	-
Carmine Macrì ⁽⁴⁾	Terna SpA	0	0	0	0	-
Piero Giuseppe Maranesi ⁽⁴⁾	Terna SpA	0	0	0	0	-
Massimo Ponzellini ⁽⁴⁾	Terna SpA	2,000	0	0	2,000	property
Franco Smurro ⁽⁴⁾	Terna SpA	0	0	0	0	-
Salvatore Machì	Terna SpA	0	0	0	0	-
Massimo Romano	Terna SpA	12,000	1,200 ⁽⁶⁾	0	13,200	property
Fulvio Conti ⁽⁷⁾	Terna SpA	12,000			12,000	property
Sergio Mobili ⁽⁷⁾	Terna SpA	0	0	0	0	-
	RSN - Transmissora Sudeste Nordeste S.A.	1	0	0	1	property
	Novatrans Energia S.A.	1	0	0	1	property
Luca Arnaboldi ⁽⁷⁾	Terna SpA	0	0	0	0	-
Paolo Cantarella ⁽⁷⁾	Terna SpA	0	0	0	0	-
Davide Croff ⁽⁷⁾	Terna SpA	0	0	0	0	-
Claudio Machetti ⁽⁷⁾	Terna SpA	12,000	1,200 ⁽⁶⁾	13,200	0	property
Paolo Ruzzini ⁽⁷⁾	Terna SpA	12,000	0	0	12,000	property
Salvatore Sardo ⁽⁸⁾	Terna SpA	12,000	0	0	12,000	property
Giovanni Ferreri	Terna SpA	0	0	0	0	-
Giancarlo Russo Corvace	Terna SpA	0	0	0	0	-
Roberto Tasca	Terna SpA	3,000	0	0	3,000	property
Bruno Franceschetti ⁽⁹⁾	Terna SpA	0	0	0	0	-
Daniela Gallucci ⁽¹⁰⁾	Terna SpA	0	0	0	0	-
Fabrizio Orazi ⁽¹⁰⁾	Terna SpA	0	0	0	0	-

⁽³⁾ This column - added to the schedule of annex 3C provided by Article 79 of CONSOB resolution no. 11971/99 to provide the requested information - states if the interest is held under title of property, pledge, beneficial interest, deposit, borrowed security, etc

⁽⁴⁾ In office from November 2, 2005

⁽⁵⁾ Of which: 5,204 held personally and 2,601 held by spouse

⁽⁶⁾ Assigned as bonus share

⁽⁷⁾ In office until November 2, 2005

⁽⁸⁾ In office until June 30, 2005

⁽⁹⁾ In office, as auditor, until April 1, 2005

⁽¹⁰⁾ In office until April 1, 2005

SIGNIFICANT EVENTS AFTER YEAR-END

FTSE4GOOD Europe index

On March 10, 2006 confirmation occurred of inclusion of the Parent Company in the FTSE4GOOD EUROPE, the stock exchange index of the Financial Times Stock Exchange of London which gathers the top European companies which stand out in terms of sustainable economic growth.

EMTN (EUROPEAN MEDIUM TERM NOTES) PROGRAM

The Board of Directors of the Parent Company, with regard to the development investments scheduled in the industrial plan and related needs, passed a motion to draw on the capital market by setting up a framework program for future medium/long-term bond issues (EMTN - program) worth up to € 2 billion.

TRANSITION TO THE INTERNATIONAL ACCOUNTING STANDARDS (IFRS)

Preliminary considerations

As from 2005, the Terna Group has adopted the International Financial Reporting Standards, with IFRS transition date January 1, 2004. The last Consolidated Financial Statements drawn up in accordance with the Italian accounting principles are those relating to the year ended December 31, 2004.

As required by IFRS 1, this document contains the tables illustrating the reconciliation between the values stated previously in accordance with the Italian accounting principles and those reclassified in accordance with the IFRS, accompanied by the related notes commenting on the adjustments.

These tables have been drawn up exclusively for the purposes of the transition project for preparation of the first complete consolidated financial statements pursuant to the IFRS approved by the European Commission. As such they are without the comparative balances and the necessary explanatory notes which would be required for a complete representation of the equity-financial situation and the consolidated economic result of the Terna Group in compliance with the IFRS standards.

