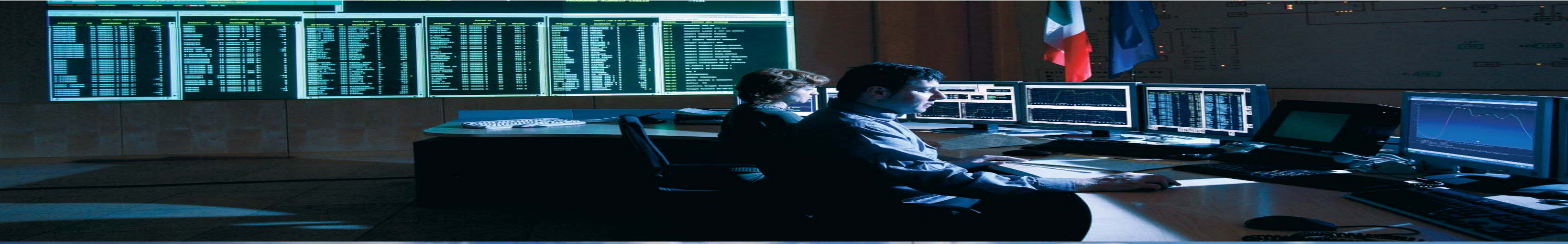



ANNUAL REPORT 2006

Terna
Rete Elettrica Nazionale

OUR PRESENT

PROVIDING SERVICES BASED ON CONCESSIONS AND GUARANTEEING
THEIR SAFETY, QUALITY, AND COMPETITIVE VALUE OVER TIME.
GUARANTEEING EQUAL ACCESS CONDITIONS TO ALL GRID USERS.
DEVELOPING MARKET ACTIVITIES AND NEW BUSINESS OPPORTUNITIES WITH EXPERIENCE
AND TECHNICAL KNOWLEDGE ACQUIRED THROUGH THE MANAGEMENT OF COMPLEX SYSTEMS.
CREATING VALUE FOR SHAREHOLDERS WITH A STRONG COMMITMENT TOWARDS PROFESSIONAL EXCELLENCE
AND WITH A SENSE OF RESPONSIBILITY TOWARDS THE COMMUNITY, WHILE RESPECTING THE ENVIRONMENT.

SEPARATE AND CONSOLIDATED FINANCIAL STATEMENTS 2006

Terna
Rete Elettrica Nazionale

A **grid** for supporting

Terna Rete Elettrica Nazionale is responsible in Italy for the transmission and dispatching of electricity on the high and extra high voltage electricity grid. Terna supports the country's development: it owns over 39 thousand kilometers of power lines, 97,6% of the total. Terna meets the electricity needs and provides the highest quality transmission service in line with the best European practices. The company guarantees all users equal access to the grid.


Terna A useful **grid** for the Country.

A **grid** for protecting

Protection also means safety and being defended from possible critical situations. Terna's task is to guarantee, 24 hours a day, 365 days a year, the transmission of electricity throughout Italy. The National Control Center in Rome safely manages each year over 330 billion KWh of electricity distributed throughout Italy. Furthermore, Terna publishes statistics on electricity in Italy and collects data relative to the major aspects of the national electricity sector.

Terna A useful **grid** for the Country.

A **grid** for implementing

Terna has planned investments for 3,1 billion euros as part of its development plan for 2006/2015. Over 130 million euros a year are invested in high technology. Infrastructures are built based on extensive research and outstanding know-how. In addition to 276 engineers working towards development, over 1.200 specialized technicians carry out complex operations such as the maintenance of the 380.000 volt lines. Professionals are trained at Terna, a unique school in Italy.


Terna A useful grid for the Country.

A **grid** for defending

Terna defends the grid's sustainable development. The procedure for strategic environmental assessment (SEA) was introduced in 2002 to identify, for the new lines, the best solutions shared by Institutions and territorial organizations. Terna also takes action with regard to materials and project's characteristics in order to find the best balance between development needs and environmental protection. Terna considers its Code of Ethics a founding element of its company identity and draws up its social and environmental sustainability report.


Terna A useful grid for the Country.

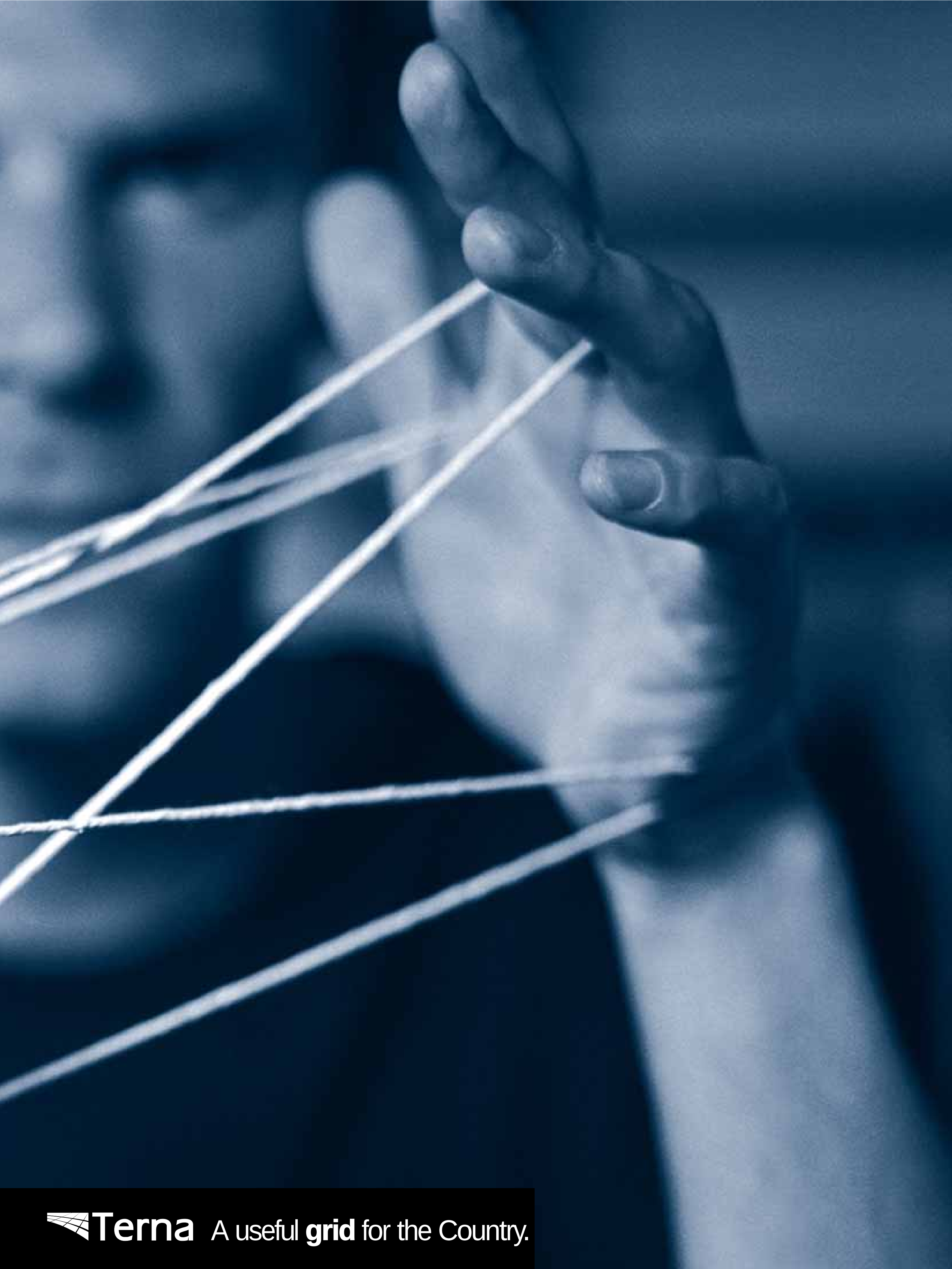
A **grid** for collecting

Terna has collected great results with the growth of the most important financial indicators. Objectives have been reached that have created value for shareholders and stakeholders through an attractive dividend policy, supported by stable cash flows. 2006 was an exceptional year for financial results and strategic objectives reached such as the company's listing in Brazil and the acquisition of other portions of the National Transmission Grid.

Terna A useful **grid** for the Country.

A **grid** for unifying

Terna's grid is linked to the network of European electricity grids. There are 18 extra high voltage lines to and from Europe that allow exchanging and regulating the balance of electricity with other countries. Terna also operates outside of the Italian territory. Since 2003, two subsidiaries in Brazil, grouped into Terna Participações, are entirely controlled by Terna which is listed in the San Paolo stock market and operates in the electricity transmission sector through 2.340 km of lines.


Terna A useful grid for the Country.

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CHAIRMAN'S MESSAGE

Dear Terna Shareholders and Stakeholders,

the 2006 Annual Report marks an important step for Terna, that of consolidation. Consolidation of a company that is already strong and rich in experience and value and that has entered the market with a new image and a renewed structure, with many projects to be implemented and to be communicated. We have come a long way to the present, essentially pursuing two objectives: the first has been that of strengthening Terna's presence and impact on the markets as an independent operator of the large electricity transportation grids, nationally and internationally. The second objective has been that of profoundly rethinking our mission and our values, to continue improving our relations with the community, the environment and the world surrounding us. We have also conceived a specific reference system for Terna for its human and professional conduct since our stakeholders continue to place the same trust in us as they did in the past, only more so.

To strengthen Terna's presence on the market and increase its impact, first of all we aimed at greater competitiveness and professionalism of those who work in our company. A combination of knowledge, experience acquired over the years in this sector that is significantly strengthened by the use of the most advanced technology. In these twelve months we have developed the national grid and undertaken many activities abroad, in particular in Brazil, through our subsidiary Terna Participações.
For us, developing the grid has a broad meaning: it does not only mean building new lines in addition to the existing ones. Building new plants allows to implement "rationalization" measures that call for dismantling parts of the grid with positive consequences in terms of environmental impact and the new plants have improved technical characteristics that replace the old ones. The past and present challenge, even more so for the future, is that of having an electricity system which is safer, more efficient and reliable. This is the essential condition for favoring national competitiveness to the benefit of enterprises and citizens and of the countries where Terna operates. A top priority challenge.

Rethinking our mission and our values was a key aspect in elaborating Terna's new ethical system. Several months of joint and coordinated work were required to draw up the new Code of Ethics, a milestone in the company's relations with stakeholders and the community. At the same time, a large commitment was undertaken in drawing up and publishing the first sustainability report that brought Terna to being reconfirmed in the ethical rating it had previously reached when it belonged to the Enel Group. Today we are working on the new edition, but above all we continue to improve our activity's environmental impact aspects. Even though we are pleased with the results, we are just as aware that sustainability, ethics, respect and responsibility are commitments to be pursued and enriched each day and are not merely transient superficial concerns.

Terna is a young, competitive company that has entered the market successfully and innovatively. It is responsible for an essential service: safely managing, 365 days a year, 24 hours a day, electricity flows on the national high voltage and extra high voltage transmission grid. At the same time, Terna aims at economic results and at creating value for shareholders. These two "souls" make Terna a strategic company for the country's interest, with a high and responsible socio-environmental profile; yet a company which also pursues industrial objectives and produces revenues for its shareholders.

We strongly feel this responsibility towards shareholders and all stakeholders, to the point that we have coined a slogan in the claim of our advertising campaign: "an asset for the country". We believe in this role and wish to continue being viewed this way.

The Chairman
LUIGI ROTH

LETTER TO SHAREHOLDERS

Dear Terna Shareholders and Stakeholders,

also in 2006 Terna demonstrated it was capable of achieving significant results, continuing to apply strategy aimed at operational excellence through improved efficiency, optimization of investments and of service quality; these are operational tools that combined with the consolidation of activities acquired with the TSO business activity and the professionalism of the men and women forming the company, have contributed and will continue to significantly contribute to the growth of the Group's value in the years to come. Moreover, all the objectives set at the end of 2005 were reached and surpassed, starting from those pertaining to service quality and grid reliability.

2006 was in fact characterized for Terna by highly significant company events that continue to increase its management responsibilities. On one hand, the consolidation - following the acquisition of the TSO business activity - of the obligations deriving from the status of being responsible for electricity transmission that have led to pursuing safety, reliability, efficiency and competitiveness objectives in the transmission and dispatching service pursuant to the concession and to the Grid Code, operating according to neutral and impartial criteria with respect to other entities of the electricity sector.

On the other hand, the acquisition of Edison Rete SpA and AEM Trasmissione SpA, owners of approximately 6% of the National Transmission Grid, as well as the success of the listing of the Brazilian companies on the stock market, have allowed fully expressing their value also providing the opportunity for accessing the local capital market, thus expanding future growth possibilities in the country while reducing Terna's exposure to direct risks.

The Group's revenues reached 1.307,8 billion euros, registering a 20,9% growth over 2005; the consolidated gross operating margin was equal to 899,9 million euros, with a growth of 25,6%. The operating results reached 687,5 million euros, registering a 27% increase. Net revenues reached 366,3

million euros with a 23% growth. These results, obtained also thanks to the significant contribution of the Brazilian companies, allowed us to propose a distribution of dividends that increased by 7,7% with respect to last year and at the highest levels of the sector.

Maintaining a high performance through an attractive dividend policy supported by the stable generation of cash flow, represents the most important commitment taken with the market by the new management of the Company, rendered even more interesting by the continuity of the Company's commitment to distribute dividends twice a year.

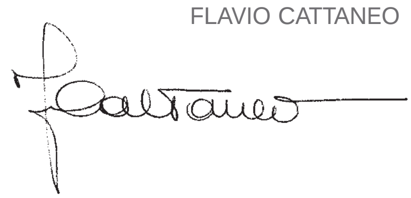
The solidity of assets and the limited risk level characterizing the Group continue to be confirmed by the evaluations expressed by the rating agencies Standard & Poor's and Moody's and Fitch.

Operational management will continue to be aimed at efficiency and quality service, constantly monitoring the level of costs and the quality of the best operators in the sector. Within the Industrial Program we have set ambitious operational, financial and strategic goals for the next five years aimed at maintaining the same quality service together with a high profits level for the Group.

Throughout 2007, we will continue the acquisition process of the remaining portions of the National Transmission Grid, while still pursuing business opportunities abroad with the objective of protecting and increasing the shareholder's profits with the same risk level.

The CEO

FLAVIO CATTANEO



CALLING THE ORDINARY AND EXTRAORDINARY MEETING

The Shareholders' Meeting is called in ordinary session for May 23 and 24, 2007, respectively in the first and second calling, at 11,00 in Rome, at the "Centro Convegni Matteo Ricci", Piazza della Pilotta, 4, and in extraordinary session is called for May 23, 24 and 28, 2007, respectively in the first, second and third calling, same time and same place, to discuss and vote on the following:

AGENDA

Ordinary Session

1. Appointment of two members of the Board of Directors.
2. Financial statement as of December 31, 2006. Reports of the Board of Directors, of the Board of Statutory Auditors and of the Independent Auditors. Relative resolutions. Presentation of the consolidated financial statement as of December 31, 2006.
3. Allocation of net earnings.
4. Appointment of the Accounting Audit.

Extraordinary Session

1. Amendment to Articles 14, 15, 21, 26 of the Bylaws; numbering of individual paragraphs forming the articles of the Bylaws.

Shareholders for whom timely notice was received by the Company through an authorized intermediary according to the terms of the existing law are entitled to attend the Meeting. Specifically, Art. 10.1 of the Bylaws envisages that the Meeting can be attended only by those who deposited shares at least two days prior to the date set for the first calling and have not withdrawn them prior to the Meeting.

Reports submitted by the Directors regarding the items on the agenda as pursuant to the existing laws and the proposal of the Board of Statutory Auditors with reference to the assignment of the auditors, will be made available to the public at the company registered office and at the headquarters of the Borsa Italiana SpA within May 8, 2007; shareholders may request a copy. This documentation will also be published in the Company's website: www.terna.it.

The appointment of the Directors will be made pursuant to Article 14.3 letter c) of the Bylaws.

In order to verify if they are entitled to participate in the Meeting, shareholders and others having the right to vote can submit documentation proving their entitlement to the Segreteria Societaria di Terna SpA by mail (Terna SpA - Segreteria Societaria - Via Arno 64 - 00198 Roma), also in copy, or via fax at no. 06/83138317, at least two days prior to the date set for the first calling of the Meeting.

To facilitate the verification of the powers they represent, those who wish to participate in the Meeting as legal representatives or as persons carrying out the will of Shareholders or of others having the right to vote must submit documentation proving their powers to the Segreteria Societaria di Terna SpA according to the terms stated in the previous paragraph.

The offices designed for identifying personnel and for verifying entitlement to participate in the Meeting will be open as of 9:00 a.m. on the dates set respectively for the first, second and third calling.

A Meeting assistance service is available for additional information at these numbers: 06/88345112 - fax n. 06/88345203.

The Chairman

LUIGI ROTH

THE NOTICE FOR CALLING OF THE ORDINARY SHAREHOLDERS' MEETING IS PUBLISHED IN THE OFFICIAL GAZETTE OF THE ITALIAN REPUBLIC, PART II°, N° 46 DATED APRIL 19, 2007

SUMMARY OF THE RESOLUTIONS PASSED BY THE ORDINARY AND EXTRAORDINARY SHAREHOLDERS' MEETING

The Ordinary and Extraordinary Shareholders' Meeting of Terna SpA met on second call on May 24, 2007 in Rome at the "Centro Convegni Matteo Ricci", Piazza della Pilotta 4, and:

- Approved Terna SpA's Financial Statement as of December 31, 2006;
- Examined the figures of the Consolidated Financial Statement of the Terna Group, referred to the period as of December 31, 2006, that closed with net profits for the Group equal to 366,3 million euros;
- Resolved to allocate the 2006 net profits of Terna SpA, equal to 355.757.526,68 euros, as follows:
  - 106.000.000,00 euros to cover the interim dividends paid on November 23, 2006;
  - 174.000.000,00 euros as the balance of the dividends to be distributed in the amount of 0,087 euros for each of the 2.000.000.000 ordinary shares to be paid - gross of any withholding taxes as envisaged by law - on June 21, 2007 with "registration date" of coupon n. 6 set on June 18, 2007. The total amount established may vary on the basis of the possible greater number of ordinary shares that are actually in circulation as of the date set for the coupon registration, relative to the balance of the dividends for the year 2006;
  - 75.757.526,68 euros or the amount that is left over after any other previous attributions as carry forward;
- Resolved to entrust the Board of Directors and for it its CEO, to verify in a timely manner, in relation to the exact and final number of shares to be remunerated, the total amount of the profits distributed and of the profits carried forward.

During the Ordinary Session, the Meeting also resolved the following:

- To appoint Board Members of the Company Vittorio Rispoli and Claudio Machetti, already co-opted by the Board of Directors respectively during the meetings held on July 13, 2006 and March 21, 2007;
- To approve the proposal made by the Board of Statutory Auditors and to assign through an extension to KPMG SpA, for the years from 2007 to 2010, the accounting audit already assigned to this company, according to the terms and methods proposed by the Board of Statutory Auditors.

During its Extraordinary Session, the Meeting approved amendments to Articles 14, 15, 21, 26 of the Bylaws connected to both the new law provisions regarding saving protection and to the guidelines from the Code of Self-Governance of Borsa Italiana.

The principal amendments concern:

- The appointment of Directors and Auditors, for which, notwithstanding the mechanism for competitor lists adopted according to the law on privatization, it was considered that the possibility that the Consob's regulatory action implementing law provisions on savings could foresee a different capital share for the submission of lists with respect to the amount established as at least 1%;
- Establishing the deadline for submitting the lists on the part of the members for appointing the administrative and control bodies in 15 days prior to the date set by the Meeting on first call and according to applicable existing regulations for submitting, depositing and publishing such lists;
- Introducing provisions aimed at guaranteeing that the formation of the Board of Directors respects the new independence and integrity requirements introduced by the law with the provision that requirements for integrity must exist for all the Board Members and that the requirements for independence must exist for at least one third of the Board Members in office;
- Introducing provisions aimed at guaranteeing that the formation of the Board of Statutory Auditors respects the integrity and professionalism requirements introduced by the law and the applicable rules referring to the maximum number of assignments for the Auditors;
- Appointing the Chairman of the Board of Statutory Auditors selecting the candidate from the minority list;
- Defining the modalities for the appointment and for the professional requirements of the Executive in charge of drawing up accounting and company documents;
- Attributing the power to call the meetings of the Board of Directors to at least one Auditor and of the Meeting, to at least two Auditors.