It is specified that in this document, some information on the effects of transition to IFRS, previously approved and published with the obligatory interim accounts at June 30, 2005 of the Terna Group, contained in the IFRS 1 reconciliation tables, have been reclassified and integrated, without however modifying the effects of transition on shareholders' equity at December 31, 2004 and in the Income Statement 2004.

The most significant accounting standards and policies used in drawing up the reconciliation tables are those described in the notes to the Consolidated Financial Statements at December 31, 2005.

IAS/IFRS Consolidated Balance Sheet at January 1, 2004 and at December 31, 2004

IAS/IFRS Consolidated Income Statement for the year ended at December 31, 2004

The balance sheet at January 1, 2004 and at December 31, 2004 and the income statement for the financial year 2004 are provided below and show:

- The balances according to the Italian accounting principles reclassified according to the IAS/IFRS formats;
- The adjustments for adaptation to the IAS/IFRS standards.

BALANCE SHEET AT JANUARY 1, 2004

In millions of Euro	Notes	Italian accounting principles reclassified as per IAS	IFRS_IAS conversion effect	IFRS_IAS
NON-CURRENT ASSETS				
Property, plant and machinery	1	4,195.8	9.4	4,205.2
Intangible assets		0.0		0.0
Goodwill		115.5		115.5
Pre-paid tax assets	3	22.3	23.9	46.2
Financial assets and other assets	4	12.8	1.1	13.9
Total non-current assets		4,346.4	34.4	4,380.8
CURRENT ASSETS				
Inventories		15.6		15.6
Trade receivables	5	213.5	0.1	213.6
Cash and cash equivalents		340.0		340.0
Other current assets		35.4		35.4
Total current assets		604.5	0.1	604.6
TOTAL ASSETS		4,950.9	34.5	4,985.4
NON-CURRENT LIABILITIES				
Loans	6	945.4	-6.8	938.6
Termination indemnities and other employee benefits	7	71.4	70.1	141.5
Provision for risks and charges	8	59.7	-9.9	49.8
Deferred tax liabilities	9	417.2	4.5	421.7
Non-current financial liabilities	10	0.0	10.6	10.6
Non-current liabilities		148.0		148.0
Total non-current liabilities		1,641.7	68.5	1,710.2
CURRENT LIABILITIES				
Current portions of long-term loans	11	0.0	6.8	6.8
Trade payables	12	232.5	0.1	232.6
Income tax payables		40.2		40.2
Other liabilities		70.1		70.1
Total current liabilities		342.8	6.9	349.7
TOTAL LIABILITIES		1,984.5	75.4	2,059.9
Share capital		2,036.1		2,036.1
Other reserves		709.7		709.7
Retained earnings (losses carried forward)	20	220.4	-40.9	179.5
Minority interests in capital and reserves		0.2		0.2
TOTAL SHAREHOLDERS' EQUITY		2,966.4	-40.9	2,925.5
		4,950.9	34.5	4,985.4

BALANCE SHEET AS OF DECEMBER 31, 2004

In millions of Euro	Notes	Italian accounting principles reclassified as per IAS	IFRS_IAS conversion effect	IFRS_IAS
NON-CURRENT ASSETS				
Property, plant and machinery	1	4,313.6	9.7	4,323.3
Goodwill	2	111.2	5.8	117.0
Pre-paid tax assets	3	14.8	36.8	51.6
Financial assets and other assets	4	6.3	42.0	48.3
Total non-current assets		4,445.9	94.3	4,540.2
CURRENT ASSETS				
Inventories		19.6		19.6
Trade receivables	5	157.4	0.5	157.9
Current financial assets		4.6		4.6
Cash and cash equivalents		231.8		231.8
Other current assets		34.8		34.8
Total current assets		448.2	0.5	448.7
TOTAL ASSETS		4,894.1	94.8	4,988.9
NON-CURRENT LIABILITIES				
Loans	6	2,090.1	-5.2	2,084.9
Termination indemnities and other employee benefits	7	61.1	77.2	138.3
Provision for risks and charges		40.8		40.8
Deferred tax liabilities	9	465.4	4.6	470.0
Non-current financial liabilities	10	0.0	31.5	31.5
Non-current liabilities		158.2		158.2
Total non-current liabilities		2,815.6	108.1	2,923.7
CURRENT LIABILITIES				
Current portions of long-term loans	11	0.0	47.0	47.0
Trade payables	12	183.1	0.5	183.6
Income tax payables		12.1		12.1
Current financial liabilities		12.9		12.9
Other liabilities		50.5		50.5
Total current liabilities		258.6	47.5	306.1
TOTAL LIABILITIES		3,074.2	155.6	3,229.8
Share capital		440.0		440.0
Other reserves	20	1,236.9	-12.7	1,224.2
Retained earnings (losses carried forward)	20	-3.0	-43.2	-46.2
Net income for the period net of the advances distributed	20	146.0	-4.9	141.1
TOTAL SHAREHOLDERS' EQUITY		1,819.9	-60.8	1,759.1
		4,894.1	94.8	4,988.9

INCOME STATEMENT AT DECEMBER 31, 2004

In millions of Euro	Notes	Italian accounting principles reclassified as per IAS	IFRS_IAS conversion effect	IFRS_IAS
Ordinary revenues		993.9		993.9
Other revenues	13	29.8	-3.7	26.1
Total revenues		1,023.7	-3.7	1,020.0
Raw materials		20.1		20.1
Services	14	127.4	2.4	129.8
Personnel costs	15	176.2	2.0	178.2
Amortization, depreciation and write-downs	16	161.7	-4.7	157.0
Other operating costs	17	71.9	-9.0	62.9
Capitalized costs		-22.5		-22.5
Total costs		534.8	-9.3	525.5
OPERATING INCOME		488.9	5.6	494.5
Financial expense	18	139.2	62.4	201.6
Financial income	18	59.7	42.0	101.7
Income before taxes		409.4	-14.8	394.6
Income taxes for the period	19	173.4	-9.9	163.5
Net income for the period		236.0	-4.9	231.1

Comments on the main IAS/IFRS adjustments made to the balance sheet items at January 1, 2004 and at December 31, 2004.

Brief notes on the main adjustments made to the individual items of the balance sheets at the beginning and end of 2004 are provided below.

Balance sheet items - Assets

1) Property, plant and machinery

(€ 9.4 million at January 1, 2004 and € 9.7 million at December 31, 2004). These adjustments refer to the reinstatement of the book value of land attached to electrical stations at its historical cost through the reversal of the related accumulated depreciation recorded in the financial statements. With regard to the year 2004, the adjustment is attributable to the reversal of the portion of depreciation pertaining to land. This approach is based on the assumption that the land has an unlimited useful life and, accordingly, is not subject to depreciation.

2) Goodwill

(€ 0.0 million at January 1, 2004 and € 5.8 million at December 31, 2004). This balance reflects the combined effect of reversal of the portions of depreciation for the period on goodwill generated at the time of the consolidation of the foreign equity investments (consolidation difference equal to € 4.3 million), given that, for IFRS purposes, it is no longer subject to systematic amortization but rather to periodic valuation (impairment test) and the increase recorded for adjustment of the same to the exchange rate at December 31, 2004 for a total of € 1.5 million.

3) Prepaid tax assets

(€ 23.9 million at January 1, 2004 and € 36.8 million at December 31, 2004). These reflect the balancing entry under balance sheet assets of the tax effects on adjustments made, mainly referring to post-employment benefits paid to employees (€ 24.1 million at January 1, 2004 and € 26.5 million at December 31, 2004) and to transactions in cash flow hedge derivative financial instruments (€ 3.5 million at January 1, 2004 and € 6.2 million at December 31, 2004).

4) Financial assets and other assets

(€ 1.1 million at January 1, 2004 and € 42.0 million at December 31, 2004). These refer to the recording in the balance sheet of the fair value of the derivative financial instruments held in the portfolio at January 1, 2004 (€ 1.1 million Novatrans exchange-rate fluctuation hedges) and at December 31, 2004 (€ 42.0 million fair value hedges on Terna Public Offer).

5) Trade receivables

(€ 0.1 million at January 1, 2004 and € 0.5 million at December 31, 2004). This item represents the re-determination of the net amount receivable referring to work in progress for third party contracts, relating to the periods under review, negotiated by the Parent Company. These values are offset by trade payables.

Balance sheet items - Liabilities

6) Loans

(-€ 6.8 million at January 1, 2004 and - € 5.2 million at December 31, 2004). This adjustment represents the reclassification of the current portions of long-term loans under current liabilities. As far as the change at December 31, 2004 is concerned, it also carries the adjustment to fair value of the bond issues (relating to the hedged portion) negotiated by the Parent Company (€ 41.8 million adjustment for Public Offer; - € 47.0 million current portions of loans reclassified under current liabilities).