COMPANY BODIES

Board of Directors

Chairman

Luigi Roth

CEO

Flavio Cattaneo

Directors

Luigi De Paoli

Mario Garraffo

Claudio Machetti[1]

Salvatore Machì

Carmine Macrì

Piero Giuseppe Maranesi

Vittorio Rispoli[2]

Franco Smurro

Secretary of the Board of Directors

Ernesto Calaprice

Board of Statutory Auditors

Chairman

Giovanni Ferreri

Standing Auditors

Giancarlo Russo Corvace

Roberto Tasca

Alternate Auditors

Vito Di Battista

Bruno Franceschetti

Independent Auditors

KPMG SpA

(1) Co-opted on 21 March 2007 to replace outgoing Director Massimo Romano.
(2) Co-opted on 13 July 2006 to replace outgoing Director Massimo Ponzellini.

POWER STRUCTURE

Board of Directors

The Board of Directors is vested by the Bylaws 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 necessary for the implementation and achievement of the corporate purpose, excluding only those acts which the law and the Bylaws reserve for the Shareholders’ Meeting.

Chairman of the Board of Directors

Pursuant to the Bylaws, the Chairman is empowered to legally represent the Company and sign on its behalf, chair the General Meeting, call and chair the Board of Directors Meetings and verify the implementation of the resolutions of the Board. On the basis of Board resolution dated November 2, 2005, the Chairman is also acknowledged particular powers of a non-operational nature.

Chief Executive Officer

Pursuant to the Bylaws, the Chief Executive Officer is also empowered to legally represent the Company and sign on its behalf and is also vested, on the basis of 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 Bylaws or reserved for the Board of Directors pursuant to the same resolution.

TERNA'S MANAGEMENT

From left to right:

1. FRANCESCO DEL PIZZO Dispatching and Conduction Director **2.** LUIGI DE FRANCISCI Regulatory Affairs Director **3.** GIACOMO DONNINI Planning Manager and Energy Operations **4.** LUCA D'AGNESE Italy Operations Director **5.** STEFANO CONTI Institutional Affairs Director **6.** GIOVANNI BUTTITTA External Relations and Communication Director **7.** ELISABETTA COLACCHIA Investor Relations Manager **8.** CESARE RANIERI Human Resource and Organization Director **9.** UMBERTO COLONNA Plant Maintenance Director **10.** GIUSEPPE LASCO Company Safety Director

11. FLAVIO CATTANEO Chief Executive Officer **12.** LUIGI ROTH Chairman, **13.** LUIGI CELANI Procurement Director **14.** FILOMENA PASSEGGIO Corporate Secretary and Legal Department Director **15.** LUCIANO DI BACCO Administration and Fiscal Manager **16.** EVARISTO DI BARTOLOMEO Engineering Director **17.** FABIO TODESCHINI Chief Finance Officer **18.** GIANNI ARMANI Grid Planning and Development Director **19.** FULVIO DE LUCA Internal Audit Manager **20.** CARLO SABELLI Dispatching Manager **21.** ALESSANDRO FIOCCO Business Development and International Director

THE TERNA GROUP

The Company

Terna is a major grid operator for the transmission of electricity. It is the principal owner of the National Transmission Grid for high voltage electricity with over 97% of the national electricity infrastructures (as of 31.12.06). It is also responsible for transmission and dispatching of electricity throughout the national territory and also for the safe management, 365 days a year, of the balance between demand and supply of electricity. The Company is also responsible for the Grid's planning and development activity, for its maintenance and development while respecting the environment and combines experience with technology to improve its efficiency.

Terna SpA is listed in the Italian Stock Market since 2004. Presently, its majority shareholder is Cassa Depositi e Prestiti with a shareholding of 29,99%. 68% of the corporate capital is owned by Italian companies while 32% is held by foreign funds. The Company's principal shareholders include Enel, Assicurazioni Generali and Pictet Asset Management SA accounting for 5%, Barclays Global Investors LTD and Barclays Global Investors NA accounting for 2%. The remaining 51% approximately is divided among institutional and retail investors. This shareholding structure guarantees the company's mission at its best; on one hand, guaranteeing –through third parties- a general interest service such as the transmission of electricity, and on the other, creating value for its shareholders by focusing largely on results.

An International Group

Terna is an international Group: it has consolidated its position worldwide and is one of the most important players of the sector, the second Transmission System Operator in Europe in terms of strategic assets. The Terna Group operates within the electricity transmission sector in Italy and Brazil, provides consulting services abroad to other grid operators and evaluates development opportunities in other countries, consistently with its own activities and with particular attention to the quality of services offered and to the economic and financial efficiency. Furthermore, Terna also belongs to the Union for the Coordination of Transmission of Electricity (UCTE), one of the most important associations in the world in this sector that coordinates electricity transmission in continental Europe. 36 electricity grid operators belong to the UCTE from 23 European countries with the main objectives of guaranteeing the safety of interconnected electricity systems.

In Italy, Terna owns the high voltage electricity National Transmission Grid with over 97% of the country's electricity infrastructures (as of 31.12.06). In particular, Terna owns:

- 39.056 km of lines
  - 380 kV lines: 9.587 km
  - 220 kV lines: 9.753 km
  - Lines <150 kV: 19.716 km
- 357 transformation and distribution stations
- 3 remote plant operation centers
- 18 interconnection lines with other countries

The elements that form the grid are: EHV transformers (extra high voltage) that collect electricity from the national electricity plants (or from border points for imported electricity); the EHV and HV lines (high voltage) that transport electricity; and lastly, transformation stations that give electricity to the distribution companies which in turn (through sales companies) bring electricity to homes and industries.

Abroad, **Terna** controls **Terna Participações SA**, a company that is listed in the San Paolo Stock Market and that operates in the electricity transmission sector in Brazil through its two subsidiaries Trasmissione Sudeste Nordeste (TSN) and Novatrans. The Brazilian Group operates through thirty-year concessions in planning, construction, operation, maintenance and development of the country's high voltage electricity grid portions. With over 2.400 km of lines connecting the areas of the center and north of Brazil, Terna Participações SA is the second private electricity transmission company listed in terms of Brazilian market share with 8,2% of the total revenues of the sector. From the technical and operational points of view, it stands out for its high quality standards and for its excellent service performance levels. Following the listing of Terna Participações in the San Paolo Stock Market last October, the Group aims at further consolidating its presence in Brazil by assessing other business opportunities in the country.

The 2.447 km of 500 kV lines and the 12 sub-stations are divided and managed as follows:

- 1.169 km and 6 sub-stations managed by TSN
- 1.278 km and 6 sub-stations managed by Novatrans

Growth opportunities abroad

Terna evaluates development opportunities abroad through strategic initiatives and possibilities in line with the Group's growth objectives. Strategic initiatives are carried out in areas that represent a natural expansion of present activities: first of all, in the Balkans, Eastern Europe and Brazil. The Balkans represent a possibility of exploiting opportunities created by private investments in electricity transmission and to favor underwater interconnections in the Adriatic; in Brazil, pursuing the strategy that led to the listing of Terna Participações in the Stock Market.

Initiatives are considered opportunities when they regard investment possibilities with adequate returns according to the risk profile and a limited direct financial exposure for Terna in countries that offer socio-economic and regulatory stability.

Terna's History

Terna - Rete Elettrica Nazionale SpA has been for years an industrial and service company for the country. The changes within the electricity scenario over the last years, including the process of deregulation of the electricity market, the privatization of the grid, the appearance of a variety of market competitors in Italy and abroad, once again allowed Terna to be among the leading players of the national electricity sector. The unification between ownership and management of the National Transmission Grid, which was effective as of November 1, 2005 and the appointment of the new Board of Directors and of Luigi Roth and Flavio Cattaneo, respectively Chairman and Chief Executive Officer, marked the beginning of a new route which was traced many years ago.

The principal stages of its recent history are summarized below:

May 31, 1999: Terna SpA is established within the Enel Group through the implementation of Italian Legislative Decree no. 79/99 (Bersani Decree) which within the process of deregulation of the Italian electricity sector, ratified the separation between ownership and management of the National Transmission Grid. Terna's activities, operative as of October 1 of the same year, concern the operation and maintenance of the Enel Group plants belonging to the National Transmission Grid and the development of the grid according to the guidelines issued by the Grtn (National Transmission Grid Operator).

May 11, 2004: the Prime Minister's Decree is issued which establishes the criteria, formalities and conditions regarding the unification between ownership and management of the National Transmission Grid and the corporate governance system.

June 23, 2004: 50% of Terna SpA's share capital is listed in the Italian Telematic Stock Market.

September 15, 2005: Enel transfers 29,99% of Terna SpA's corporate capital to the Cassa Depositi e Prestiti: the shareholding structure of the company adopts the present structure.

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

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

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

Energy Framework

In the past twenty years the electricity demand has been in constant growth also when the country's economic development was at a low. In the next ten years a further steady growth is expected (+2,2%), connected on one hand to a partial economic recovery with respect to the previous years, and on the other, to maintaining the same development rate of electricity intensity. Peak consumption increases, mainly referred to domestic and services uses, are owed to the use of air conditioners and to the cold chain in the summer and to climatic conditions in the winter. It is expected that in the next ten years consumption will increase by 100 billion kWh. In the past years we have witnessed a marked acceleration in building more modern and efficient new power plants. We are speaking of approximately 7.000 MW that already went into operation and of an additional 14.000 that are scheduled to be added in the next years.

These are significant figures that indicate the extent of a development process underway that has already produced benefits regarding greater safety and that in the future will also produce economic advantages.

A top priority: developing the grid

Transmission grids in many countries suffer development and investment delays with respect to the changed needs of power systems; in Italy, however, this appears to be stronger than elsewhere. The use of the transmission grid, measured in the ratio between transported power and the grid's extension, has increased in the past 30 years by 60% in Italy, while in the rest of continental Europe it has grown only by 5%. The causes for this lie both in the significant delay in building new transmission lines and in the constant increase of electricity consumption. The increased use of electricity infrastructures has not been met with an adequate modernization and development process. The electricity grid's development rate in Europe over the past 30 years has registered an average 2,5% increase, while in Italy the growth in kilometers of long distance power lines registered 1,2%.

The electricity market needs more grid infrastructures to allow competition among production plants that are also distant from consumption centers.

Most of the authorized plants or those being built are located in the north-west and in the south of the country, in areas that are already congested. If adequate connections do not exist between these two extremes, the grid's bottleneck will prevent transmitting electricity where it is needed (limited production areas).

Developing the National Transmission Grid is a top priority and represents a present challenge which Terna is committed to meeting with the greatest effort, while pursuing objectives that guarantee a service for the community in a neutral and independent way and also seeking economic results by creating value for shareholders.

The results are visible

Revenues and earnings grew in 2006, respectively of 20,9% and of 23% with respect to the same period for 2005; the volume of investments increased by 29%. Various works have also been added to these figures, the main ones being:

- 1. the 380 kV "Matera-Santa Sofia" line (218 km between Basilicata and Campania)
- 2. the 380 kV long distance power line "Laino-Rizziconi" (215 km), in Calabria (October 2005)
- 3. the connection between Sardinia and Corsica (SAR.CO.), for a total of 31 km (January 2006)
- 4. the 380 kV "Turbigo-Rho" line (26 km), in Lombardy

Furthermore, an important project, the SAPEI, is being carried out between Sardinia and the Italian peninsula (420 km). An underground cable (1.600 m under sea level) will be placed representing the greatest depth ever reached for an underground cable. After years, the electricity grid is being built again. Development activity is aimed at:

- improving reliability, quality, efficiency and economic competitiveness of the electricity system
- increasing safety and continuity of power supplies

Developing the grid only within the national territory is not enough. Imported electricity (that covers 15% of the Italian requirements) owing to lower European prices represents an economic advantage for both industries and families. Together with the objective of promoting the creation of a European electricity market, this highlights the need for developing new interconnection with other countries.

Building new electricity interconnection infrastructures with other countries, in particular with the Balkan countries and north-African Mediterranean countries would represent a possibility not only for receiving electricity at significantly lower costs, but also for increasing safety of supplies both in terms of greater availability as well as in terms of greater geopolitical diversification.

Within this context, Italy will play an increasingly strategic role. International development opportunities will make our country an ideal platform for the creation of an electricity hub. For this reason Terna has conducted feasibility studies for new connections with the Balkan countries and the Mediterranean.

A sustainaible business model

During 2006 Terna strengthened its commitment in its corporate social responsibility relying on experience acquired in the past within a large group to define and create its own independent program. At the bottom of this program a sustainability objective lies: build and maintain over time a relationship based on trust with all the stakeholders that is essential for improving medium-long term performance.

A first important step was taken with the adoption of the new Code of Ethics approved by the Board of Directors in December 2006. The new Code, fine-tuned with the contribution of several managers that shared their direct knowledge of ethical problems related to management, was drawn up according to Terna's new operational status and indicates the principles and guidelines to be followed and referred to on an every day conduct basis. Consistently, with the objective of generating trust, the establishment of conduct criteria towards stakeholders was based on considering their expectations towards Terna. In the near future, the Code and its application will be the subject of assessments carried out together with the principal categories of stakeholders.

Furthermore, with the defining of the Code of Ethics, the first Sustainability Report was also drawn up that included the activities carried out in 2005 and programs and commitments that Terna intends to carry out within its ethical approach. The Report attributes a role of primary importance and of responsibility to the electricity service joined by economic, environmental and social responsibilities.

2006 has represented the first test for Terna's social responsibility commitments. Activities and projects will be illustrated in the second edition of the Sustainability Report. Below some of the main points are listed:

- in the environmental field, the grid's development activities have continued to pursue a constructive approach that Terna systematically adopts in its relations with the local institutions. Thanks to this approach, the environmental aspects tied to the construction of new lines and stations - for example the respect of protected areas, inclusion into the artistic context and landscape - are integrated in the early planning phases with the aim of minimizing their environmental impact. In order to extend the environmental focus in a structured way also to grid management and maintenance operations, an environmental management process has been initiated based on the ISO 14001 criteria with the objective of obtaining certification in 2007;

- in the social field, the commitment to place greater value on human resources was confirmed also through training initiatives that involved 87% of the staff for a total of over 118.000 training hours. Terna also significantly increased its contribution to initiatives having a social, cultural and charity nature.

Our values

The new Code of Ethics reflects the transformation that has made Terna an autonomous operator in the electricity transmission market.
Values and principles that have always been present within the company were strengthened and joined with new conduct criteria that specifically determined relations with stakeholders.

THE CODE IS BASED ON THREE GENERAL PRINCIPLES:
lawfulness since respecting the law is mandatory
honesty that implies refusing corruption in every form
responsibility for one's own actions,
also towards the community and the environment

TERNA RECOGNIZES FOUR PRINCIPLES AS BEING PARTICULARLY SIGNIFICANT:
sound business management
respect personal and professional
equal treatment
transparency in conduct and in communication

Terna's numbers

Numbers can be important for understanding the extent and the activity of a company. Below the most important numbers are listed for understanding how Terna works: :

0,4	Km, the length of the shortest 380 kV line ("Ostiglia-Ostiglia C.le", in Lombardy)
1	National Control Center
1	Main headquarters in Rome
1	Subsidiary in Brazil
2	Subsidiaries in Italy
2	Sub-marine interconnection lines (Italy-Greece and Italy-Corsica)
3	Remote Control Centers
8	Territorial Operational Areas (AOT)
9	Percentage of women employees
18	Interconnection lines along the northern border
30	Percentage of Total Shareholder Return
46	Average age of employees
73	Wires inside a conductor or electrical cable
91	Percentage of male employees
95	Millions of euros earned by Terna SpA from the stock market listing in Brazil of Terna Participações
97	Percentage of ownership of the National Transmission Grid

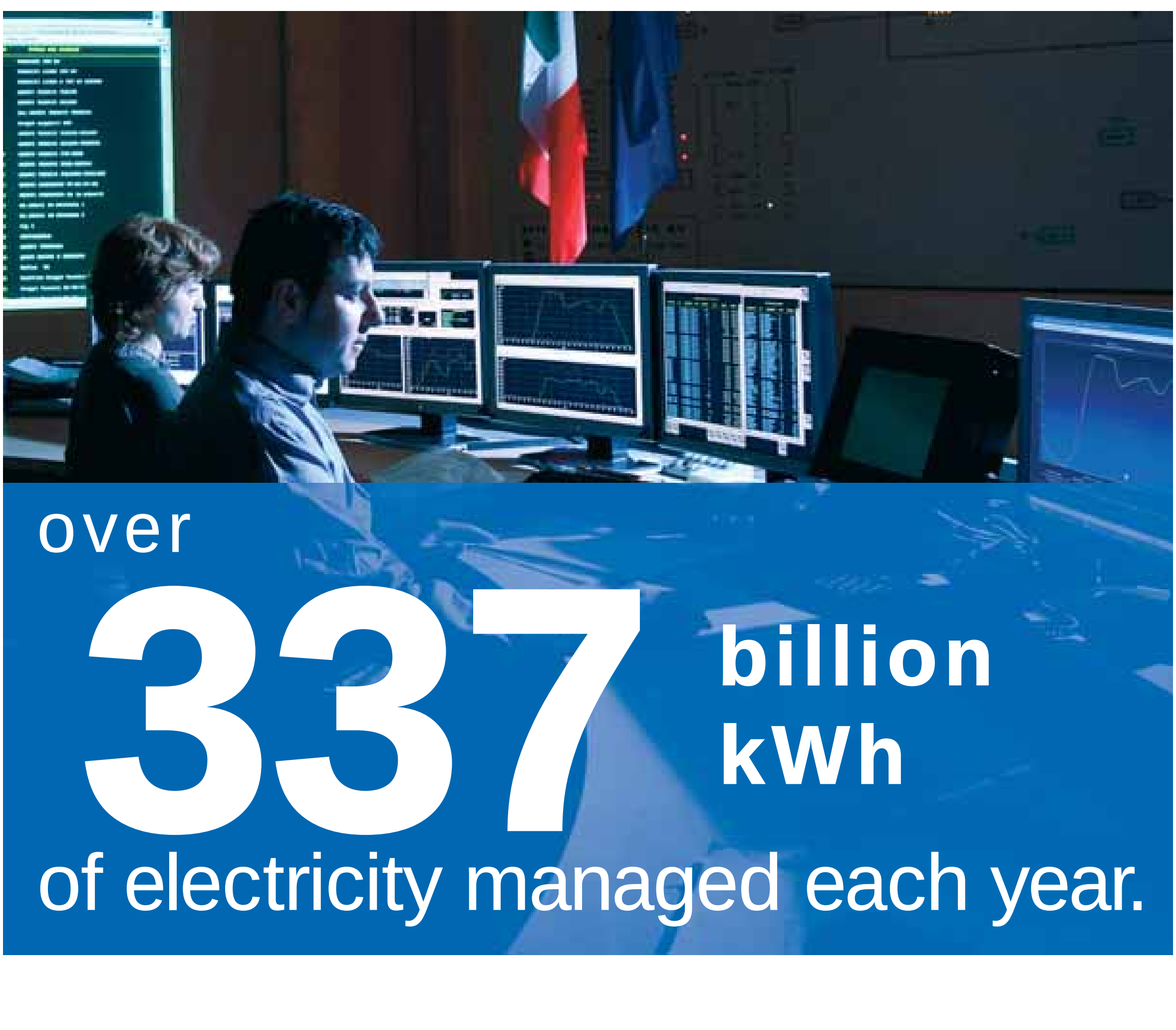
218	Km in length of the longest 380 kV line (“Matera-Santa Sofia”, between Puglia, Basilicata and Campania)
276	Engineers
337,8	Billions of KWh demand in Italy in 2005
357	Transforming and switching stations
595	Transformers
1.000	Megawatt transportation capacity of the most powerful lines
1.098	Blue-collar workers and specialized technicians
1.600	Meters below sea level, the depth of the SaPei sub-marine cable (between Sardinia and the Italian peninsula)
3.555	Employees (Italy and Brazil)
4.316	Bays
9.753	Km of 220 kV lines
9.587	Km of 380 kV lines
19.716	Km of 150 kV lines
39.056	Km of total transmission lines (approximately 3 times the world’s diameter)
55.620	Megawatt representing the national requirement on June 27, 2006 (record high)
114.145	MVA (MegaVoltAmper) of transformation capacity
600.000	Tons of iron of the pylons that form the Terna SpA grid (82 times greater than the quantity of iron used for the Eiffel tower)
2.000.000.000	Investments in euros envisaged in the Strategic Plan 2006-2010
2.200.000.000	IPO value of Terna Participações at the San Paolo, Brazil Stock Market

TERNA HIGHLIGHTS

The National Control Center

The core unit of the entire Italian electricity system

Located just outside of Rome, it represents the heart of the national electricity system. The central department can exert a capillary control while also having a global vision of the entire high voltage and extra high voltage grid that transmits electricity to all the regions of Italy. This department controls instant by instant the flow of electricity produced in our country and imported from abroad; it is here that every day the transmission of electricity is safely managed taking action where necessary to balance the demand and supply of electricity. Monitoring and managing electricity flow occurs at a constant pace, 24 hours a day, 365 days a year, for over 337 billion KWh a year.