7) Termination indemnities and other employee benefits.

(€ 70.1 million at January 1, 2004 and € 77.2 million at December 31, 2004). These adjustments are summarized in the table below:

In millions of Euro	Jan. 1, 2004	Dec. 31, 2004
Employee termination indemnities	-3.1	-2.9
"Energy discount" allowance	49.7	53.2
Other provisions	23.5	26.9
Total	70.1	77.2

These refer essentially to application of actuarial methods to the employee termination indemnities and to the recording of the current financial-actuarial value of the obligations relating to post-employment fixed-benefit programs.

8) Provision for risks and charges

(-€ 9.9 million at January 1, 2004 and € 0.0 million at December 31, 2004). The adjustment is entirely attributable to reversal of the portion of the provision for risks and charges which does not qualify for recording under the IAS/IFRS.

9) Deferred tax liabilities

(€ 4.5 million at January 1, 2004 and € 4.6 million at December 31, 2004). These reflect the balancing entry under balance sheet liabilities of the tax effects on the adjustments made, mainly referring to the employee termination indemnities and to the reversal of the accumulated depreciation on accessory land.

10) Non-current financial liabilities

(€ 10.6 million at January 1, 2004 and € 31.5 million at December 31, 2004). These refer to the recording in the balance sheet of the fair value derivative financial instruments held in the portfolio at January 1, 2004 (CFH interest rate hedges for EIB loans) and at December 31, 2004 (18.9 million CFH on EIB loans and 12.6 million trading derivatives).

11) Current portions of long-term loans

(€ 6.8 million at January 1, 2004 and € 47.0 million at December 31, 2004). This represents the reclassification of the current portions of long-term loans.

12) Trade payables

(€ 0.1 million at January 1, 2004 and € 0.5 million at December 31, 2004). This represents the re-determination of the net liability referring to work in progress for third party contracts. These values are offset by trade receivables.

Adjustments to the 2004 consolidated income statement items**13) Other revenues (-€ 3.7 million)**

Derive from the reinstatement of provisions for risks and charges no longer recordable on the basis of the IAS/IFRS standards and re-allocated under accumulated gains and losses. The specific amount refers to the reversal of the release to the income statement of the excess portion of the provision.

14) Services (€ 2.4 million)

As in point 13 above, this refers to the reversal of the use of the provision for risks and charges made during 2004 and, as already indicated in point 8 above, re-allocated under accumulated gains and losses at January 1, 2004.

15) Personnel costs (€ 2.0 million)

These refer to the adjustment of the provisions to the current value (financial-actuarial) of the obligations relating to post-employment fixed-benefit programs. The period adjustment is attributable to greater costs recorded.

16) Amortization, depreciation and write-downs (-€ 4.7 million).

The adjustment is essentially attributable to the reversal of depreciation of the goodwill generated at the time of the consolidation of the foreign equity investments (consolidation difference), given that, for IAS/IFRS purposes, it is no longer subject to systematic amortization but rather to periodic evaluation of impairments. It also comprises the reversal of depreciation referring to accessory land (- € 0.3 million).

17) Other operating costs (-€ 9.0 million)

These mainly concern the reversal of the charges attributable to the correction of errors noted during the period, reclassified and directly deducted from shareholders' equity in accordance with the retrospective method (- € 11.0 million). They relate to charges for the tax clean-up pertaining to operating grants which are in excess of the depreciation rates pertaining to years prior to 2003.

18) Net financial expense (€ 20.4 million)

The adjustment essentially comprises:

- The financial component deriving from actualization of benefits due to employees (€ 7.0 million);
- The net effect in the income statement of financial expense (€ 55.5 million) and income (€ 42.1 million) referring to derivative financial instruments (hedging and trading) held in the portfolio at December 31, 2004.