The Organization

Structure and human resources

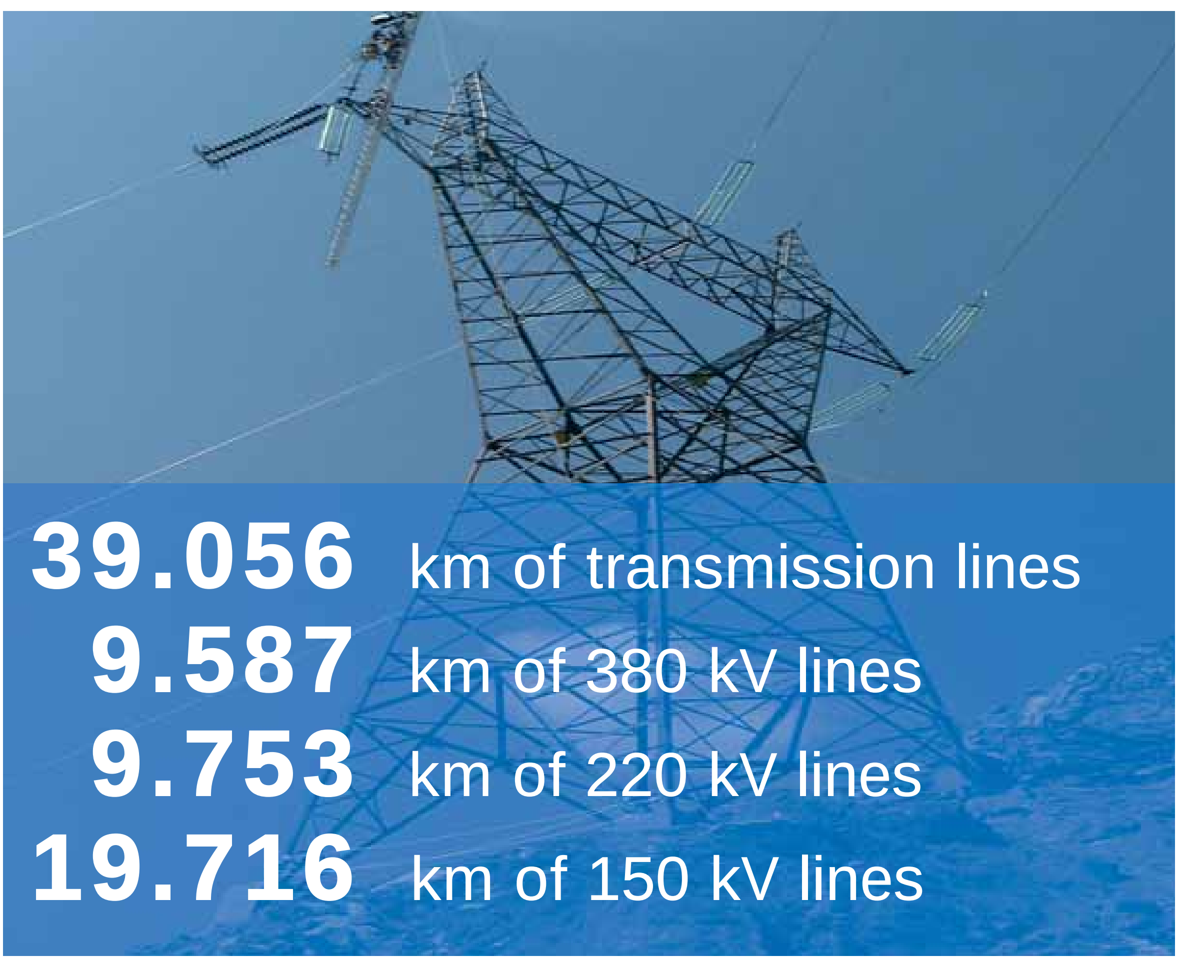
Through its subsidiary Rete Trasmissione Locale RTL SpA, the Terna Group purchased in November 2006 the entire capital of Edison Rete and 99,99% of the capital of AEM Trasmissione which, based on the improved agreement and changed corporate name, became RTM1 and RTM2, respectively. In Brazil, through Terna Participações SA, company listed in the San Paolo Stock Market, Terna has two subsidiaries, TSN - Transmissora Sudeste-Nordeste SA and Novatrans Energia SA, that operate in the country's electricity transmission sector. People are Terna's most important capital. A great team of 3.550 employees that support the Italian and Brazilian electricity system. Professionals motivated by passion and by the awareness of the profound social value of their work in continuous human and professional growth.

1	National Control Center	3.555	Employees in both Italy and Brazil
1	Main Headquaters	1.200	Industrial experts
1	Subsidiary in Brazil	276	Engineers
3	Remote Control Centers	9%	Female employees
8	Territorial Operational Areas	91%	Male employees

The grid

High voltage power lines

A power line is a system which links two power stations, or a station and a point where electricity enters or leaves the system. It is formed by electrical conductors (three-phase alternating conductors, one or two direct power conductors, etc), support structures (pylons, insulators, etc.) for overhead lines, protection cables and other components required for the proper electrical and mechanical operation of the plant. A line normally carries one or more power circuits (single or double circuit lines). The length of a power line (km/line) 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, 357 EHV and HV power stations belong to Terna. These stations are another strong point of a service which, also for 2006, is marked by the leading quality indicators in relation to its outstanding high levels. This result was obtained thanks to the organization, procedures, work methods and the technological innovations used that have also provided reduced costs for the activities.

99,2% the result, according to the ASA quality indicator (Average System Availability) that measures the average real availability of all the grid elements in the period under review

0,58 min/year the result according to the AIT quality indicator (Average Interruption Time), that measures the average time of interruption in supplying the electricity system in the period under review

Grid development: Terna, three in a row. Three new long distance power lines operating in one year.

After nearly 20 years of delays and a relative standstill in the national electricity development, Terna was able to build **three new long distance power lines** that are fundamental for the development of the country and of the south: **Matera-S.Sofia** (Basilicata, Campania, Puglia), **Turbigo-Rho** (Lombardy), **Sar.Co** (Sardinia), with an overall investment of 150 million euros. Energy and the development of power lines are among the priorities of all the European governments. The most important infrastructures in the next few years will be those for the transmission of electricity; in Italy, more than anywhere else. Blocked construction of power lines and increased consumption have created a situation of energy deficit in our country with respect to the demand. In the past few years new power plants went into operation but the sole production of energy is not enough, the development of the National Transmission Grid is also necessary.

Matera-S.Sofia

13 years after work began, the longest high voltage line in Italy, **Matera-S.Sofia**, finally went into operation with its 218 km of lines (longer than the Palermo-Messina highway and the Rome-Naples high-speed railway). This line crosses Puglia, Basilicata and Campania. The completion of the line will mark a development for the south of Italy and will finally close one of the longest and most complex chapters in the construction of our country's infrastructures. Terna began working on the line in 1993, following authorization procedures that lasted 5 years. Work was completed for over 90% back in 1995, but had been interrupted following requests submitted by various local associations to modify the project. Work resumed again and was finally completed in 2006. The new line allows using 1000 MW more of extra capacity, increasing safety and efficiency of the grid in Basilicata and in Campania; it has succeeded in eliminating congested areas by "unblocking" the electricity production in the plants in Puglia and Calabria, thus allowing the full use of the 500 MW interconnection cable between Italy and Greece which up to now was not in use. Another result obtained was greater safety and reduced grid losses for approximately 250 million kWh per year.

Turbigo-Rho

To decongest the Western area of Milan, the new 380 kV **Turbigo-Rho** power line began operating. This new line was created from the need to increase the transmission capacity of a high density population and industrial area that was traditionally "congested" from the electricity aspect. The line is particularly significant for the technological solutions used that required strong innovative capacities both for implementing the power line as well as for respecting environmental aspects: 28 kilometers form the line which crosses 11 townships; 8 kilometers are underground in order to minimize the environmental impact. The construction of the new line also allowed Terna to dismantle 10 km of old lines by tearing down existing pylons. As part of its environmental protection policy, Terna was also involved in the replanting of the Bosco of Arbuno Bruglliereza in the Parco Lombardia. Building the new line led to advantages both in terms of greater safety and of control of the electricity system in the area and also made it possible to fully use the electricity plants of the Milan area by "releasing" 1.000 MW of production capacity, with a 10 million euros savings and reduced grid losses equal to 150 million kWh/year.

Sar.Co

In order to significantly improve the electricity grid's quality and safety among the islands and also as part of mutual assistance in case of need, the **Sar.Co** 10kV interconnection cable was built between **Sardinia and Corsica** with a 50 MW capacity, representing one of the major strategic element of the system. Furthermore, the synchronous connection between high voltage grids stabilizes the frequency with greater safety benefits. For Sardinia it finally represents the possibility of increasing its electricity exports.

TERNA AND THE FINANCIAL MARKETS

TERNA AND THE FINANCIAL MARKETS

Terna share highlights	2006
Dividend (euros) [1]	0.140
Peak price	2.630
Minimum price	2.039
Average price in December	2.565,6
Stock market capitalization [2] (in millions of euros)	5,131
Number of shares (in millions)	2,000

[1] including an interim dividend of euros 0.053 distributed on 23 November 2006 and euros 0.087 to be distributed on 21 June 2007.
[2] calculated on the average price of December 2006.

FINANCIAL INDICATORS

		2006
WEIGHT OF TERNA SHARES [3]		
> on the MIB30 index (%)	0.95%	
> on the S&P/MIB index (%)	0.89%	
RATING		
Standard & Poor's	Outlook	Stable
	M/L-term	AA -
	Short-term	A1+
Moody's	Outlook	Stable
	M/L-term	Aa3
	Short-term	Prime1
Fitch	Outlook	Negative
	M/L	AA -
	Short Term	F1-

[3] Source: Borsa Italiana. Figures at 29 December 2006.

Performance of the Terna SpA share

Financial market across the globe grew in 2006, benefiting from abundant liquidity and performances of companies whose performance continued to improve. The Italian stock market recorded its fourth consecutive year of growth and from the start of January, the S&PMib index rose 15%, while Mibtel shot up 18%. The utilities sector also performed strongly in 2006, reaching record levels at European level and yielding twice market returns (DJ Stoxx600 +17%; DJ Utilities +35%).

In this overall favourable context, the Terna share also fared extremely well, rising 23% to outperform the Italian stock market (15%), as well as the European market (17%). The share's growth was especially sharp in the second half of the year, when it rose from the 2006 minimum recorded in late June (euros 2.039 per share), following the detachment of the balance of the 2005 dividend, to its peak in mid-December (euros 2.63 per share).

From placement in June 2004 to December 2006, Terna's shareholders have enjoyed growth of 51%, substantially in line with the average of Italian companies (S&PMib +49%), while total shareholder return (returns, including the appreciation of the share price and dividends paid) in the same period has risen to over 73%, compared to the Italian market average of approximately 61%.

This growth trend continued in the first few months of 2007. After the 2007-2011 business plan was unveiled, the share exceeded its historic record, peaking at euros 2.805 per share on 14 February 2007, with a stock market capitalization of euros 5.6 billion. At the end of that month, international markets slowed due to the downturn in Asian stock markets. The Terna share also slowed, but recovered in mid-March.

During the year, an average of 11 million shares were traded daily on Borsa Italiana's MTA market, equal to roughly 0.5% of the share capital.

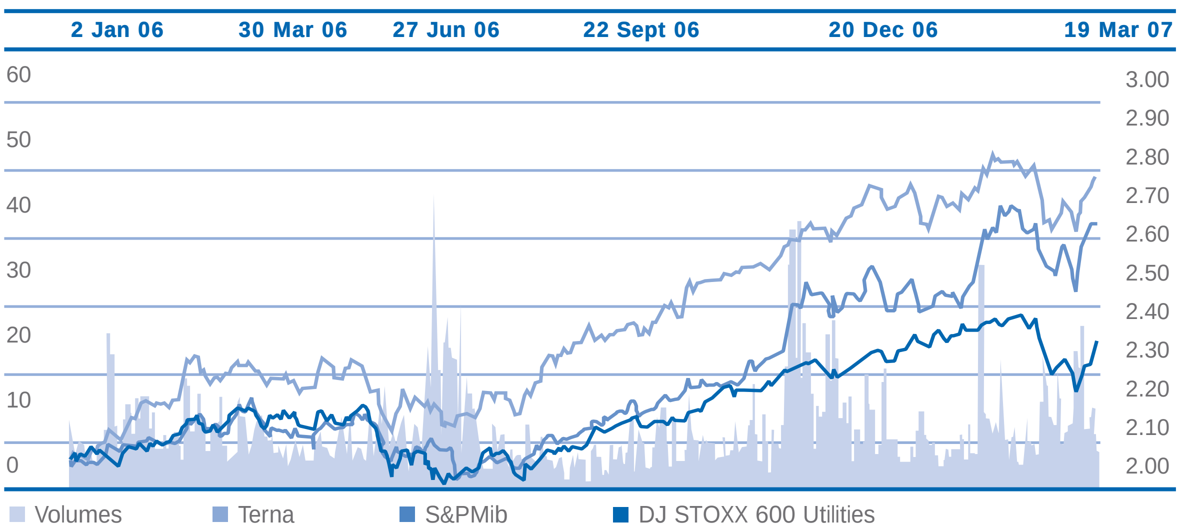
On 19 June 2006, shareholders received the final portion of the 2005 dividend of euros 0.080 per share, while on 20 November 2006, they collected the 2006 interim dividend of euros 0.053 per share. As a result, shareholders have received total dividends of euros 0.133 per share in the last twelve months, reflecting one of the highest dividend yields on the SP&PMib index and the sector.

Performance of the Terna Participações share

On 27 October 2006, Terna Participações SA certificates, representing one ordinary and two preference shares each, were listed on the Nivel 2 segment of Brazil's San Paolo stock market ("BOVESPA"). From placement to the end of December, these certificates grew approximately 15%, outperforming the Brazilian market's benchmark index in the same period (IBOV +12%).

The average capitalization of the IPO exceeds real 2 billion, equal to roughly euros 700 million.

TERNA STOCK AND S&PMIB & DJ STOXX 600 UTILITIES INDEX PERFORMANCE



Source: Bloomberg

Shareholders

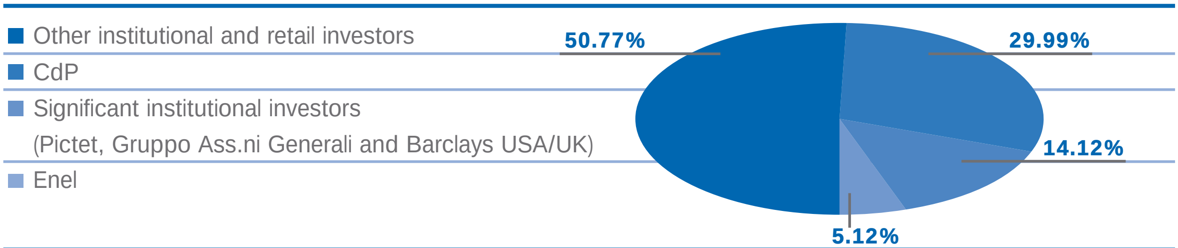
Terna SpA share capital amounts to euros 440 million, made up of 2,000,000,000 ordinary shares with a nominal value of euros 0.22 each.

On the basis of the shareholders' book and other information gathered at the date these financial statements were prepared, Terna SpA shares are held by the following:

- Cassa Depositi e Prestiti SpA (CdP): 29.99%
- Enel SpA: 5.1%
- relevant institutional investors: 14.1% (including Pictet Asset Management SA with 5.2%, Assicurazioni Generali Group with 4.9%, and Barclays USA/UK with 4.0%)

• other institutional investors and retail investors: 50.8%.

TERNA'S SHAREHOLDING STRUCTURE

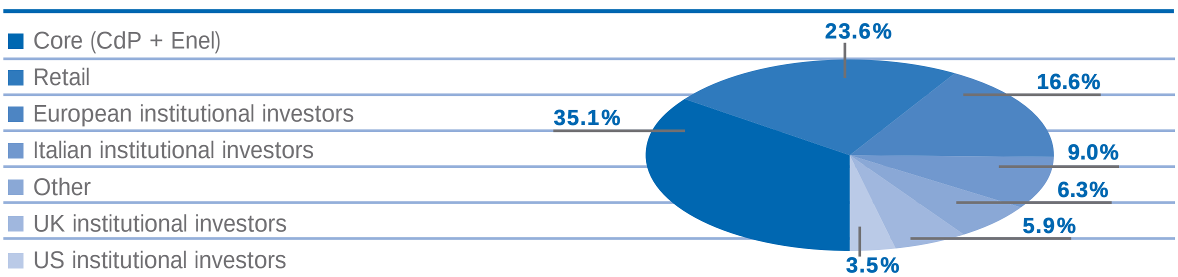


Total 100%

Based on the company's periodic surveys, 68% of Terna SpA shares is held by Italian shareholders, while the remaining 32% is held by foreign institutional investors, mainly in Europe and the US (UK 5.9%, Switzerland 5.4%, Germany 5.2% and the US 3.5%).

In 2006, the impact of institutional investors has grown significantly (from 38.1% of share capital to the current 41.3%), especially abroad, with a parallel decrease in the impact of retail investors (from 26.8% to 23.6%).

TERNA'S SHAREHOLDERS BY TYPE AND GEOGRAPHICAL AREA



Total 100%

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 shareholders', 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 istitutional investors (phone number: 06.8313.8145; e-mail address: investor.relations@terna.it) have also been set up.

HAVING VALUES CREATES VALUE

TERNA SPA FINANCIAL STATEMENT 2006

Terna
Rete Elettrica Nazionale

CONTENTS

DIRECTORS' REPORT

INTRODUCTION

Following Legislative Decree no. 38 of 28 February 2005, exercising the power granted by EEC Regulation no. 1606/2002, from 2006, companies with shares traded on regulated markets in the member states of the European Union are required to prepare their separate financial statements in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board and endorsed by the European Commission ("IFRS").

Accordingly, Terna SpA has adopted IFRS from 2006, with transition date at 1 January 2005. The last set of separate financial statements prepared in accordance with Italian GAAP are those as of and for the year ended 31 December 2005.

HIGHLIGHTS

	2006	2005	Change	%
ELECTRICAL ENERGY HIGHLIGHTS (GWh) *				
Net production of electrical energy	301,726.0	290,608.0	11,118.0	3.8%
Net electrical energy imported	44,718.0	49,155.0	-4,437.0	-9.0%
Demand for electrical energy	337,796.0	330,444.0	7,352.0	2.2%
Maximum demand (MW)	54,387.0	55,015.0	-628.0	-1.1%
FINANCIAL STATEMENTS HIGHLIGHTS (in millions of euros)				
Revenues	1,110.2	910.3	199.9	22.0%
Gross operating profits	740.9	587.5	153.4	26.1%
Operating profits	550.8	430.5	120.3	27.9%
Profits for the year	355.8	265.6	90.2	34.0%
Net non-current assets	4,978.2	4,470.9	507.3	11.3%
Net working capital	-455.9	-191.3	-264.6	138.3%
Net invested capital	3,907.4	3,663.4	244.0	6.7%
Provisions for termination benefits, taxes and contingencies and charges	-614.9	-616.2	1.3	-0.2%
Equity	1,901.7	1,797.9	103.8	5.8%
Net financial position	2,005.7	1,865.5	140.2	7.5%
Investments	345.0	266.0	79.0	29.7%
OTHER FIGURES AND RATIOS				
Average number of employees	3,370	2,966	404	13.6%
Number of employees at year end	3,367	3,388	-21	-0.6%
Earnings per share	0.178	0.133	0.045	33.8%

* Energy figures for 2006 are provisional.

SIGNIFICANT EVENTS OF 2006

FTSE4GOOD Europe index

On 10 March 2006, the Financial Times Stock Exchange of London confirmed Terna SpA's inclusion in its FTSE4GOOD Europe, an index of Europe's leading companies in terms of sustainable economic development.

2006 stock option plan

During their meeting of 15 March 2006, in addition to approving the consolidated financial statements and draft separate financial statements as of and for the year ended 31 December 2005, the Board of Directors acknowledged the non-achievement of the targets set in the 2005 stock option plan, with specific reference to the performance of Terna SpA shares. Indeed, the share under-performed the benchmark index (average performance of MIBTEL), with a weight of 50%, and the FTSE Eurotop 300 Electricity, with a weight of 50%, in the relevant period set forth in the stock option regulation. Accordingly, the Directors:

(I) announced that the options granted under the 2005 stock option plan were no longer valid, following the company's failure to achieve one of the conditions for exercise provided thereby;

(II) resolved to implement the 2006 stock option plan approved by the Board of Directors on 21 December 2005, in accordance with the mandate conferred by the shareholders on 1 April 2004, and increase the share capital in one or more instalments up to a maximum of euros 2,200,000 by 30 June 2010.

Renegotiation of the revolving credit facility

On 10 April 2006, Terna SpA signed the renegotiated credit agreement with a pool of banks for a five-year credit facility that it had originally agreed in December 2004, raising the amount from euros 500 million to euros 750 million.

The main changes relate to the following:

- the reduction of the spread from Euribor plus 17.5 base points to Euribor plus 15 base points, eliminating the previous rating index;
- a decrease in availment and non-availment fees;
- the addition of two one-year options to extend the facility. The first maturity date is 10 April 2011.

The shareholders' meeting

During their ordinary meeting of 27 April 2006, the shareholders of Terna SpA approved the separate financial statements as of and for the year ended 31 December 2005.
They also approved the proposal put forth by the Board of Directors to distribute a dividend of euros 0.13 per share for all of 2005, through the distribution of euros 0.08 following the interim dividend of euros 0.05 paid in November 2005.
The final dividend to be paid from 22 June 2006, with coupon detachment date no. 4 on 19 June 2006.

Acquisition of Terna Participações SA and contribution of investments

On 13 March 2006, the parent Terna SpA acquired 100% of the Brazil-based Donnery Holdings SA (worth real 100) for roughly real 25 thousand (approximately euros 10 thousand).
During the annual meeting, the new shareholders resolved to change the company's name to Terna Participações SA.
On 27 April 2006, the Board of Directors of Terna SpA resolved to reorganize the group's Brazilian businesses, also in view of floating the company on the Brazilian stock exchange.

As part of the reorganization process, on 6 June 2006, Terna SpA contributed the investments held by Transmissora Sudeste-Nordeste SA ("TSN") and Novatrans Energia SA ("Novatrans") to Terna Participações SA, after it had received authorization from the local regulatory authority ANEEL (*Agência Nacional de Energia Elétrica*) and TSN's and Novatrans' lending banks.

Stock market listing of Terna Participações SA

On 27 October 2006, the placement of the subsidiary Terna Participações SA on the Nivel 2 segment of Brazil's San Paolo stock market (*Bolsa de Valores de São Paulo - BOVESPA*) was successfully concluded. It entailed an IPO in Brazil and an institutional offer in Brazil and abroad, consisting of a secondary offer (sale of shares held by Terna SpA) and a primary offer (Terna Participações share capital increase subscribed by third parties), accounting for 40.7% and 59.3% of the overall offer, respectively.

The main conditions of the offer were as follows:

Seller - Terna - Rete Elettrica Nazionale Società per Azioni;

Issuer - Terna Participações SA;

Market - *Nivel 2 segment - Bolsa de Valores de São Paulo* (BOVESPA);

Underlying securities - *Certificados de deposito de ações*, representing one ordinary and two preference shares each (the "**Certificates**");

Price - real 21 per certificate;

Structure - IPO in Brazil and offer to institutional investors in Brazil and abroad for 29,841,453 certificates, equal to 34.0% of total Terna Participações share capital, broken down as follows:

Global offer of 22,104,780 certificates, equal to 26.1% of total Terna Participações share capital;

Hot issue of 20% of global offer, i.e., 4,420,956 certificates, equal to 4.2% of total Terna Participações share capital;

Greenshoe option for up to 15% of the global offer, i.e., 3,315,717 certificates, equal to 3.7% of total Terna Participações share capital.

Lock-up agreements - For 100% of the certificates underlying the offer for the first 180 days and for 40% for the subsequent 180 days;

Global coordinators - Banco UBS SA and Banco Itaú BBA SA;

Financial advisor - Goldman Sachs & Co;

Co-managers - Banco ABN AMRO Real SA and Banco Santander Brasil SA.

The success of the offer generated gross receipts of approximately real 255 million (approximately euros 94 million) on the secondary offer for Terna SpA and approximately real 372 million (approximately euros 137 million) on the primary offer for Terna Participações, which it will use to finance the company's growth in Brazil and Latin America.

Following the offer, Terna SpA holds 66% of the share capital of Terna Participações and 85.3% of ordinary shares.

Terna joins Confindustria

On 27 April 2006, Terna SpA became a member of Confindustria.

Terna SpA will join the main trade associations in Italy to encourage a healthy relationship between businesses and Italy's main infrastructural and electricity transmission company, in line with the 2006-2015 business plan.

Standard & Poor's and Moody's confirm Terna's rating

The credit rating agency Standard & Poor's confirmed Terna SpA's current long-term rating of AA- and short-term rating of A-1+ on 3 February.

On 2 May 2006, Moody's confirmed Terna SpA's issuer and long-term debt rating of Aa3, bringing its outlook back to stable. It also confirmed the company's short-term rating of P-1.

Fitch rated Terna SpA's long-term debt AA

The credit rating agency Fitch gave Terna SpA an issuer default rating (IDR) of AA- with a negative outlook, a short-term rating of F1+ and a senior unsecured rating for its long-term debt of AA on 4 May 2006.

EMTN (European Medium Term Notes) Programme

In relation to development investments provided for in the business plan, the Board of Directors of Terna SpA resolved to tap capital markets for the related funding requirements. Accordingly, it prepared a general plan for the future issue of medium/long-term term notes (EMTN programme) for up to euros 2 billion, which was subscribed on 12 July 2006.

Standard & Poor's rated the programme AA-, while Moody's and Fitch gave it an Aa3 and AA, respectively.

The programme will enable the company to benefit from potential financing opportunities on international capital markets, through the issue of bonds with various maturities in the main currencies.

2006 interim dividend

During its meeting of 6 September 2006, the Board of Directors resolved to distribute an interim dividend for 2006, after having obtained an opinion in this respect from the independent auditors KPMG, as required by Article 2433 *bis* of the Italian Civil Code.

Considering Terna SpA's profits for the first half of 2006 of euros 190 million and its outlook for the rest of the year, the Board of Directors resolved to distribute an interim dividend totalling euros 106 million, equal to euros 0.053 per share. The interim dividend, gross of any legal withholdings, was paid out on 23 November 2006, following detachment of coupon 5 on 20 November 2006.

Acquisition of other portions of the National Transmission Grid

On 24 November 2006, through its subsidiary RTL, Terna concluded the acquisition of 100% of Edison Rete SpA and 99.99% of AEM Trasmissione SpA, once it had received authorization from the Anti-Trust Authority, in accordance with the agreements signed on 16 October 2006 with Edison SpA and AEM SpA, respectively. With this acquisition, Terna has achieved a significant objective in its strategy to unify the National Transmission Grid, in accordance with the provisions of Law no. 290/2003 on the restructuring of the energy sector, as well as with the Prime Minister's Decree of 11 May 2004.

On the same day, the shareholders of Edison Rete SpA and AEM Trasmissione SpA met and appointed the new company officers, moved the offices and changed the company name. Edison Rete became Rete Trasmissione Milano 1 Società per azioni ("RTM1 SpA") and AEM Trasmissione became Rete Trasmissione Milano 2 Società per azioni ("RTM 2 SpA").

The consideration paid to acquire RTM1 and RTM2 amounted to euros 311 million and euros 123 million, respectively.

Adoption of the new Codes of Conduct and Ethics

On 21 December 2006, the Board of Directors of Terna SpA resolved to adopt the new Code of Conduct for listed companies published in March 2006.

At the same time, the Board of Directors also passed resolutions implementing the provisions of the new code and taking the necessary steps to apply other recommendations included in the new code not yet in place at Terna.

During the same meeting, the Board also resolved to adopt the new Code of Ethics and update and integrate the “Managerial and administrative model pursuant to Legislative Decree no. 231 of 8 June 2001”, which the company has adopted since 2002, to reflect new legislation and integrate National Transmission Grid management activities.

SUBSIDIARIES

Italy

RTL - Rete Trasmissione Locale

This company was set up in 1999 (as Acea Transmission) following the contribution of National Transmission Grid transmission plant owned by ACEA SpA.

On 1 October 2005, Terna acquired ACEA SpA's investment in Acea Transmission SpA, and renamed the company Rete Trasmissione Locale - RTL SpA.

RTL owns 723 km of high-voltage electrical energy transmission lines in central Italy.

As described above, the most significant event of 2006 in relation to the unification of the National Transmission Grid (RTN) provided for by Law no. 290/2003 on electricity sector reform and the subsequent Prime Minister's Decree of 11 may 2004, was the acquisition:

- of 100% of Edison Rete SpA (renamed Rete Trasmissione Milano 1 SpA - RTM1) from Edison SpA;
- of 99.99% of AEM Trasmissione SpA (renamed Rete Trasmissione Milano 2 SpA - RTM2) from AEM SpA.

The consideration for the sale agreed with AEM amounted to euros 123 million, while that paid to Edison totalled euros 311 million. Total expenditure incurred by RTL for these acquisitions amounted to euros 121 million and euros 304 million, respectively, net of the incentives provided for by the Electricity and Gas Regulator, in Resolution no. 73/06.

The parent made the financial resources needed to acquire the companies available through a capital injection.

RTM1 - Rete Trasmissione Milano 1

This company was set up in 1999 following the contribution of National Transmission Grid transmission plants owned by Edison SpA and Edison Termoelettrica SpA. Integrating the original contribution, in 2001, electrical stations were further contributed. The grids contributed connecting the thermoelectric power plants in Alto Adige, Veneto and Padana plains region to the Edison Group's industrial sites in Northern Italy. From 2002 to 2004, another three companies were merged into the Edison Group, each owning portions of the National Transmission Grid:

- Sondel Trasmissione, owner of grids linking plants in Valtellina and Tuscany to the Milanese industrial area, contributed by Sondel SpA;
- Caffaro Trasmissione, owner of grids in Friuli, contributed by Caffaro Energia SpA;
- ISE Rete, owner of grids in the industrial area of Taranto, contributed by ISE SpA.

Edison Rete owns 2,756 km of high-voltage electrical energy transmission lines, in addition to 30 electrical substations scattered throughout Northern Italy. The company also manages two control centers.

RTM2 - Rete Trasmissione Milano 2

This company was set up in 1999 following the contribution of National Transmission Grid transmission plants owned by its parent AEM SpA, in turn controlled by the Municipal Authorities of Milan.
The transmission lines link hydroelectric power plants in Valtellina and the thermoelectric power plant in Cassano d'Adda with stations in the Milan metropolitan area.
In the years that followed, the company acquired additional plants (in particular, transformation stations) in the scope of the National Transmission Grid from its parent and the related company AEM Distribuzione Elettricità.
AEM Trasmissione owns 1,095 km of high-voltage electrical energy transmission lines and 12 electrical substations scattered throughout Northern Italy. It also manages two control centres.

The following table provides the highlights of the subsidiaries RTL, RTM1 and RTM2. The figures relate to the subsidiaries' approved financial statements as of and for the year ended 31 December 2006, which have been reclassified in accordance with the parent's accounting policies.

HIGHLIGHTS

In millions of euros	RTL	RTM1	RTM2
FINANCIAL STATEMENTS HIGHLIGHTS AT 31 DECEMBER 2006			
Revenues	6.6	49.2	16.0
Gross operating profits	4.6	29.8	12.4
Operating profits	2.8	19.3	8.5
Profits for the year	1.7	10.9	5.3
Net non-current assets	430.5	191.0	77.7
Net working capital	1.5	6.1	5.1
Net invested capital	432.0	195.9	82.9
Provisions for termination benefits, taxes and contingencies and charges	0.0	1.2	-0.1
Equity	450.9	175.1	85.1
Net financial position/(indebtedness)	-18.8	20.8	-2.2
Investments	0.1	2.1	2.0
OTHER FIGURES AND RATIOS			
Number of employees at year end	1	80	27
Earnings per share	0.318	0.102	0.035

New contracts with subsidiaries

Under specific agreements, on 1 February 2007, Terna SpA was entrusted with operating and carrying out ordinary maintenance on the lines owned by its subsidiaries RTM1 SpA and RTM2 SpA. These activities consist of the following:

1. inspections and testing;
2. emergency assistance;
3. preparing and implementing conventional work plans without shutting off voltage;
4. managing interference;
5. managing unavailability and operating events;
6. ordinary maintenance;
7. damage to the National Transmission Grid.

In addition, also on 1 February 2007, a management fee agreement was signed by Terna SpA and RTM1, making the parent responsible for outlining strategies and handling business coordination, as well as providing direct and indirect services to the subsidiary. These include:

1. the coordination of managers, through suitable training programmes;
2. the administrative and financial coordination of the subsidiary, including the set-up and management of its financial activities;
3. the provision of other services in specific business areas.

A similar management fee agreement will be signed by Terna SpA and its subsidiary RTM2 SpA.

Brazil

Terna Participações

Terna Participações SA ("Terna Part") was set up in São Paulo, Brazil, on 23 January 2006 under the name of Donnery Holdings SA, to participate as shareholder in other Brazilian or foreign companies active in the transmission of electrical energy.

During an extraordinary meeting on 3 April 2006, the shareholders approved the change of name from Donnery Holdings SA to Terna Participações SA.

On 13 March 2006, all shares in the company were sold to Terna - Rete Elettrica Nazionale SpA (Terna SpA), except for those held by members of the Board of Directors (each of the three Directors owns one share).

On 6 June 2006, Terna SpA contributed controlling TSN - Transmissora Sudeste Nordeste SA ("TSN") and Novatrans Energia SA ("Novatrans") to Terna Part, with the authorization of the Agência Nacional de Energia Elétrica - ANEEL and lending banks.

On 27 October 2006, Terna Part carried out an IPO, substantially changing its corporate structure. The offer generated approximately real 371.4 million, with the issue of 53,051,472 new shares. The IPO was carried out in the *Nivel* 2 segment of the *Práticas de Governança Corporativa da Bolsa de Valores di São Paulo (BOVESPA)*, in the form of units, comprised of one ordinary and two preference shares. Following the offer, roughly 8% of ordinary shares and 84% of preference shares are now outstanding.

Novatrans Energia (NVT)

Novatrans Energia SA ("Novatrans"), a Brazil-based company set up on 18 October 2000, holds a thirty-year licence agreement (no. 095/2000 of 20 December 2000) with the local Authority for Electrical Energy (ANEEL) to operate and maintain the North-South II line. The licence expires on 20 December 2030.

The 500-kV North-South II transmission line covers approximately 1,278 km, from Samambaia (Federal district) to Imperatriz (Maranhão) with sub-stations in Serra da Mesa, Gurupí, Miracema and Colinas. It has been fully operational since the first quarter of 2005.

Construction of the transmission line began in 2002 and was completed on 8 April 2004.

Novatrans holds the commercial rights on the transmission installations for the first 15 years of operations, with annual revenues (RAP - *Receita Anual Permitida*) adjusted each year for inflation. On the sixteenth year of operation, and until the expiry of the licence, the RAP will be halved.

Transmissora Sudeste Nordeste (TSN)

On 20 December 2000, Transmissora Sudeste Nordeste SA (“TSN”), a Brazil-based company set up on 11 October 2000, obtained a thirty-year licence (no. 097/2000) to operate the South-North line from the local Authority for Electrical Energy (ANEEL). This licence expires on 20 December 2030.

The transmission line has nominal voltage of 500 kV and runs for roughly 1,062 km, from the Serra da Mesa substation in Goias to the Sapeaçu sub-station in Bahia.

TSN holds the commercial rights on the transmission installations for the first 15 years of operation, with annual revenues (RAP - *Receita Anual Permitida*) adjusted each year for inflation. On the sixteenth year of operation, and until the expiry of the licence, the RAP will be halved by 50%.

After having received the necessary authorizations from ANEEL, SFF-ANEEL and BNDES, during an extraordinary meeting held on 31 March 2006, the shareholders approved the creation of Munirah, a licensee for the Camaçari - Sapeaçu line. TSN’s Board of Directors, which met on the same day, resolved to set up a TSN branch in Sapeaçu, in which the balance sheet and income statement figures relating to the licence will be consolidated, as required by ANEEL.

The Camaçari - Sapeaçu line covers approximately 107 km, bringing TSN’s total length to 1,169 km.

The following table provides the highlights of the subsidiaries Terna Participações, TSN and Novatrans. The figures relate to the subsidiaries' approved financial statements as of and for the year ended 31 December 2006, which have been reclassified in accordance with the parent's accounting policies.

HIGHLIGHTS

In millions of euros	Terna Part	TSN	Novatrans
FINANCIAL STATEMENTS HIGHLIGHTS AT 31 DECEMBER 2006			
Revenues	0.0	91.6	97.2
Gross operating profits/(loss)	-6.9	76.9	82.3
Operating profits/(loss)	-6.9	68.4	71.8
Profits/(loss) for the year	-4.1	30.5	32.3
Net non-current assets	317.5	285.3	327.5
Net working capital	0.3	14.9	16.0
Net invested capital	317.8	299.0	343.2
Provisions for termination benefits, taxes and contingencies and charges	0.0	1.2	0.3
Equity	452.0	86.0	144.7
Net financial position/(indebtedness)	-134.1	213.0	198.5
Investments	0	2.6	4.4
OTHER FIGURES AND RATIOS			
Number of employees at year end	0	10	70

RELEVANT LEGISLATION

Legislative Framework

A variety of legislative measures affecting the company were issued in 2006, including the following:

Legislative Decree no. 152 of 3 April 2006, containing "Environmental regulations", was published in the Official Journal, edition no. 88 of 14 April 2006.

The legislation most affecting Terna is listed below:

- **Strategic Environmental Assessment (SEA) (Section II): Articles 7-22:**
  - a) **The application of a strategic environmental assessment (SEA) procedure is introduced to the development plan for the National Transmission Grid.** The SEA is applicable to all energy plans and programmes that *"contain the definition of a benchmark framework for the approval, authorization, location or the construction of works for which the related projects are subject to an environmental impact assessment under current legislation"* or that *"could have significant effects on the environment although they are not subject to environmental impact assessments."* (art. 7).
  - b) Moreover, this regulation also introduces the obligation for Terna to prepare, in advance and for the purpose of plan approval, an environmental report that constitutes an integral part of the plan or programme documentation.

- **Environmental Impact Assessment - EIA (Section II): Article 6 and Articles 23-47:**
  - a) Extension of the national EIA's scope: all works **requiring national authorization and those with inter-regional environmental impact are subject to national EIA** (previously lines up to kV 150 and up to 5 km were subject to regional EIA);
  - b) Within the Ministry of the Environment, creation of a technical/advisory commission for environmental assessments within 90 days of publication of this Legislative Decree (see art. 49), with the Prime Minister's Decree, on the Minister of the Environment's proposal;
  - c) For projects subject to national EIA, introduction of the denial by silence rule: the EIA commission must express its opinion within 90 days, considering any extensions or suspensions. If no opinion is expressed by the end of this term, the Council of Ministers may exercise its power within 60 days. If the council does not express an opinion on projects subject to national EIA, the denial by silence rule applies.

- **SEA and EIA (art. 33)**

  The provisions state that: *"for projects and works to be carried out in implementation of plans or programmes already subject to SEA, and which fall under categories for which EIA is required, while the latter is being carried out, all the information that is evaluated positively during the SEA, or decided during the plan or programme approval, is considered accepted".*

The enactment of Section II on SEA and EIA regulations was postponed to 31 July 2007 with recent Decree Law no. 300 of 28 December 2006, referred to as "one thousand extensions", published in the Official Journal edition no. 300 of 28 December 2006.

The new procedure for the reclamation of polluted sites also affects Terna. It is contained in Section IV (Articles 177- 266).

Law no. 248 of 4 August 2006 stating: "Conversion into law, with modifications, of Decree Law no. 223 of 4 July 2006, providing urgent measures for the economic and social recovery, containment and rationalization of public spending, as well as measures relating to taxes and anti-tax evasion initiatives", published in the Official Journal edition no. 186 of 11 August 2006.

- The provisions with the most impact include the deductibility of depreciation.

  Article 36, paragraphs 7 and 8, as amended by Law no. 286/06, introduces the principle according to which land and the areas on which own properties stand cannot be depreciated. Under the provisions of paragraph 7, to calculate the portions of deductible depreciation, the cost of buildings should be taken net of the cost of areas on which they stand or which constitute pertinent land.

  These provisions are applicable from the current tax period for depreciation and lease payments on buildings acquired in previous tax periods.

  The cost of areas adjacent or pertinent to buildings to be subtracted from the total is calculated as the greater of that recognized in the financial statements in the year in which they were acquired and 20%, or 30% for industrial buildings, of the total cost. Industrial buildings are those used for the production or transformation of goods.

The Law of 6 February 2007: "Provisions for the fulfilment of Italy's obligations as member of the European Union - Community Law 2006", published in the Official Journal, edition no. 40 of 17 February 2007, ordinary supplement no. 41.