19) Income taxes for the period (-€ 9.9 million)

This amounts reflects the tax effects of adjustments to income statement items, as broken down below:

TAX EFFECT OF THE IAS ADJUSTMENTS

In million of Euro	1 st half 2004
Termination indemnities and other employee benefits	-2.2
Separation of land from buildings	0.1
Derivative instruments	-4.1
Provisions	-3.7
Total tax effects	-9.9

20) Statement of reconciliation of the shareholders' equity

As supplement to the reconciliation tables for the balance sheet and income statement illustrated above, the following table provides reconciliation of the shareholders' equity at January 1, 2004 and at December 31, 2004 and the 2004 net income, accompanied by comments relating to the adjustments made to the balances drawn up according to the Italian accounting principles.

In million of Euro	Notes	Shareholders' equity at Jan. 1, 2004	Shareholders' equity at Dec. 31, 2004	Income statement 2004
ITA Gaap		2,966.4	1,819.9	236.0
Tangible fixed assets and related depreciation	a	9.4	6.0	-3.4
Goodwill	b	0.0	5.8	4.3
Employee benefits	c	-70.1	-77.2	-7.1
Derivative financial instruments	d	-9.5	-31.3	-13.5
Provisions for risks and charges	e	9.9	3.8	-6.1
Other adjustments	f	0.0	0.0	11.0
Tax effects of adjustments	g	19.4	32.1	9.9
Total		-40.9	-60.8	-4.9
IAS / IFRS		2,925.5	1,759.1	231.1

a) Tangible assets and related depreciation

The international accounting standards provide that the item "land" is recorded in a separate asset class and is not subjected to depreciation. Accessory land, which was previously depreciated together with the asset standing thereon, has been incorporated and the related depreciation eliminated, giving rise to an overall positive effect on shareholders' equity at January 1, 2004 and at December 31, 2004, of approximately € 9.4 million and € 6.0 million, respectively.

b) Goodwill

As provided by IFRS 1, the net book value of goodwill recorded in the financial statements drawn up in accordance with the Italian accounting principles at the transition date, is periodically subject to impairment test and no longer subject to amortization.

Goodwill relating to acquisitions of equity investments in currencies other than the euro, is adjusted for IFRS purposes to the year-end exchange rates. The overall effect on the shareholders' equity at December 31, 2004 was positive to the extent of € 5.8 million.

c) Employee benefits

The IFRS identify "Post-employment benefits" among the various types of employee benefits. They represent the benefits due to employees upon termination of the employment relationship. In the fixed-benefit programs, the actuarial risk (that the benefits are lower than those expected) and the investment risk (that the assets invested are insufficient to meet the expected benefits) rest with the company rather than the employee. Therefore, it is necessary to record the current financial-actuarial value of the liability anticipated and the related costs and revenues, including financial expense and actuarial gains and losses. For the fixed-benefit programs implemented by the Terna Group, identified in the benefits associated with the termination indemnities, the Additional Monthly Salaries Allowance (IMA) and the Indemnity in lieu of Notice, the Loyalty Bonus and the Energy Discount (energy at a reduced tariff), measures were taken to "newly" record and valorize:

- Liability for the energy discount;
- Liability for the loyalty bonus.

and to assimilate the various valorization criteria for:

- Employee termination indemnities;
- Additional monthly salaries provision and the indemnity in lieu of notice.

The afore-mentioned adjustments have had a negative effect on the shareholders' equity at January 1, 2004 and at December 31, 2004 to the extent of approximately € 70.1 million and € 77.2 million respectively, and a negative effect on the 2004 income statement to the extent of approximately € 7.1 million.

d) Derivative financial instruments

In order to deal with the risk of fluctuation in interest and exchange rates, derivative contracts have been stipulated hedging both specific transactions and overall exposure. The IFRS establish specific rules for the accounting of these derivatives which differ from those provided by the Italian accounting principles.

Specifically, for derivatives hedging the risk of changes in future financial flows assigned to an asset, liability or future transaction (Cash Flow Hedge -CFH), the main effects can be seen:

- In the balance sheet recording of the fair value of the "derivative" asset/liability item;
- In the recording of the reserve for cash flow hedging, for the effective part of the hedge;
- In the booking to the income statement of the ineffective part of the hedge.

With reference to derivatives hedging the risk of changes in the fair value of the elements hedged comprising an asset or a liability recorded in the financial statements (Fair Value Hedge on interest rates), the main impacts can be seen:

- In the balance sheet recording of the "derivative" asset/liability item at its fair value;
- In the booking of the fair value delta attributable to the risk hedged adjusting the item hedged.

As far as "non-IAS hedging" derivatives are concerned, these are valued at fair value and the related effects are taken directly to the income statement.