- Article 1 of the Law gives the Government the power to implement the directives contained in annexes A and B through the adoption of the appropriate Legislative Decrees within 12 months of the date the Law is enacted.

  The directives that affect Terna include:

  - **Directive 2005/89/EC** of 18 January 2006, concerning **security measures for the supply of electricity and investments in infrastructures;**

  - **Directive 2006/32/EC** of 5 April 2006, concerning **the efficiency of final uses of energy and related services** and repealing Council Directive 93/76/EEC.

In particular, Directive 2005/89/EC, which should be implemented by Italian legislation by 24 February 2008, provides that:

- *"the member states ensure* ***a high level of security [.] defining roles and responsibilities [.] of the concerned market operators*** **[including transmission system managers]** *and publishing information in this respect",* paragraph 1, Article 3;

- in applying the measures for the above aims, the member states are required to consider certain issues, including *"the need to carry out* ***routine maintenance*** *and, where necessary,* ***renew the transmission grids [.] to keep them efficient"***, paragraph 2, Article 3, as well as *"the importance of* ***removing administrative barriers to investments in infrastructures****"*, paragraph 3, Article 3.

- ***"the member states or relevant authorities ensure that the transmission system managers [.] meet service levels in terms of the quality of supply and the security of the grid [and] comply with the minimum operating grid security regulations and obligations".***

  These objectives, which are subject to the approval of the member states, have been published.

  In addition, Article 4 adds that *"members states ensure that* ***curtailments in supply during emergency***

situations are based on established parameters *relating to the management of imbalances by transmission system managers".*

- **with respect to grid development ,** *"member states establish a regulatory framework that* ***provides favorable emphasis on investments so that [.] transmission system managers can develop their grids to meet foreseeable market demand [and] facilitate grid maintenance and,*** *as the case may be,* ***renewal".*** The directive adds that ***"without prejudice to EU regulation no. 1228/2003, member states can also authorize*** [in close collaboration with the concerned transmission system managers] ***commercial investments in interconnections",*** Article 6.

- the **security control report** that relates, among other things, to the quality and level of grid maintenance, which the member states are required to prepare, pursuant to Article 4 of Directive 54/2003/EC, must be **drawn up in collaboration with the transmission system managers** and illustrate ***"the general upgrade of the grid to meet existing and forecast demand for electrical energy, [.] the operating security of the grid; the required balance between supply and demand for the next five years;*** *prospects for* ***the secure supply of electrical energy for the period from five to fifteen years from the date of the report; transmission system managers' investment plans for the next five years*** *and any other known parties for the supply of transborder interconnection supply capacity".*

In particular, Directive 2006/32/EC of 5 April 2006, which should be implemented by 17 May 2008, includes Article 10, which provides that *"member states ensure the* ***restriction of incentives, in transmission tariffs [.], that increase volumes of transmitted energy without purpose [.] . To this regard,*** *under paragraph 2, Article 3 of Directive 2003/54/EC [.],* ***member states can establish obligations for*** *companies operating in the energy or gas sectors* ***in relation to the public service in terms of energy efficiency".***
In addition, paragraph 2 of the same Article adds that ***"member states can allow certain elements of the tariff systems and structures to service a social purpose as long as the negative effects on the transmission system as a whole*** *[.] are kept to the necessary minimum and are not out of proportion with respect to the social purpose".*

The Ministry of Labour’s Decree no. 39135: “Exemption from the obligation of contributing to the involuntary unemployment insurance” published in the Official Journal edition no. 213 of 13 September 2006

- Based on an assessment conducted by the Labour Inspector’s Office and concluded with the report of 16 June 2006, the Ministry of Labour passed Decree no. 39135, confirming the exemption from contributing to involuntary unemployment insurance for Enel and Enel Group companies.
  Following the Ministry of Labour’s request, the Labour Inspector’s Office carried out a similar assessment on Terna to verify whether it met the requirements of a stable workplace for exemption from the contributions.
  This assessment is preliminary to the Ministry of Labour’s passing a measure exempting Terna from contributing to the involuntary unemployment insurance.

Law no. 296 of 27 December 2006, “Measures for the preparation of annual and multi-year financial statements of the Government (Finance Act)” published in the Official Journal edition no. 299 of 27 December 2006, ordinary supplement no. 244

- The provisions of the Finance Act include paragraph 1334 and following paragraphs of Article 1, which apply to the operations of **SACE** - Institute for insurance services abroad, wholly owned by the Ministry of the Economy and Finance.

  Under the provisions of the Finance Act, SACE can carry out i**nsurance activities and offer financial guarantees for Italian operators’ projects abroad**, as previously permitted, **including investments of foreign subsidiaries or associates of Italian companies.**

  SACE is also authorized to grant guarantees, and **insure risks relating to politics, disasters, the economy, trade or currency to which Italian companies are exposed through their business activities abroad and through the internationalization of the Italian economy.**
  Within the categories of insurable risks, Article 1 of CIPE Resolution no. 93 of 9 June 1999 identifies the **risks of Italian operators or companies investing abroad** (including non-profit organizations) **that set up a company abroad or control or hold indirect investments through foreign companies controlled by the Italian operator or company in companies and business abroad.**
  The risks are divided into the risk of losing capital invested abroad due to equity losses by the company

set up, controlled or invested in abroad or its definitive inability to continue activities and the risks of the Italian operator or company losing any form of amounts due thereto, including earnings on the investment abroad (including loans granted or secured on behalf of the company set up abroad or arising on the sale of the investment).

AEEG Resolutions

Below is a brief summary of the main resolutions passed by the Electricity and Gas Regulator in 2006 with an impact on Terna’s activities.

Resolutions no. 39/06 and 49/06

With these resolutions, the Regulator participated in the approval process for the Grid Code.

With Resolution no. 39/06, the Regulator’s Board delegated certain responsibilities regarding the Grid Code to the offices. In particular, it made the Manager of Electrical Energy Management responsible for all aspects relating to the electrical energy transmission service quality, with the support of the Regulator’s Consumer and Service Quality Management Department. The activities delegated relate to the following:

- checking the compliance of Grid Code updates with directives adopted by the Regulator, not reserved for the approval of the Regulator’s Board;
- approving or denying Terna’s proposals to waive application of the Grid Code.

In this context, the Regulator subsequently passed Resolution no. 49/06, in which it:

- approved the version of the Grid Code issued on 30 November 2005, provided that, within 45 days of adoption of the measure, Terna implements the two recommendations put forth in the resolution, as well as other recommendations made, pursuant to Resolution no. 39/06, by AEEG’s electrical energy section;
- asked the Director of AEEG’s electrical energy section to inspect the application of the Grid Code provisions, as well as documents attached thereto, through work groups with the concerned parties and in conjunction with any proposals made by the Consultancy Committee to require that Terna update the Grid Code as necessary, including the documents attached thereto.

Resolution no. 58/06

With Resolution no. 58/06, the Regulator began a procedure to check the National Transmission Grid development plan for 2006. In implementation of Article 27.2 of Resolution no. 250/04, which contains the directives for the preparation of the Grid Code, the Regulator verifies the compliance of the National Transmission Grid development plan and the actual level of implementation with the following:

a) transmission service efficiency;

b) free access to electrical grids;

c) encouragement of competition;

d) minimization of charges in the procurement of resources for dispatching.

Resolution no. 73/06

In implementing the provisions of Article 2 of the Prime Minister's Decree of 11 May 2004, the Regulator passed Resolution no. 73/06, containing *"Provisions for incentives to unify ownership of the National Transmission Grid".*

The incentive mechanism defined by the Regulator provides for the following:

- the quantification of the maximum amount of incentives as euros 14 million, reflecting the estimated efficiency recoveries following the unification process. These incentives are financed through the profits margin on the considerations for use of the 2004 transmission capacity paid to Terna by GSE (the electrical service manager);
- the maximum amount of each incentive (euros 14 million) was calculated as the ratio of the value of plants owned by the seller to the value of plants owned by others, not included Terna. The value of plants is calculated on the basis of fi parameters, i.e., the parameters used to measure the fixed portion of the annual fee (covering costs incurred to operate and carry out maintenance, depreciation and returns on invested capital) paid to owners of portions of the National Transmission Grid under the standard agreement.
- 30% of the above incentive is allocated to Terna, with the residual 70% going to the seller.

The incentive mechanism outlined above applies to sales of portions of the National Transmission Grid to Terna by other grid owners that showed interest in selling from 11 May 2004 and 30 April 2006.

Resolution no. 99/06

With Resolution no. 99/06, the Regulator integrated the provisions regarding the assignment of importing rights governed by Resolution no. 269/05. In particular, the 2006 measure defined the methods by which such importing rights are transferred in the event that captive end customers become eligible and vice versa.

Resolutions no. 86/06 and 100/06

With these measures, the Regulator modified the implementation process of Resolution no. 281/05 concerning the connection of electrical grids for generation and use plants.

In particular, Resolution no. 86/06 extended the term for Terna and other grid operators to prepare the connection rules and procedures, setting the new deadline on 22 May 2006.

Resolution no. 100/06 introduced changes to the system provided for by Resolution no. 281/05 with respect to the following two aspects:

a) in the event of production plants from renewable sources, the incentive measures clarify that the producer of electricity from a renewable source receives more advantageous treatment than a producer from conventional resources, under the terms specified in the resolution;

b) payment by the grid manager to the entity requesting the connection of amounts for delays in the construction of plants.

Resolution no. 111/06

With this resolution, which includes the *"Conditions for the supply of the public electrical energy dispatching service in Italy and for the procurement of the related resources based on economic merit, pursuant to Articles 3 and 5 of Legislative Decree no. 79 of 16 March 1999,"* the Regulator defined the new conditions for the supply of the dispatching service, thereby repealing, with effect from 1 January 2007 (subsequently postponed to 1 April 2007) the conditions established under Resolution no. 168/03.

The main changes introduced by this resolution relate to the following:

1. the adoption of an account-based system;
2. the creation of a system of guarantees.

With respect to the account-based system, the resolution introduced two accounts for the registration of electrical energy forward purchase and sales contracts, i.e., for the purchase and sale of energy outside the system of bilateral contracts:

- the forward Energy Account for the recognition of operators' positions with Gestore del Mercato Elettrico

SpA (GME - the Electricity Market Operator), in relation to forward purchases and sales;
- the actual Unbalancing Account for the recognition of operators' positions with Terna, in relation to dispatching considerations.

Terna manages actual unbalancing accounts and the related balances reflect each operator's exposure thereto.

In terms of the guarantees, the resolution requires that Terna organize and manage a guarantee system establishing for each dispatching system user the maximum exposure allowed, and setting up a monitoring and guarantee recovery system. To this end, the resolution includes a guarantee clause for charges related to insolvency situations. In the event that costs arise due to the insolvency of users not covered by guarantees, Terna informs the Regulator, which then establishes the recovery methods through a specific consideration.

Resolution no. 112/06

The Regulator issued this resolution, dictating the *"Planning and allocation methods of unbalancing considerations for CIP 6/92 production units"*. Following the contribution of electrical energy transmission and dispatching activities to Terna, while GSE remained responsible for, *inter alia*, CIP 6/92 plants, certain clarifications were needed regarding the various roles relating to the provision of dispatching services. In particular, in distinguishing between dedicated CIP 6/92 units and mixed CIP 6/92 units according to whether production is entirely dedicated to GSE, or also to the plant owner in part, the resolution established the following:

- that the GSE is the entity required to sign the dispatching service agreement with Terna for these units;
- specifically how plans should be presented;
- how the unbalancing of units should be broken down and allocated.

Resolution no. 123/06

The Regulator issued this resolution, beginning a procedure to introduce emergency measures to become effective on 1 August 2006 to increase the level of competition in the Ancillary Services Market and, accordingly, contain dispatching service costs for end customers. These measures, which were also taken due to the increase in the uplift value recorded in April 2006, in particular, will be developed to:

- reduce resource procurement charges for the dispatching service, through corrective measures taken in the Day-Ahead Market;
- enable Terna to coordinate its Ancillary Services Market;
- update the unbalancing considerations to align them more closely with the costs actually incurred by Terna;
- ensure production plant input from CIP 6 and renewable unplannable resources is correctly scheduled;
- intensify the Regulator's monitoring of the Ancillary Services Market and establish the measures to be taken in the event of irregular behaviour on the part of operators on that market.

As part of this procedure, on 11 July 2006, the Regulator published a consultation document for concerned parties, containing *"Guidelines for the definition of emergency measures to contain electrical energy dispatching service costs for end customers"*.

Resolution no. 143/06

With this resolution, the Regulator identified the amount of the consideration to cover expenses incurred by the electricity market operator, Gestore del Mercato Elettrico SpA (GME) in carrying out functional monitoring activities under Resolution no. 50/05. The amount of the consideration that Terna is required to pay GME for 2005 and 2006 is euros 394,000 (three hundred and ninety-four thousand euros) per year. The expenses incurred by Terna to settle the consideration due to GME, pursuant to the provisions of Resolution no. 168/03, are covered by the consideration to cover Terna's operating costs, as per Article 37.1 of Resolution no. 168/03.

Resolution no. 162/06

With this resolution, the Regulator clarified that the transmission service tariff proceeds for 2005, based on the tariffs in place in that period, did not adequately remunerate the transmission operators. The tariff deficit recorded amounts to a total of euros 51.7 million, which GSE SpA will pay to rightful transmission operators, by using a portion of the transmission capacity considerations realized in 2004 and 2005. In particular, the revenues relating to Group companies includes approximately euros 47.3 million for the parent, euros 0.3 million for the subsidiary RTL, euros 2.2 million for the subsidiary RTM1 and euros 0.8 million for the subsidiary RTM2.

Resolution no 165/06

With this resolution, which includes *"Emergency changes to Resolution no. 168/03 of 30 December 2003 and Resolution no. 50/05 of 24 March 2005 and directives for Terna SpA to contain dispatching service costs for end customers"*, issued as part of the proceedings initiated with Resolution no. 123/06, the Regulator introduced certain changes to the methods of procurement of resources for dispatching and the provision of the service by Terna. These changes are applicable from 1 August 2006, and aim to increase the level of competition, while containing costs incurred by end customers. In the same measure, the Regulator also established specific directives in accordance with which Terna was required to change its Grid Code.

Resolution no. 181/06

With this resolution, the Regulator approved the new time brackets in effect from 1 January 2007, following the conclusion of the consultancy commenced on 3 July 2006.

The approved system provides for three different time brackets by which the value of electrical energy will be differentiated. These brackets are based on daytime hours, night-time hours and weekdays, Saturdays and holidays.

The consultancy document provided for three alternative options with respect to the previous configuration, comparing them in terms of the consistency - within each time bracket - of the expected value of electrical energy provided to end customers in each hour. They were also compared with respect to the simplicity and stability of their time structure. The resolution approved option 2 (grouping of different times between Saturday and Sunday; another grouping from 7.00 and 8.00 on weekdays and Saturday, in an intermediate bracket and another grouping from 7.00 pm and 8.00 pm on weekdays, in an intermediate bracket). The change was made to take account of the recommendations made in response to the consultancy.

Resolution no. 183/06

With this resolution, containing *"Amendments and integrations of Resolution no. 168/03 concerning the consolidation of electrical energy measures for dispatching"*, the Regulator introduced measures to resolve the critical areas noted by some distributors regarding the assignment of PODs (point of delivery codes that are consistent throughout Italy) within the established terms (30 June 2006).

Resolution no. 203/06

With this resolution, which contains the 2007 *update of electrical energy transmission and distribution service considerations and amounts to be paid for the recovery of service continuity and the collection of amounts for work to increase energy efficiency in the electricity sector, as well as connection contributions and fixed rights established in section I of the Minister of Industry, Commerce and the Trades' Decree of 19 June 1996*, the Regulator updated the parameters and tariff components to the introduction of the new time brackets under Resolution no. 181/06.

Resolutions no. 208/06 and 209/06

With these resolutions, the Regulator began proceedings to decide the tariffs for the provision of electrical energy transmission and distribution services, as well as the related service level parameters for the 2008-2011 regulatory period.

The joint introduction and parallel implementation of these proceedings are aimed at ensuring that the tariffs and considerations are established in complete compliance with the service quality rules and standards.

The main updates to the tariffs relate to the mechanisms promoting the recovery of service provision efficiency, incentives for the development of infrastructures (transmission grid, distribution grids and metres), the simplification of tariff mechanisms, the superseding of the system based on the tariff options introduced in 2000 and the upgrade of the tariff system for connections and fixed rights.

The main updates to the service levels relate to the quality of commercial companies' call centers and the extension of indemnities to low voltage customers in the event of failure to meet "service continuity standards" or "interruption rates".

Both resolutions provide that the settlement criteria applied to larger companies for both tariff costs and service quality standards be expanded to encompass small distribution companies, i.e., "minor electrical businesses".

Resolution no. 253/06

With this resolution, containing *amendments and integrations to the Electricity and Gas Regulator's Resolution no. 111/06 of 9 June 2006 and Appendix A to that resolution, for the start-up of the forward purchase and sale registration platform*, the Regulator postponed the date that Resolution no. 111/06 takes effect, consequently, the repeal of Resolution no. 168/03 to 1 April 2007. It also provided for an economic adjustment in the dispatching service for the scheduled unbalancing that makes it possible for Terna to purchase energy on the electricity market.

Resolution no. 256/06

With this resolution, the Regulator began a procedure to create measures concerning the conventional definition of electrical energy withdrawn as part of the dispatching service, with regard to the possibility of extending the hourly rates or grouping medium and low voltage end customer withdrawal hours together.

Resolution no. 288/06

With this resolution, containing 2007 *measures for the management and joint management of foreign imports and exports on the interconnection grid*, the Regulator established the methods and conditions for electricity imports and exports for 2007, implementing the parameters provided for in the Minister of Economic Development's Decree of 15 December 2006. Market mechanisms were established for the allocation of rights to use transmission capacity, on the basis of annual, monthly and daily auctions.

This measure provides for the allocation of transmission capacity following joint procedures carried out by the grid managers concerned for all borders with EU member countries.

In implementation of this resolution, Terna completed the allocation of transmission capacity for imports and exports of electricity on an annual basis for 2007 across the electric borders shared with France, Switzerland, Austria, Slovenia and Greece.

Resolution no. 289/06

With this resolution, containing *measures for the procurement and remuneration of resources capable of ensuring immediate interruption or suspension with notice of electrical energy withdrawals from 1 January 2007*, the Regulator established the methods to be used for the procurement of resources capable of ensuring immediate interruption or suspension with notice of electrical energy withdrawals from 2007, following the consultation process commenced with the document published on 24 May 2006.

The resolution provides for the definition of procedures that allow Terna to carry out forward purchases of resources that can be immediately interrupted or suspended with notice. To ensure that these procedures are implemented in a reasonable amount of time, the resolution provides for a simplified system for 2007. In particular, the resolution establishes that the same entities that supplied interruptible resources in 2006 may continue to do so in 2007 with similar methods.

However, from 2008, Terna will vet resource suppliers based on the new mechanisms set forth in the regulatory measure.

Resolution no. 314/06

With this resolution, containing *amendments to the Electricity and Gas Regulator's Resolution no. 168/03 of 30 June 2003*, following that described in the consultation document of 28 November 2006, Terna was given the power to agree forward resource procurement contracts for dispatching services, provided that the technical, economic and procedural methods applied in relation thereto were approved by the Regulator. In addition, this resolution:

- changed the method of calculation of the resource procurement consideration on the Ancillary Services Market;
- confirmed permission for Terna to make additional offers on the day-ahead market, as per the provisions of Resolution no. 165/06;
- changed the method of calculation of the actual unbalancing considerations for immaterial consumption amounts, by reducing the threshold under which unbalancing is calculated at the day-ahead market price from 7% to 3% in 2007;
- extended operations of the bilateral adjustment platform for demand to the start-up of the account-based platform;
- confirmed the timing of dispatching consideration calculations and invoicing used in 2006 for 2007 as well.

Resolution no. 315/06

With this resolution, containing a *modification to the breakdown of the relevant grid into zones provided for by Article 15 of Resolution no. 168/03 of 30 December 2003*, the Regulator approved the “Identification of relevant grid zones” document, as proposed by Terna, which modified the breakdown of the relevant grid into zones, by eliminating the “Turbigo-Roncovalgrande” zone.

Resolution no. 11/07

With this resolution, the Regulator approved the integrated code of measures concerning functional and accounting unbundling requirements for companies operating in the electricity and gas sectors.

The measure supersedes previous resolutions relating to administrative and accounting unbundling (Resolutions no. 310/01 and 311/01).

As previously outlined in the consultation document published on 16 March 2006, this resolution introduces the following two unbundling systems:

1) functional unbundling, applicable only to companies that are integrated vertically;
2) accounting unbundling applicable to all electricity and gas operators.

Vertically integrated companies are required to give each of their business that the Regulator defines as essential for the purposes of market deregulation decisional and organizational autonomy, thus unbundling it from an administrative standpoint from all other businesses conducted by the company. The Regulator has explicitly provided for a limitation to functional unbundling in Terna’s case, with respect to transmission, dispatching and metering activities. Accordingly, the company is permitted to manage them jointly without them being individually subject to the functional unbundling requirement.

The resolution takes effect at the start of the first year beginning after 31 December 2006. The functional unbundling requirements are applicable from 1 January 2008.

THE GRID CODE

The following updates were made to the grid transmission, dispatching, development and security code (the “Grid Code”):

- on 12 May 2006, the company published on its website the Grid Code updated based on the Electricity and Gas Regulator’s observations set forth in Resolution no. 49/06 approving the document, and other observations set forth pursuant to Resolutions no. 39/06, by the offices of the same Regulator;
- on 23 May 2006, a new version of Chapter 1 of the Grid Code was published, regarding National Transmission Grid connections in line with the new regulations introduced in the Electricity and Gas Regulator’s Resolution no. 281/05;
- on 31 July 2006, a new version of Chapters 4 (dispatching rules) and 7 (regulation of dispatching and transmission service items) was published to implement the measures contained in the Electricity and Gas Regulator’s Resolution no. 165/06;
- on 13 December 2006, updated versions of Chapters 4 and 7 of the Grid Code were published in order for the concerned parties to consult them. In addition, certain attachments, which form an integral part of the Grid Code, were also published, in accordance with the provisions of Resolution no. 111/06. Following the consultation procedure, the Ministry of Economic Development is currently studying the documentation to carry out the relevant assessments.

In the first few months of the year, the Users Consultation Committee, provided for by paragraph 4, Article 1 of the Prime Minister’s Decree of 11 May 2004 completed the procedure to appoint its members. The six associations representing the various user categories (AIGET, APER, Assoelettrica, CNCU, Confindustria and FederUtility), as identified by the Ministry of Production Activities, appointed their representatives for the Committee, which was completed with Terna’s appointment of its Chairperson, as provided for by the Grid Code.
The Committee began activities with the meeting held on 5 May 2006.
During the meetings held up to the date of this report, the Committee carried out the following:

- approval of its own rules of procedure;
- approval of attachments A 13 and A 54 to the Grid Code;
- preparation of an opinion on the new measures provided for by the draft 2007 development plan;
- preparation of an opinion on the definitive draft of Terna’s 2007 development plan;
- approval of the consultation documents relating to the implementation of Resolution no. 111/06 in the Grid Code.

ENERGY FRAMEWORK

Italy's energy demand

According to initial figures, in 2006, demand for electrical energy reached 337,796 GWh, up 2.2% on the previous year. This figure was affected by the way the dates fell (there were two business days less in 2006 than in 2005) and different weather. On a like-for-like basis, the growth in demand would have been 2.6%.

During the year, domestic production met 86.8% of demand for electrical energy on the grid (85.1% in 2005), which corresponds to 293,078 GWh, net of the consumption of ancillary services and pumping, showing an increase of 4.2% on 2005. The remaining demand (13.2%) was met through trading abroad, for a total of 44,718 GWh in 2006, compared to 49,155 GWh in the previous year (down 9.0%).
An analysis of the trend in trading abroad shows imports down 7.8% to 46,323 GWh, against 50,264 GWh in 2005.
However, exports rose by 44.7% from 1,109 GWh to 1,605 GWh.

ENERGY IN ITALY

GWh	Jan-Dec 2006 *	Jan-Dec 2005	Change	%
Gross production	315.016	303.672	11.344	3,7%
Ancillary services	13.290	13.064	226	1,7%
Net production	301.726	290.608	11.118	3,8%
Foreign suppliers	46.323	50.264	-3.941	-7,8%
Foreign customers	1.605	1.109	496	44,7%
Pumping	8.648	9.319	-671	-7,2%
TOTAL ITALIAN DEMAND	**337.796**	**330.444**	**7.352**	**2,2%**

* Provisional figures

Consumption

In 2006, total consumption of electrical energy rose by 2.1% on 2005 to 316,434 GWh. Electrical energy sold on the market shows the growth in the portion covering eligible customers, which a reduction in the portion sold to captive customers. In 2006, captive market consumption (147,000 GWh) was just about equal to the consumption on the free market, which rose by 8.8% on 2005 to 147,500 GWh. Lastly, the following table shows a substantial stability in internal consumption, which made up 6.9% in 2006, in line with the previous year.

Distribution losses as a percentage of total demand were also substantially unchanged (6.3% in 2006).

ITALY'S ELECTRICAL ENERGY CONSUMPTION BY MARKET

GWh	2006 *	2005	Change	%
Captive market	147,000	152,991	-5,991	-3.9%
Free market	147,500	135,509	11,991	8.8%
Own consumption	21,900	21,317	583	2.7%
Total Consumption	**316,400**	**309,817**	**6,583**	**2.1%**
Leaks	**21,396**	**20,626**	**770**	**3.7%**
in % of demand	(6.3%)	(6.2%)		
TOTAL ITALIAN DEMAND	**337,796**	**330,443**	**7,353**	**2.2%**

* Provisional figures

The breakdown of electrical energy consumption by sector, shown in the following table, underscores above average increases (up 3.7%) in the service sector, which used 86,900 GWh, making up 27.5% of total consumption. The production sector, which reached 156,800 GWh, accounted for 49.6% of total consumption in 2006, showing 2.0% growth on the previous year, in line with the rise in total consumption. Lower than average increases, but in line with previous trends, were seen in the domestic sector, with growth of 0.5% to 67,300 GWh and a share of 21.3% of the total, and in the agricultural sector, with growth of 0.7%.

ITALY'S ELECTRICAL ENERGY CONSUMPTION BY SECTOR

GWh	2006 *	2005	Change	%
Agriculture	5,400	5,364	36	0.7%
Industry	156,800	153,727	3,073	2.0%
Services	86,900	83,793	3,107	3.7%
Domestic use	67,300	66,933	367	0.5%
TOTAL CONSUMPTION	**316,400**	**309,817**	**6,583**	**2.1%**

* Provisional figures

Electrical energy generation

In 2006, net domestic production rose by 3.8% on the previous year (see table below) in relation to the decrease in imported energy, as described above. An analysis of production figures by source, net of ancillary services, shows an increase in thermoelectric production of 4.1% on 2005.

Net production from renewable sources, exclusively hydroelectric generation, increased by 14.3%. This increase was considerable with respect to wind energy and photovoltaic production, which grew by 37.0%, while geothermal energy production increased by 3.8% on average.

In 2006, hydroelectric production remained at the same levels as the previous year, with a slight increase of 0.2%.

The annual hydroelectric production index was also in line with the previous year, coming in at 0.80 in 2006, compared to 0.79 in 2005.

ITALIAN PRODUCTION OF ELECTRICAL ENERGY

GWh	2006 *	2005	Change	%
Gross hydroelectric production	43,022	42,927	95	0.2%
Gross thermoelectric production	263,252	253,073	10,179	4.0%
Gross geothermal production	5,527	5,325	202	3.8%
Gross wind and photovoltaic production	3,215	2,347	868	37.0%
Total gross production	**315,016**	**303,672**	**11,344**	**3.7%**
Hydroelectric ancillary services	572	570	2	0.4%
Thermoelectric ancillary services	12,397	12,186	211	1.7%
Geothermal ancillary services	315	303	12	4.0%
Wind and photovoltaic ancillary services	6	5	1	20.0%
Total ancillary services	**13,290**	**13,064**	**226**	**1.7%**
Net hydroelectric production	42,450	42,357	93	0.2%
Net thermal production	250,855	240,887	9,968	4.1%
Net geothermal production	5,212	5,022	190	3.8%
Net wind and photovoltaic production	3,209	2,342	867	37.0%
TOTAL NET PRODUCTION	**301,726**	**290,608**	**11,118**	**3.8%**

* Provisional figures

Generation plants

Net generation capacity reached 89.8 GW in 2006, up 4,336 MW (5.1%) on 2005. The sharpest increases were seen in the thermoelectric sector, with growth of 4,036 MW, up 6.5% on 2005. In percentage terms, the highest increases were recorded in the wind and photovoltaic sector, up 13.6% or 223 MW. Net hydroelectric capacity recorded a more modest increase, up 77 MW (0.4%). Geothermal production capacity remained unchanged on 2005.

ITALIAN PRODUCTION CAPACITY

MW	2006 *	2005	Change	%
Gross hydroelectric power	21,430	21,343	87	0.4%
Gross thermoelectric power	68,800	64,645	4,155	6.4%
Gross geothermal power	711	711	0	-
Gross wind and photovoltaic power	1,870	1,646	224	13.6%
Total gross power	**92,811**	**88,345**	**4,466**	**5.1%**
Net hydroelectric power	21,070	20,993	77	0.4%
Net thermoelectric power	66,200	62,164	4,036	6.5%
Net geothermal power	671	671	0	-
Net wind and photovoltaic power	1,865	1,642	223	13.6%
Total net power	**89,806**	**85,470**	**4,336**	**5.1%**

* Provisional figures

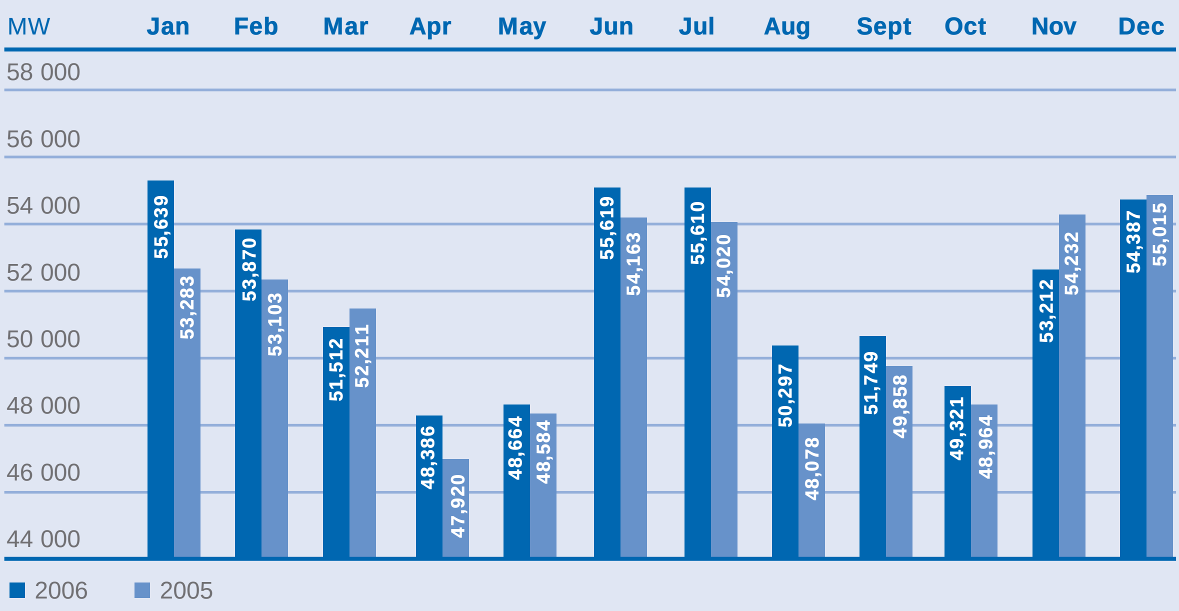
DISPATCHING AND SALES

Terna is responsible for the transmission and dispatching of electrical energy on the high and extra high voltage grid throughout Italy.
During the year, Terna guaranteed secure procurement by ensuring there were adequate resources to meet demand and by continuously balancing out energy requirements and available resources in real time.
In 2006, system management enabled Terna to successfully resolve critical issues, guaranteeing security and adequate margins of reserve.

Performance of the electricity business

The trend in peak power demand is illustrated in the chart below. In 2006, domestic demand peaked the all-time record of 55,619 MW on 27 June 2006, up 1.1% on the previous year (55,015 MW on Tuesday 20 December 2005 at 6.00 pm).
On 28 June 2006, a new record of 1,125 GWh for the daily demand of electrical energy was set (up 2.5% on 2005).
The relationship between energy and peak power demand in the year (hours of use) rose from 6006 in 2005 to 6073 in 2006. This increase was due to growth in demand for energy in excess of demand for power during the year (2.2% versus 1.1%).

MAXIMUM MONTHLY POWER DEMAND

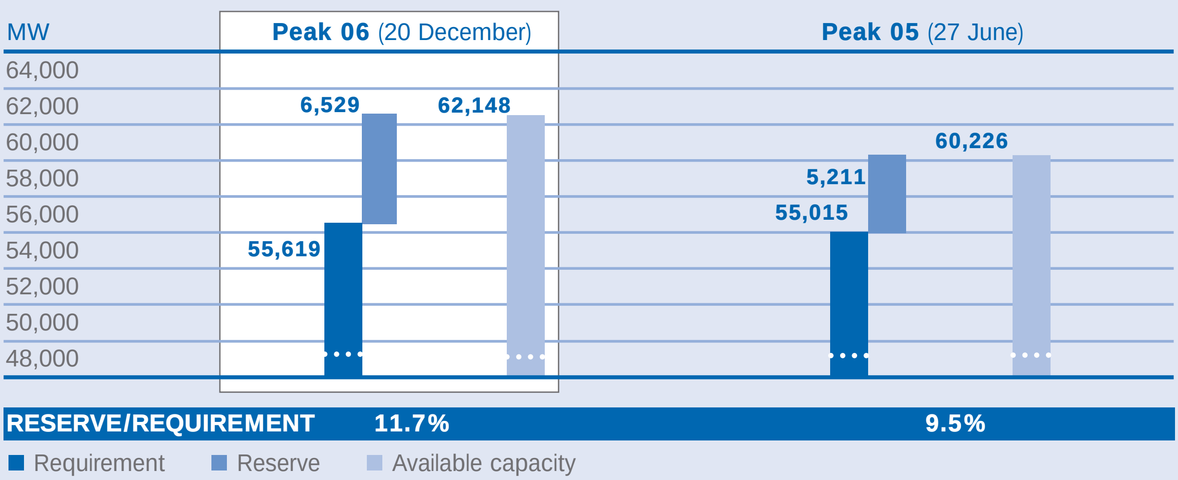


Meeting power demand

The forecasting and maintenance coordination measures implemented by Terna enabled it to meet power demand with adequate margins of reserve during the year, in which the peak summer day (27 June 2006) was higher than the peak recorded in 2005 (20 December 2005).

The same processes enabled the company to overcome the winter gas crisis and the summer water crisis.

MARGINS OF RESERVE DURING PEAKS - 2006 VS. 2005



From December 2005 to March 2006, Italian operators requested the export of power abroad. At first, this was justified by the increase in prices in Central Europe's electricity market, partly due to particularly severe weather conditions in that area and partly to market strategies implemented by the same operators. The exporting of power abroad led to potentially critical situations with respect to meeting Italian demand on certain days, given the narrow margins of reserve.

The reduced use of interconnection capacity with foreign countries generated an increase in the thermoelectric consumption of natural gas, contributing to an emergency situation in the procurement of the necessary natural gas reserves.

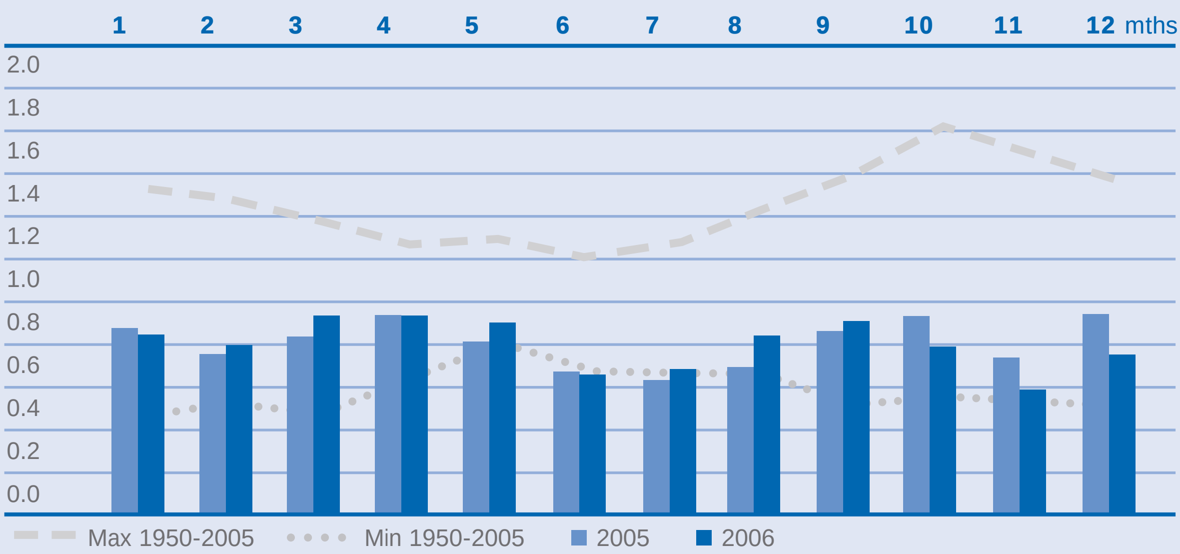
In order to contain gas consumption for thermoelectric plants and safeguard the adequacy of supply to the electric system, Terna implemented the measures provided for by Decree Law no. 19 of 25 January 2006 containing "Emergency measures to ensure the procurement of natural gas".

In the summer of 2006, the effects of below average water indexes in previous months arose, as illustrated in chart 1, although average reservoir capacity levels were recorded during the period (chart 2).

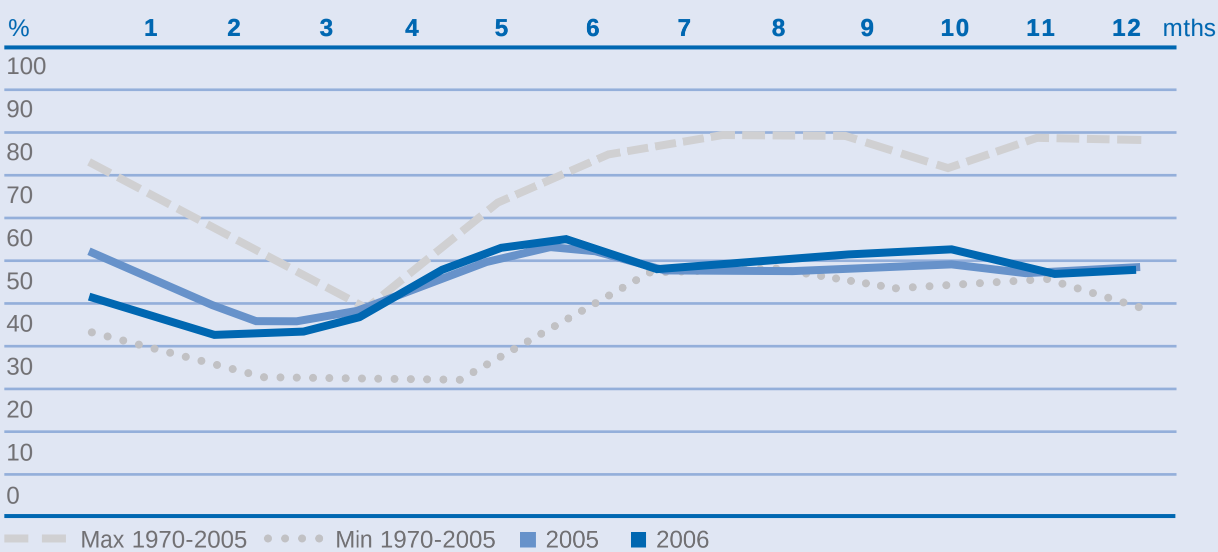
In particular, the water situation in the Po basin was characterized by reduced flows similar, in flow rate and level, to the situation that arose in the summer of 2003, although to a lesser extent in some cases.

In accordance with the memorandum of understanding prepared for the joint management of water crises in the Po River basin, the Po Basin Authority carefully monitored water flows and implemented a suitable water release programme from the mountain basins, which also affected hydroelectric plants. Terna actively contributed to the monitoring by providing weekly figures on water resources drained from hydroelectric reservoirs, by concession holder and hydrographic basin.

WATER INDEXES (CHART 1)



AVERAGE RESERVOIR CAPACITY LEVELS AT MONTH END (CHART 2)



However, the Po River water system conditioned the availability of power from thermoelectric power plants located along the Po Basin using that water in the cooling cycle of production units.

In this context, during the last week of July, exceptional weather conditions affected Italy - and most of Europe. These conditions led to considerably high power requirements and reductions in the availability of electrical energy throughout Europe, which gave rise to a decrease in the balance of imports from abroad. In particular, on 25, 26 and 27 July 2006, a high rate of accidental unavailability from thermoelectric plants was recorded, with an increase of roughly 20% in unavailable supplies on the same period in 2005. Supply to customers with interruptibility clauses in their agreements was suspended (BMI) to ensure that the national electricity system would continue operating.