This approach had a negative effect on the shareholders' equity at January 1, 2004 and at December 31, 2004, equal to € 9.5 million and € 31.3 million, respectively.

e) Provisions for risks and charges

The IFRS provide that the provisions for risks and charges must be stated only when a past binding event exists and the company has no realistic alternative other than to fulfill the obligation. The adjustment refers to the elimination of the provision for faults and the plant demolition provision which did not possess said characteristics, for a total of approximately € 9.9 million on the shareholders' equity at January 1, 2004 and approximately € 3.8 million on the shareholders' equity at December 31, 2004.

f) Other adjustments

This concerns the reversal of the charges attributable to corrections of errors noted during 2004, reclassified by direct deduction from shareholders' equity in accordance with the retrospective method.

g) Tax effect of adjustments

This originates from the tax effects of the adjustments to the income statement and balance sheet items generating a positive effect on shareholders' equity at January 1, 2004 and at December 31, 2004, of € 19.4 million and € 32.1 million, respectively.

Effects on the cash flow statement at December 31, 2004

The table of reconciliation of the consolidated cash flow statement has not been presented as the effects deriving from the application of the IAS/IFRS accounting standards have not produced any significant impact. The following table illustrates reconciliation of the net financial borrowings at December 31, 2004, involving the balances previously determined in accordance with the Italian accounting principles and those re-determined according to the IAS/IFRS.

In millions of Euro	Dec. 31, 2004
Net financial borrowings ITA Gaap	1,865.3
Application of amortized cost on Terna Bond issues	-7.1
Fair value delta calculated on the Bond issues hedged by fair value hedge transactions	41.8
NET FINANCIAL BORROWINGS IAS/IFRS	1,900.0

The net change reveals a € 34.7 million increase in financial borrowings, mainly attributable to the bonds issued by the Parent Company. Application of the amortized cost includes discounts and transaction costs directly attributable to the afore-mentioned loans no longer stated separately in the items provided by the Italian accounting principles.

Audit of the reconciliations required by IFRS 1

IFRS reconciliation of the balance sheet at January 1, 2004 and at December 31, 2004, and of the income statement for the financial year 2004, accompanied by the related notes, has been submitted to audit. The independent auditors KPMG SpA have completed their activities and the related report has been published together with this document.



REPORTS

REPORT OF THE BOARD OF STATUTORY AUDITORS ON THE CONSOLIDATED FINANCIAL STATEMENTS AT DECEMBER 31, 2005 OF TERNA SPA

To the Shareholders' Meeting of Terna SpA

The consolidated financial statements of the Terna Group at December 31, 2005 have been drawn up by the Parent Company, for the first time, in compliance with the provisions set forth in EEC Regulation no. 1606/2002, according to the international accounting standards (IAS/IFRS) and comprise the Balance Sheet, the Income Statement, the summary Statement, the Notes to the Financial Statements, the Statement of Cash Flows and are accompanied by the Directors' Report, with the specification that information on the events of greater significance in 2005, on Corporate Governance and other information, can be found in the Report on Operations accompanying the financial statements of Terna SpA. With specific reference to the Notes to the Financial Statements, the following is reported:

- the area of consolidation extends to the equity investments that are wholly owned, through the holding of all of the voting rights that may be exercised in Shareholders Meetings. Accordingly, the aforesaid area includes Terna SpA, in its capacity as Parent Company, the Brazilian subsidiaries Transmissoria Sudeste Nordeste S.A. and Novatrans Energia S.A. as well as RTL SpA
- in the consolidation phase the intergroup transactions, balances, revenues and costs have been eliminated and the equity investments in associated companies have been valued at equity. By contrast, the equity investments included in the consolidation area have been written off against assumption of the relative asset or liability, giving rise to a consolidation difference which is classified, pursuant to IFRS 1, as Goodwill.

The impairment test gives rise to a recoverable value of the aforesaid Goodwill which exceeds its book value.