The BMI suspension plan was applied as shown in the table.

In accordance with current regulations and emergency procedures, the CNC suspended customers only after having:

- maximized national production within the safety limits;
- activated, in real time, contracts for maximum supply of emergency energy from abroad.

SUMMARY OF CUT-OFFS WITH NOTICE

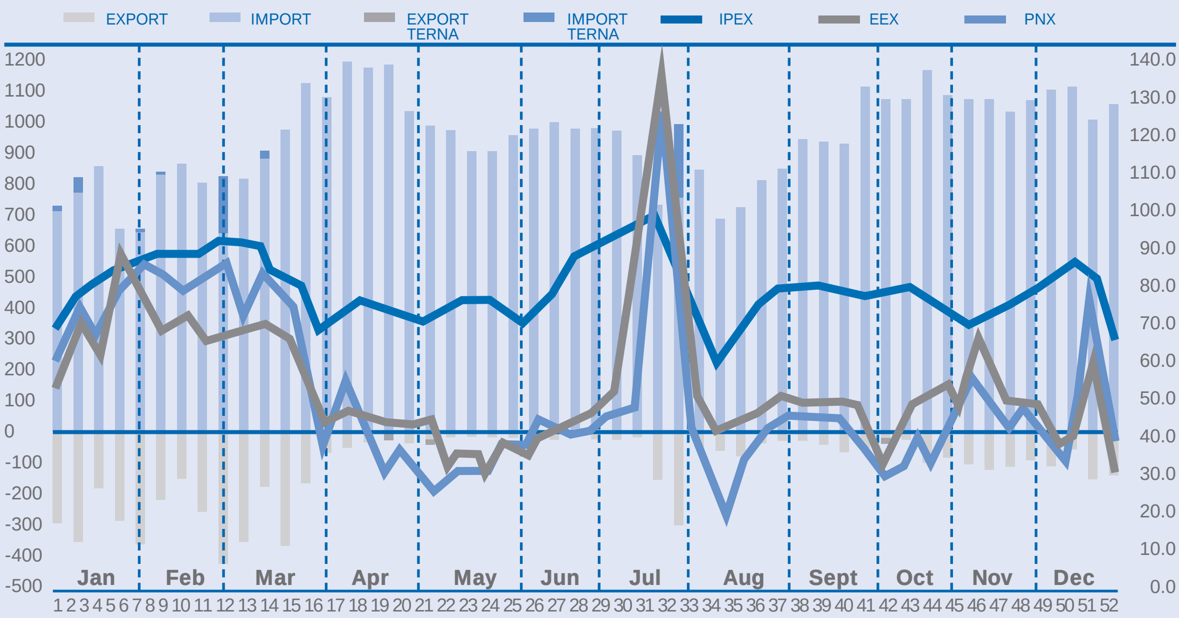
DATE	START	END	DURATION (h.m.s.)	POWER (MW)	ENERGY (MWh)	AREA
25.07.2006	11.26	12.42	1.15.27	79,2	99,6	CNC_PRE___NORTH_EAST
	11.27	12.42	1.15.46	82,4	104,0	CNC_PRE_LOM__LOMBARDY1
	13.40	20.03	6.22.44	593,7	3.786,9	TOTAL
26.07.2006	9.52	20.01	10.09.00	681,5	6.917,1	TOTAL
	9.56	20.01	10.05.00	2,0	20,2	CNC_PRE_SIC_SICILY
27.07.2006	9.50	16.04	6.16.00	5,5	34,3	CNC_PRE_SIC_SICILY
	9.52	16.04	6.12.00	703,1	4.359,3	TOTAL

SUMMARY OF CUT-OFFS IN REAL TIME

DATE	START	END	DURATION (h.m.s.)	POWER (MW)	ENERGY (MWh)	AREA
25.07.2006	11.24	21.01	8.36.19	440,77	3.792,9	CNC_REA___NORTH_EAST
	11.24	20.01	8.36.35	218,42	1.880,5	CNC_REALOM__LOMBARDY1

With respect to imports from the North, the sharp drop recorded in the first quarter, and which was seen even more dramatically in late July, related to price fluctuations in Central European electricity markets, mainly in France and Germany, which are even more volatile than the Italian market, reaching prices that are up to 20 times higher than average value in just a few hours.

To cover the drop in imports, particularly in the last few days of July, when summer demand peaked and very little energy was available from Italian thermoelectric plants, creating a critical situation in meeting Italian requirements and a reduction in margins of reserve, Terna procured energy from foreign TSOs, to maximum imports from the South.



Procurement of dispatching resources

The structure of the Electricity Market did not change significantly in 2006 with respect to the previous year. Accordingly, Terna's role on the Day Ahead Market was confirmed with respect to defining the transit limits between market zones, publishing energy requirement estimates before the market opening and authorizing the presentation of sales or purchase offers to realign total demand on energy markets with the forecast requirement, where differences exceed 5%. In order to limit the total cost of forecast error incurred by demand operators, since August, the intervention threshold has been reduced to 2%.

In line with the previous year, in 2006, Terna operated on the Day Ahead Market on a daily basis, selling approximately 3.1 TWh and acquiring approximately 3.9 TWh.

Monthly volumes purchased and sold were highly variable, due to the varied behaviour of operators. The maximum net purchase balance was recorded in January (369 GWh), while December saw the maximum net sales balance (331 GWh).

The main market for the Procurement of dispatching resources is the Ancillary Services Market, which is a pay as bid market, i.e., one in which each unit is remunerated at the offer price, rather than the marginal price.

Operators are required to submit a sales price and a purchase price for each unit of energy. Prices submitted are valid in both the *ex ante* and *ex post* phases.

- *Ex ante Ancillary Services Market*

  In the planning phase that takes place the day before the flow, energy is purchased and sold for the purpose of procuring power reserves, disposing of residual amounts following market outcome (Day Ahead Market and Adjustment Market) and covering residual requirement errors.

  During the year, 12.6 TWh of energy was purchased and 14.3 TWh was sold on the *ex ante* Ancillary Services Market.

  The quantities traded are variable from one month to the next due to the fluctuating need for requirement corrections, which was highest in July (715 GWh) and lowest in August (14 GWh).

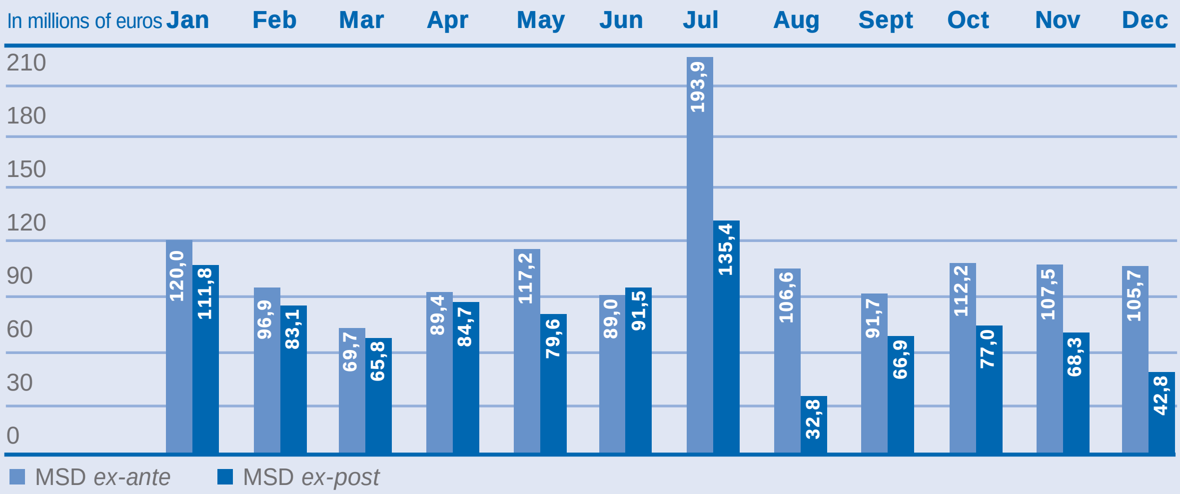
  The residual charge grew substantially on 2005 due to the significant increase in energy sales prices, which rose from an average of euros 98/MWh to an average of approximately euros 134/MWh in 2006.

- *Ex post Ancillary Services Market*

  Energy is purchased and sold in real time to balance the grid, by sending commands to authorized production units.

During the year, 11.1 TWh of energy was purchased and 8.0 TWh was sold on the *ex post* Ancillary Services Market.

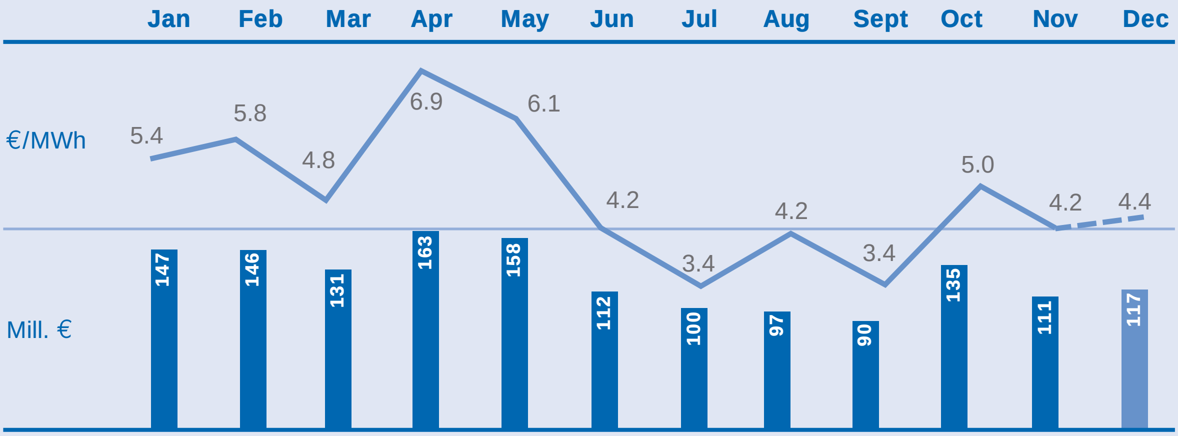
The quantity purchased was higher on average than that sold, due to the need to cover the unbalancing of generation plants, which is generally negative. The maximum purchase balance was 692 GWh in July.



Downstream of real time, Terna verifies that operators have correctly performed their commercial obligations, both in terms of generation and demand. To this end, with the support of distributors, it reads the metres at each issue and withdrawal point and calculates the differences with respect to defined outcome schedules of the energy markets. These differences, which are called unbalancing, are measured using algorithms defined by the regulatory framework. The net charge resulting from the measurement of the unbalancing and the purchases and sales carried out by Day Ahead Market and the Ancillary Services Market is calculated each month and charged on a *pro quota* basis to each consumer.

This consideration, which is called an uplift, grew significantly in the first few months of the year and peaking in April, to then stabilize in the last few months of 2006, also following the modifications to the Ancillary Services Market measurement methods from August (AEEG Resolution no. 165/06).

DISPATCHING CONSIDERATION



Interruptibility service

The supply interruptibility service, with and without notice, enables Terna to have a quantity of interruptible power that it may use:

- in the event of instantaneous interruptibility, i.e., without notice, mainly in order to rapidly restabilize reserves and balance in real time;
- in the event of interruptibility with notice, to manage situation of actual risk for the national electricity system with the possibility of implementing load lightening procedures.

More than one critical situation arose during the year (which are detailed below) in which the availability of supplies that could be interrupted was essential in preventing or limiting the use of load lightening procedures. The following table gives the number of entities that provided the interruptibility service for 2006 and contractual power.

	Number of customers	Contractually-agreed power (MW)
Instantaneous	91	1,946
With notice	84	1,119

Service quality, unsupplied energy and faults

In 2006, energy not supplied, with respect to the relevant grid, totalled approximately 2,323 MWh, net of interruptions on the contractually-agreed loads with interruptibility clauses. This figure, which is significantly higher than that recorded in 2005 (2,101 MWh), was impacted substantially by the event that affected the Sicilian grid on 17 July 2006, leading to a widespread and prolonged non-supply of approximately 748 MWh throughout the island.

During the year, claims were made against the fact that supply can be interrupted, with and without prior notice, following accidents, and to restore a sufficient reserve, as well as safety conditions in the energy system. The most important events were the following:

- on 15 February 2006 at 3:22 pm the BMI defence system was activated, following the signal on the 380 kV Bulciago-Soazza line;
- on 23 February 2006 at 2:24 am on supplies that can be interrupted with prior notice, following a fault three hours earlier at the 380 kV La Spezia electrical station, to contain transmission from the central area to the north;
- on 10 April 2006 at 10:31 pm and on 11 April 2006 at 0:46 am and 1:13 am the BMI EDA defence system was activated following the signal on the 380 kV Musignano-Lavorgo line;
- on 16 June 2006 at 4:25 pm the BMI EDA defence system was activated following the signal on the 380 kV Lavorgo-Mettlen line;
- on 26 June 2006 at 3:38 pm disconnection of supplies that can be interrupted with prior notice to contain the voltage decrease in the extra high-voltage and high-voltage nodes in the Venice area;
- on 29 June 2006 at 10:54 am disconnection of supplies that can be interrupted with prior notice to restore sufficient reserve due to the fault of production groups in Sardinia.

The various events that occurred in the national electricity system included the fault on 4 November 2006, which, originating on a portion of the electricity grid in Germany, affected the European grid, provoking non-supply of over 1,000 MWh to many users, including in Italy.

Lastly, the progressive amounts recorded in 2006 for the three “Terna service and National Transmission Grid plant quality” indexes, measured in accordance with Resolution no. 250/04 of the Electrical Energy and Gas Regulator and Terna Grid Code, are summarized below:

- AIT (average interruption time for reasons attributable to Terna) = 0.558 min/period; domestic annual target = 1.00 min/year;
- SAIFI + MAIFI (average number of short-term and long-term interruptions per user connected directly to Terna’s National Transmission Grid, for reasons attributable to Terna) = 0.215; domestic annual target= 0.23;
- ENS (energy not supplied due to users’ interruptions for reasons attributable to Terna) = 378 MWh. Annual domestic target = 560 MWh;
- ASA (total system availability of Terna grid) = 99.212%; domestic annual target = 99.000%.

NATIONAL TRANSMISSION GRID

National Transmission Grid development plan

With respect to the implementation of the 2006 plan, during the year, work was completed on the following plants, which then went into use:

- the new 380 kV “Turbigo - Ospiate” connection (approximately 20 km suspended and 8 km underground);
- as part of the rationalization of the electrical energy grid in the Milanese area: the powering up of the 220 kV “Verderio-Cislago” and “Verderio-Dalmine” lines and the 220 kV connection to the Verderio station from the 220 kV “Grosio - Ricevitrice Nord” line;
- the new 380 kV S. Barbara section (armoured) and the connection thereto of the two Santa Barbara (Cavriglia - AR) Enel Produzione combined cycle groups (TG and TV); the new 380 kV section was connected to the 220 kV “S. Barbara - Arezzo C. - Tavarnuzze” line (with a new 400 MVA ATR 380/220 kV and a short underground link) and to the existing 132 kV section (with a new 250 MVA 380/132 kV);
- a new 380 kV station in Fossoli (MO), near to the location of the current “Carpi Turbogas” power plant and adjacent to the 380 kV “Caorso - S. Damaso” line, to which the new station was connected with an in-and out line, with the construction of two 380 kV simple triad links;
- the new 220 kV section of the S. Maria Capua Vetere station (supplied by the 380 kV system using ATR 380/220 kV), to which the 220 kV “Fratta - Presenzano” and “Aversa - Capriati” in-and-out lines were connected;
- the new 150 kV underground AC connection between the Bonifacio (Corsica) electric station and the 150 kV S. Teresa (SS) CP;
- the 380 kV stations connecting to the Ferrara, Sparanise and Livorno Ferraris thermoelectric power plants;
- the 220 kV Soverzene section;
- the 132 kV Vicenza Monteviale section with 220/132 kV transformation;
- the powering of transformation capacity in the Magliano Alpi (CN), Vado Ligure (SV), Martinetto (TO) and Scorzè (VE) stations;
- 17 capacitor banks in 17 plants.

The integrated planning process

With a view to improving service quality and standards, Terna has continued to invest in the voluntary integration of the Strategic Environmental Assessment included in the development plan, in line with the provisions of European Directive no. 2001/42/EC[1], with the objective of "ensuring a high level of environmental protection and contributing to the integration of environmental considerations in the preparation and adoption of plans and programmes […] that could have a significant impact on the environment" (Article 1 of the directive). The Environmental Report, which accompanies the development plan, was prepared in 2006. In it, Terna documented how it had included environmental concerns in its planning of the National Transmission Grid, mentioning, *inter alia*, the alternatives identified, estimated potential significant effects on the environment, any mitigation measures and monitoring actions. These efforts were made in view of making the electricity grid development process increasingly transparent, well documented and easy to understand, thus encouraging collaboration and participation. The integrated planning process is now being launched with memoranda of understanding and planning agreements between Terna and the regions. The memoranda of understanding are voluntary pending implementation of Directive no. 2001/42/CE, for the coordination of strategic environmental assessment activities. The planning agreements are signed, as provided for by paragraph 1, Article 2 of Ministerial Decree of 22 December 2000 to localize and build structures for integrated work by state, regional and local authorities, as well as other public entities. The aims of these documents are to collaborate on projects, prepare environmental reports, express the region's more knowledgeable and well-informed opinion on the content of the development plan, in accordance with Ministerial Decree of 22 December 2000, and streamline the authorization procedure for work approved following the Strategic Environmental Assessment. In addition to the agreements signed in previous years, in 2006, memoranda of understanding were signed between Terna and Sardinia and the autonomous province of Trento. They are currently being defined with the regions of Ligury, Lazio and Abruzzo and the autonomous province of Bolzano.

Before 2006	**Regions:** Piedmont, Calabria, Emilia-Romagna, Lombardy, Sicily, Campania, Basilicata, Umbria, Tuscany and Marche
2006	**Region Sardinia and the Autonomous Province of Trento**
Currently being defined	**Regions:** Ligury, Lazio, Abruzzo and the Autonomous Province of Bolzano

[1] European Parliament and the European Council's Directive no. 2001/42/CE concerning the assessment of the environmental effects of certain plans and programmes, also referred to as the SEA (Strategic Environmental Assessment) directive, extends the requirement of environmental assessment to planning and programming processes as well. Previously only an Environmental Impact Assessment was required for projects with a potential impact on the environment. Its implementation has been postponed to 31 July 2007.

To define and experiment the Strategic Environmental Assessment process jointly and in compliance with Directive no. 2001/42/CE, in 2005, a technical commission was created with the participation of Terna, the Minister of the Environment, the Minister of Heritage, the Minister of Economic Development, the Minister of Infrastructure, more than 12 regions and autonomous provinces that had signed memoranda of understanding with Terna. In this context, in 2006, the methodology and procedures for the integrated planning and Strategic Environmental Assessment process were defined, which will be fully applied, unless it is revised by the Italian legislation that implements the directive.

Institutional agreements

The following agreements were signed in 2006:

- memorandum of understanding between the autonomous region of Sardinia and Terna on 3 May 2006 for the application of the Strategic Environmental Assessment to electricity planning in that region;
- framework planning agreement and memorandum of understanding with the autonomous province of Trento on 12 May 2006; the agreement concerns collaboration on the rationalization of the Val d’Adige grid. The memorandum of understanding, which is part of the former document, relates to the joint development of the Strategic Environmental Assessment procedure applied to the National Transmission Grid in the province.
- memorandum of understanding for the reconstruction of the Crevola Toce - Domodossola - Calice line, as part of the streamlining of the National Transmission Grid, on 14 June 2006. The agreement was signed by the Piedmont Region, the Province of Verbano Cusio Ossola, the Municipal Authorities of Domodossola and Crevoladossola, two mountain communities and Terna.

Environmental initiatives

During the year, Terna continued to carry out initiatives to reduce the environmental impact of its plants. These initiatives included the following:

- adoption of compensation measures following the crossing of protected areas and natural reserves (Parco dell’Adamello, Parco del Ticino and Parco del Roccolo);
- adoption of Foster support systems (winners of the environmental support system contest) in the project for the new 380 kV Tavarnuzze-Casellina long distance line;
- adoption of tubular structures for 380 kV supports. In the year, a study began to expand on the

performance of the supports (the current performance is reduced due to traditional supports with shorter bays and limited corners).