The Notes to the Financial Statements also provide a clear account of the policies used in drawing up the financial statements, the accounting standards selected and applied to significant transactions, the

effects of transition to the international accounting standards, the nature and the economic and financial results of the transactions with related parties. The consolidated financial statements of the Terna Group provide indication of the balance-sheet format selected among those specified in IAS 1. Specifically, the Balance Sheet has been drawn up using the method by which assets and liabilities are classified as current and non-current, the Income Statement has been classified on the basis of the nature of costs, while the Statement of Cash Flows has been presented using the indirect method. Furthermore, for each item of the Balance Sheet, Income Statement, Statement of Changes in Shareholders' Equity and Statement of Cash Flows, the relative notes have been systematically prepared, as required by the international standard IAS 1.

To conclude, no significant facts worthy of mention hereunder have emerged.

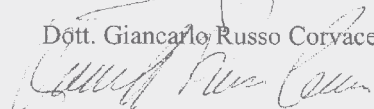
Rome, April 11, 2006

THE BOARD OF STATUTORY AUDITORS


Avv. Giovanni Ferreri



Dott. Giancarlo Russo Corvace



Prof. Roberto Tasca





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(Translation from the Italian original which remains the definitive version)

Report of the auditors in accordance with article 156 of legislative decree no. 58 of 24 February 1998

To the shareholders of
 Terna S.p.A.

- 1 We have audited the consolidated financial statements of the Terna Group as at and for the year ended 31 December 2005, comprising the balance sheet, income statement, statement of changes in equity, cash flow statement and notes thereto. These financial statements are the responsibility of Terna S.p.A.'s management. Our responsibility is to express an opinion on these financial statements based on our audit. These are the first set of consolidated financial statements prepared in accordance with the IFRS endorsed by the European Union.
- 2 We conducted our audit in accordance with the auditing standards recommended by Consob, the Italian Commission for Listed Companies and the Stock Exchange. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement and are, as a whole, reliable. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The consolidated financial statements present the prior year corresponding figures for comparative purposes prepared using consistent accounting policies. Furthermore, the section entitled "Transition to the International Financial Reporting Standards (IFRS)" of the notes to the consolidated financial statements discloses the effects of the adoption of the IFRS endorsed by the European Union and includes the disclosures on the IFRS reconciliation schedules required by IFRS 1. We audited such schedules, which had already been approved by the board of directors and published as an appendix to the half year report at 30 June 2005, and issued our report thereon on 13 September 2005.

KPMG S.p.A., an Italian limited liability share/capital company, is a member firm of KPMG International, a Swiss cooperative.

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 Capitale sociale
 Euro 5.798.620,40 i.v.
 Registro Imprese Milano e
 Codice Fiscale N. 00709600159
 R.E.A. Milano N. 512987
 Part. IVA 00709600159
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Terna Group
Report of the auditors
31 December 2005

- 3 In our opinion, the consolidated financial statements of the Terna Group as at and for the year ended 31 December 2005 comply with the IFRS endorsed by the European Union. Therefore they are clearly stated and give a true and fair view of the financial position of the Terna Group as at 31 December 2005, the results of its operations, changes in its equity and its cash flows for the year then ended.

Rome, 11 April 2006

KPMG S.p.A.

(Signed on the original)

Bruno Mastrangelo
Director

GLOSSARY

High voltage

Nominal voltage greater than 35 kV and less than or equal to 220 kV.

Extra high voltage

Nominal voltage over 220 kV.

Transmission activity

The activity of transporting and transformation electricity across the Grid.

Kilowatt-hour (kWh)

Unit of measurement that expresses the quantity of electricity equal to 1,000 Watts provided or requested in one hour.

Connection

Set of Grid elements consisting of the transmission line and the stalls at the ends of the same, including the relative circuit sectioning devices. Classification of connections by voltage level is carried out with reference to the nominal voltage. The length of the connection is normally the length of the line constituting the actual link.

Dispatching

Electricity cannot be stored. It is therefore necessary to continuously produce the quantity of energy requested by consumers and deliver it to the national transmission grid in such a way as to keep electricity supply and demand in equilibrium, thereby ensuring continuing and security in supplying this service. Management of these flows of electricity along the grid is known as Dispatching.

Requirement

Demand for electrical energy to be satisfied by the national electricity system. It shows a variable trend throughout the day, month and year.

Frequency

Represents the number of oscillations per second, during which the value of an alternating quantity, such as voltage, varies from positive polarity to negative polarity. It is measured in Hertz (Hz).

Generator

Electrical machine that transforms a source of primary energy into electricity.

Grid management

The set of activities and procedures that bring about operation and the operating plan, under every condition, of an electrical network. Said activities and procedures include the management of electricity flows, interconnection devices and the necessary auxiliary services, as well as the decisions for maintenance and development measures.

Unified management of the Grid

Coordinated management of all portions of the Grid.

Giga-watt (GW)

Unit of measurement equal to one billion Watts (1,000 megawatts).

Interconnection of electricity grid

Connection between electricity grids required for the transfer of electricity.

Interoperability of electricity grids

Operating method for the completion of management, operation, maintenance and development activities for two or more interconnected grids, in order to ensure simultaneous and coordinated functioning of the same.

Switch

Sectioning and manoeuvring device able to carry and interrupt current under normal operating conditions, as well as during specific exceptional operating conditions, such as in the case of short circuits.

kW

Unit of measurement of power (1kW=1000J/sec).

kWh

Unit of measurement of energy.

Connection line

Any power line that links the power distribution plant with the User's plant, or the power distribution plant with the connection station.

Interconnection line

High voltage power line in alternating current (AC) or direct current (DC) which links two different electrical transmission or distribution grids or even two generation plants.

Transmission Line

High and extra-high voltage power line, overhead or cable, used for the transport of electricity from the production plants to the distribution systems or to users.

Maintenance

Measures and intervention aimed at the maintenance or restoration of efficiency and proper functioning of electricity plants, taking into account any declines in performance.

Maximum total transport capacity on interconnection with foreign countries

Maximum transport capacity for importing along the lines of the interconnection grid with the electricity plants of neighbouring countries.

Medium voltage

Nominal voltage greater than 1 kV and less than or equal to 35 kV.

Megawatt (MW)

Unit of measurement equal to one million Watts.

Peak power

The highest value of electrical power supplied or absorbed at any point of the system during a specific time interval.

Producer

Natural or legal person that produces electricity, regardless of ownership of the generation plant.

Production

Generation of electrical energy, in any way.

Gross production of electricity

Sum of the quantities of electrical energy produced, measured at the electrical generator terminals.

Net production of electricity

Sum of the quantities of electrical energy produced, measured at the outgoing points of the production plants.

Planning

Definition of the usage plans, for a specific period of time, for the available means of production and transmission, in order to satisfy the energy requirements with respect to quality and continuity of service.

Operations planning

Preparation of plans and schedules for operation of the electricity system.

RAB (Regulatory Asset Base)

Value of the net capital invested, as recognised by the Italian Authority for Electricity and Gas for transport and distribution companies for the purposes of determining the applicable tariffs.

National transmission network (NTN)

National electricity transmission grid as defined by the decree of the Ministry of Industry of 25 June 1999 and subsequent amendments and additions.

Stall

Set of power plants and accessory systems linked to a power line or transformer that links said elements to the Grid with the busbars of a power station.

Switching station

Part of a grid consisting of the set of equipment used to distribute the electricity among the lines of a grid at the same level of voltage.

Transforming station

Part of a grid consisting of the set of equipment used to transfer electricity between grids with different voltages.

Power station

Part of a network, concentrated and closed within a specific site, used to distribute electricity among the lines of a grid, transfer electricity among grids at different voltages and transform electricity into the lowest voltage for the user.

Development

Intervention within the electricity grid involving an adaptation or expansion of the transport, transformation, connection and interconnection capacity, an increase in operating flexibility of the grid or a disposal of grid elements.

Transformer

Electrical machine used for the connection and transfer of energy between grids at difference voltage levels.

Transmission

Electricity transport and transformation activities along the interconnected high and extra-high voltage grid for the purposes of delivery to clients, distributors and recipients of self-produced energy.

Volt

Unit of measurement of voltage.

Watt

Unit of measurement of electric power.

Coordination and Development by Terna Spa

External Relation and Communication Department
Administration, Finance and Control Department

Editorial Design

Interno Otto, Rome

Photographs

All images are owned by Enel and Terna Spa

Andrea Sabatello
on pages 13, 15 e 21

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Printing

STI - Rome

Printed in July 2006
on Zanders ikono matt

1.000 copies

Publication not for sale

OUR FUTURE



INCREASING SERVICE EFFICIENCY AND COMPANY COMPETITIVENESS
ENHANCING OUR STAFF'S SKILLS AND OUR ENVIRONMENT
DEVELOPING AN INTERNATIONAL COMPANY PROFILE