This type of support has been installed on the following:

- 380 kV Laino-Rizziconi line (six supports in dual-triads in the Parco del Pollino);
- 380 kV S. Fiorano-Robbia line (two supports, in dual-triads in the Parco dell'Adamello);

- adoption of measures to limit the values of the electromagnetic field of long distance lines. During the period, in collaboration with Cesi, Terna developed theoretical and physical models to study active and passive screens for voltage of up to 380 kV, for the purpose of developing realization models to reduce electrical and magnetic fields generated by existing and planned lines;
- adoption of architectural solutions for the construction of buildings for new electrical stations in landscapes. In particular, the construction of a service building for the Carpi station (MDL architecture firm) was completed, while work continued on the engineering of architectural solutions (Costa & Partners) for the conversion stations in Fiume Santo and Latina of the new 500 kV DC SAPEI link.

Investments in property, plant and equipment

Investments at 31 December 2006 may be broken down by type of plant and compared with the previous year as follows:

In millions of euros	2006	2005
Transmission lines	120.1	121.3
Transformation stations	148.8	121.7
Other	49.6	18.9
TOTAL INVESTMENTS	**318.5**	**261.9**

Development investments

The main projects of the year included the completion of the Laino-Feroleto-Rizziconi line, the Turbigo-Rho long distance line, the construction of the Sardinia-Corsica line and the start-up of activities on the SAPEI underwater connection between Sardinia and the Italian peninsula.

In addition, collaboration and preliminary design activities began in advance on the Sorgente-Rizziconi line (slated for 2007), while work progressed on the Matera - S.Sofia line (expected to become operational in the first half of 2007) and on the Casellina - S.Barbara line.

Maintenance and other investments

Renovation is being completed on the Villavalle, Calenzano and Verderio (already up and running) stations where civil projects are being finished up. Work continued on the Pianezza station.

Other investments includes IT projects (rationalization of processes: basic software, LAN network upgrade, etc.), the purchase of company cars and the building in Via della Marcigliana.

Significant O&M activities

The following operating and maintenance activities were commenced or completed during the year, for the purposes of a safe and high-quality electrical service:

- full implementation of the findings of the *"operating and maintenance efficiency project"*, with changes in the equipment control, maintenance and inspection criteria;
- fully operational use of the MBI system, both for stations and lines (expert system to support maintenance activities), which optimizes maintenance work - carried out almost exclusively through diagnostic check-ups. In particular, in 2006, the system was integrated with the use of handheld computers to collect data on the status of plants during routine inspections, again both for lines and electric stations;
- fully operational use of the GIS system with the complete geographical referencing of the national electricity grid;
- start-up of a long-term plan to replace old high-voltage machinery and reduce the overall age of machines;
- continuance of the campaign to replace glass insulators with insulators in other composite materials or in glass precoated with silicone resin to eliminate their vulnerability in highly polluted areas (saline - industrial/agricultural pollution);
- continuance of the campaign to replace copper and aldrey conductors on critical lines and fully replace them on the older areas of long distance lines;
- increase in maintenance or renovation to be carried out using the live technique;
- introduction of prognostic techniques in diagnosing the integrity of electrical lines, including the use of equipment based on ultra-violet rays to measure the "crown effect".

Moreover, work groups were created:

  - to obtain information on the location of faults on high-voltage lines, using remote technologies and equipment already installed;
  - to secure lines using remote technologies, by changing station and control system equipment so that line and ground knife switches and the "special operating mode" function can be secured remotely. This

was done so that work could be carried out on the lines using traditional methods or live safely, without having to send personnel to the relevant stations.

- to look into the applications of video-communications technology to support operations (work on plant parts) and diagnostics (panoramic or targeted images of visible plant parts or using infrared rays).

Number of plants

The following table compares the number of plants owned by Terna SpA at 31 December 2006 with the previous year end.

	31.12.2006		31.12.2005	
Stations	315		302	
Transformers	576	112,333 MVA	572	109,968 MVA
Bays	4,046		3,947	
Lines	35,316 km		35,129 km	
Triads	1,968	39,222 km	1,953	38,976 km

Stations

The number of stations increased by a total of 13 compared to 31 December 2005. This increase was due to the following:

- seven new stations becoming operational: Carpi Fossoli, Ferrara Nord, Rho, Pogliano and Sparanise (380 kV); Edison Terni (150 kV); Bardi (132 kV);
- disposal of one plant: Rosen (380 kV);
- purchase of nine plants from Enel Distribuzione: Certosa (220 kV); Pettino (150 kV); Montestrutto, San Rocco, AGIP Petroli, Sondel Porcari, Centro Energia Ferrara, Degussa and Lonza (132 kV);
- sale of two stations to Enel Distribuzione: Sorio (220 kV); Bando (132 kV).

Transformers

The number of transformers increased by four, as follows:

- activation of two 220/132 kV autotransformers, which were previously available, for a total of 410 MVA in the Scorzè and Vicenza Monteviale stations;
- installation of two new 380/220 kV and 380/132 kV autotransformers for a total of 650 MVA in the S. Barbara station;
- installation of two new 380/220 kV autotransformers for a total of 800 MVA each in the S. Maria Capua Vetere and Rumianca stations;
- installation of a new 380 kV/132 kV autotransformer with 250 MVA in the S. Damaso station;
- acquisition of two machines (one 150/132 kV autotransformer and one 132/60 kV transformer) for a total of 75 MVA in relation to the acquisition of the S. Rocco and Pettino stations from Enel Distribuzione;
- replacement of two 380/132 kV, 160 MVA autotransformers with two 250 MVA autotransformers in the Avenza and Bussolengo S. Salvar stations;
- transfer of five 132 kV/MT transformers for a total of 160 MVA in relation to the transfer of the Sorio station and medium voltage section of the Tavarnuzze plant to Enel Distribuzione.

Total transformation capacity increased by 2,365 MVA during the year.

Long distance power lines

In terms of long distance lines, the total length of triads increased by approximately 246 km compared to 31December 2005. This increase is mainly due to the following:

- construction of the 380 kV Ospiate - Turbigo link (approximately 38 km, including 16.6 km underground);
- construction of the 150 kV underground/underwater line from S. Teresa di Gallura to Bonifacio (Corsica) called SARCO (approximately 14 km);
- construction of the 150 kV underground Molentargius - Selargius line (approximately 10 km);
- connection of the Larderello plant to the 132 kV Certaldo - Poggibonsi line (approximately 34 km);
- in-and-out link from the 380 kV Garigliano - S. Maria Capua Vetere line to the new Sparanise station (approximately 7 km);
- in-and-out link from the 220 kV Aversa - Capriati and Fratta - Presenzano lines to the new 220 kV section of the S. Maria Capua Vetere station (approximately 12 km);
- acquisition of the 132 kV Bulciago - Nibionno, Nibionno - Carugo, Novedrate - Salice, Carugo - Salice and Strettoia - Isola Santa lines (for a total of approximately 35 km) from Enel Distribuzione;
- acquisition of the 150 kV Benevento II - Benevento Nord 1, Viagrande - S. Venerina, Reggio Condera - Reggio Industriale, Reggio Condera - Scilla, Reggio Industriale - Scilla, Gallico - Villa S.Giovanni, Gallico - Reggio Condera, Scilla - Villa S.Giovanni, Quartucciu - Molentargius, Quartu S. Elena - Molentargius, Selargius - Quartucciu, Selargius - Quartu S. Elena lines and Isili shunt (for a total of approximately 135 km) from Enel Distribuzione;
- demolition of the 220 kV Sondrio - Robbia pole 1 line (approximately 25 km);
- sale of the 150 kV S. Agata - Capo d'Orlando line (approximately 17 km) to Enel Distribuzione.

SUMMARY OF FINANCIAL ACTIVITIES

The financial statements as of and for the year ended 31 December 2006 show profits for the year of euros 355.8 million, after amortization and depreciation of approximately euros 190.1 million, net financial income of euros 16.1 million and income taxes of euros 211.1 million.

Revenues amounted to approximately euros 1,110.2 million, including euros 1,036.2 million in relation to the consideration due to the company for the use of the National Transmission Grid and other profitable energy items (DIS generating euros 32.3 million, MIS generating euros 9.3 million and the consideration pursuant to AEEG Resolution no. 34/05 generating euros 0.3 million).

Operating expenses amounted to approximately euros 369.3 million, including personnel expenses of euros 237.0 million.

The operating profits totalled euros 550.8 million.

Income taxes of the year amounted to euros 211.1 million and included current IRES tax of euros 194.7 million and current IRAP tax of euros 39.6 million. In addition, the company recorded net deferred tax assets of euros 20 million and sundry taxes of previous years totalling euros 3.2 million.

The balance sheet includes net property, plant and equipment and intangible assets of euros 4,308.2 million and net invested capital of euros 3,907.4 million, including euros 1,901.7 million (48.7%) covered by equity and euros 2,005.7 million (51.3%) covered by financial indebtedness.

The 2006 and 2005 income statements of Terna SpA for management purposes are summarized below.

Figures have been reclassified.

THE MANAGERIAL ECONOMIC ACCOUNT OF TERNA SPA

(a)

In millions of euros	2006	2005	Change	%
REVENUES				
Grid transmission consideration [1]	994.3	821.6	172.7	21%
Other energy items [1]	41.9	6.9	35.0	507.2%
Other revenues from goods and services [1]	47.3	59.3	-12.0	-20%
Other revenues and income	26.7	22.5	4.2	18.7%
Total revenues	**1,110.2**	**910.3**	**199.9**	**22.0%**
OPERATING EXPENSES				
Personnel expenses	237.0	198.6	38.4	19.3%
Services and use of third party assets	123.7	106.7	17.0	15.9%
Materials	18.1	23.9	-5.8	-24.3%
Other [2]	27.1	20.0	7.1	35.5%
Capitalized expenses	-36.6	-26.5	-10.1	38.1%
Total operating expenses	**369.3**	**322.8**	**46.5**	**14.4%**
GROSS OPERATING PROFITs	**740.9**	**587.5**	**153.4**	**26.1%**
Amortization and depreciation [3]	**190.1**	**157.0**	**33.1**	**21.1%**
OPERATING PROFITS	**550.8**	**430.5**	**120.3**	**27.9%**
Net financial income (expenses) [4]	16.1	-10.7	26.8	-250.5%
PROFITS BEFORE TAXES	**566.9**	**419.8**	**147.1**	**35.0%**
Income taxes	211.1	154.2	56.9	36.9%
PROFITS FOR THE YEAR	**355.8**	**265.6**	**90.2**	**34.0%**

(a) In accordance with Communication no. DME/6064291 of 28 July 2006, the reclassified income statement is unaudited.

In the financial statements:

[1] the balance was classified as "Revenues from sales and services";
[2] this corresponds to the captions "Other costs" and "Amortization, depreciation and impairment losses" for the amount of the accrual to the provision for bad debts (euros 12.1 million);
[3] the balance corresponds to the caption "Amortization, depreciation and impairment losses", net of the accrual to the provision for bad debts;
[4] this corresponds to the balance of the captions described in points 1 and 2 of "Financial income and expenses".

Revenues amount to euros 1,110.2 million, up euros 199.9 million due to the following main changes:

- Revenues arising from the grid transmission consideration and other energy items rose by euros 207.7 million, as follows:
  - an increase in grid transmission consideration revenues of approximately euros 54.1 million mainly related to the tariff process;
  - an increase in revenues following the acquisition of the TSO business activity in November 2005 of approximately euros 93.9 million;
  - an increase of euros 59.6 million due to the effects of AEEG Resolution no. 162/06 and adjustments of previous years;
- Other revenues from goods and services decreased by euros 12.0 million, as follows:
  - reduction of roughly euros 23.1 million due to fewer services carried out on behalf of third parties (mainly for the Enel Group companies);
  - increase of approximately euros 11.1 million due to the rise in amounts released to revenues for contract work in progress completed and inspected in 2006;

Operating expenses of euros 369.3 million rose by approximately euros 46.5 million on the previous year, due to the sum of the following:

- a rise of around euros 38.4 million in personnel expenses, mainly as a result of the entry of personnel with the acquisition of the transmission and dispatching business activity from GSE SpA (formerly GRTN) (acquired on 1 November 2005) and the transfer of former Acea Trasmissione personnel to Terna (on 1 October 2005);
- a reduction of approximately euros 5.8 million in the use of materials;
- an increase of roughly euros 24.1 million in services and other costs, also due to the fact that the company is now fully operational as an integrated TSO operator. As mentioned above, in 2005, these costs only related to the last two months of the year;
- increase of approximately euros 10.1 million in capitalized expenses.

Amortization and depreciation, amounting to euros 190.1 million, rose by approximately euros 33.1 million. This was mainly due to the effect of the acquisition of the TSO business activity and increased depreciation in relation to new plants that went into use during the year, as well as the recalculation of the residual useful lives of certain plants earmarked for disposal in the next few years.

Net financial income of approximately euros 16.1 million increased by euros 26.8 million on 2005. This growth was mainly due to the combined effect of the gain realized on the sale of Terna Participações shares (euros 38.4 million), offset by higher financial expenses following the increase in average indebtedness and the rise in interest rates (euros 9.3 million).

Income taxes of approximately euros 211.1 million rose by euros 56.9 million.

In millions of euros	2006	2005	Change
Current taxes	234.3	165.2	69.1
Net deferred tax (income)/charges	-20.0	-5.4	-14.6
Income taxes of previous years	-3.2	-5.6	2.4
TOTAL	**211.1**	**154.2**	**56.9**

The increase in recognized current taxes (up euros 69.1 million) is mainly due to the sharp rise in the profits for the year, in addition to the following:

- introduction of new tax legislation affecting the deductibility of depreciation on land and cars and higher IRAP rates;
- tax gain on the contribution of investments in the Brazilian operating companies TSN and Novatrans to the Brazilian subsidiary Terna Participações, as well as the gain realized on the listing of Terna Participações on the São Paulo stock exchange (total of euros 9.1 million);
- non-deductible accruals to the provisions for contingencies and the provision for bad debts (euros 13.0 million).

The change in net deferred tax income/charges was also affected by the new tax legislation, as well as normal recognitions during the year.

The impact of income taxes on the profits before taxes amounted to 37.80% (net of adjustments for taxes of previous years).

Accordingly, the **profits for the year** amounted to euros 355.8 million, up by approximately euros 90.2 million on 2005.

FINANCIAL POSITION

The balance sheet as of 31 December 2006 and 2005 is summarized below. Figures have been reclassified.

(a)

In millions of euros	at 31.12.2006	at 31.12.2005	Change
NET NON-CURRENT ASSETS			
Intangible assets	159.2	151.5	7.7
Property, plant and equipment	4,149.0	4,020.4	128.6
Non-current financial assets (1)	670.0	299.0	371.0
Total	**4,978.2**	**4,470.9**	**507.3**
NET WORKING CAPITAL			
Trade receivables	1,163.7	985.7	178.0
Inventories	7.7	7.2	0.5
Other assets (2)	16.3	45.0	-28.7
Trade payables	1,282.9	959.7	323.2
Net tax liabilities (3)	114.4	16.7	97.7
Other liabilities (4)	246.3	252.8	-6.5
Total	**-455.9**	**-191.3**	**-264.6**
Gross invested capital	**4,522.3**	**4,279.6**	**242.7**
Sundry provisions (5)	614.9	616.2	-1.3
Net invested capital	**3,907.4**	**3,663.4**	**244.0**
Equity	1,901.7	1,797.9	103.8
Net financial indebtedness (6)	2,005.7	1,865.5	140.2
TOTAL	**3,907.4**	**3,663.4**	**244.0**

(a) In accordance with Communication no. DME/6064291 of 28 July 2006, the reclassified balance sheet is unaudited.

In the financial statements the captions correspond to:

(1) "Non-current financial assets" for the amount of investments in subsidiaries (euros 660.0 million), investments in associates (euros 4.6 million) and "Other noncurrent assets";
(2) "Other current assets", net of tax assets (euros 1.6 million) and "Current financial assets" for the amount of accrued financial income (euros 0.6 million);
(3) "Other current assets" for the amount of tax assets (euros 1.6 million), "Tax liabilities" and "Other current liabilities" for the amount of other tax liabilities (euros 43.8 million);
(4) "Current financial assets" for the net amount of accrued interest on derivatives hedging the bond (euros 1.5 million), "Other non-current liabilities", "Current financial liabilities" and "Other current liabilities" (euros 63 million), net of tax liabilities;
(5) "Termination benefits and other employee-related provisions", the "Provision for contingencies and charges", "Deferred tax liabilities" and "Deferred tax assets";
(6) "Non-current financial assets" for FVH derivatives and trading derivatives (euros 12 million), "Current financial assets" for the amount of the intercompany loan granted to Terna Participações (euros 0.5 million), "Cash and cash equivalents", "Long-term loans", "Financial liabilities".

Net financial indebtedness is detailed below:

In millions of euros	at 31.12.2006	at 31.12.2005	Change
Bond	1,406.6	1,498.4	-91.8
Current portion of EIB loans	570.5	400.0	170.5
Intercompany current account balance	0.2	4.8	-4.6
Short-term loans from Terna Participações	-0.5	0	-0.5
Short-term loans	50.0	55.0	-5.0
Bank account balances and cash	-15.3	-15.8	0.5
Derivative financial instruments	-5.8	-77	71.2
TOTAL FINANCIAL INDEBTEDNESS	**2,005.7**	**1,865.5**	**140.2**

Intangible assets

The increase of euros 7.7 million is due to ordinary changes of the year in relation to investments for the internal development of software or the purchase of software as part of system development programmes (euros 26.5 million) and amortization and depreciation (euros 18.8 million), including euros 5.6 million on the concession for transmission and dispatching activities.

Property, plant and equipment

The following table summarizes changes in this caption during the year:

In millions of euros	
INVESTMENTS	
Transmission lines	120.1
Transformation stations	148.8
Other	49.6
Total Investments	**318.5**
Depreciation	-171.4
Disposals and other changes	-18.5
TOTAL	**128.6**

Non-current financial assets

The increase in this caption (euros 371.0 million) is mainly due to investments, which relates to the following:

- the increase in the carrying amount of the investment in the subsidiary RTL SpA following the parent Terna SpA's capital injection totalling euros 416.8 million for the acquisition of AEM Trasmissione SpA and Edison Rete SpA;
- the euros 44.3 million reduction in the carrying amount of the Brazilian subsidiary Terna Participações following its IPO.

Net working capital amounts to a negative euros 455.9 million, down euros 264.6 million on 2005.

The main changes of the year are illustrated below.

Trade receivables

The increase of euros 178.0 million on 2005 is mainly due (euros 137.2 million) to receivable for electrical energy transmission and dispatching activities. Receivables relating to energy items include, in particular, deferred charges for participation in the ETSO-CBT (European Transmission System Operators - Cross Board Trade) agreements in relation to the offsetting of costs for the transmission of energy on foreign electricity grids. With Resolution no. 15/2005, AEEG guaranteed coverage of these charges, stating that the reimbursement methods would be defined in a specific measure.

Other assets

The decrease of euros 28.7 million is mainly due (euros 27.2 million) to the collection of interest on equity by the Brazilian subsidiaries during the year.

Net tax assets/(liabilities)

The increase of euros 97.7 million in net tax liabilities is due to IRES and IRAP of the year (euros 57.9 million) and VAT payables (euros 37.3 million).

Trade payables

The increase of euros 323.2 million in trade payables relates to payables for energy in transit (euros 276.2 million) which, as in the case of receivables for energy in transit, were affected by the longer accounting period with respect to 2005. Furthermore, increases of euros 47.0 million relate to non-energy suppliers due to more purchases of goods and services than in 2005, at the end of year for ordinary investing and operating activities.

Gross invested capital, amounting to euros 4,522.3 million, rose to euros 242.7 million.

Net invested capital, considering provisions of approximately euros 615 million, is substantially in line with 2005, showing an increase of euros 244 million to euros 3,907.4 million.

CASH FLOWS

Cash flow analysis

In millions of euros	2006	2005	Change
OPENING CASH AND INTERCOMPANY CURRENT ACCOUNT	**10.9**	**144.0**	**-133.1**
Profits for the year	355.8	265.6	90.2
Amortization and depreciation	190.1	157.0	33.1
Net change in provisions	-1.2	22.4	-23.6
Self-financing	**544.7**	**445.0**	**99.7**
Change in net working capital	264.6	-8.3	272.9
Cash flows generated by/(used in) operating activities	**809.3**	**436.7**	**372.6**
INVESTMENTS			
Property, plant and equipment	-318.5	-259.4	-59.1
Intangible assets	-26.5	-4.1	-22.4
Investments	-371.6	9.8	-381.4
Other changes in non-current assets	19.1	-208.9	228.0
Total cash flows generated by/(used in) investing activities	**-697.5**	**-462.6**	**-234.9**
Change in loans	144.4	131.9	12.5
Other changes in equity	14.0	0.9	13.1
Dividends	-266.0	-240.0	-26.0
Total cash flows generated by/(used in) financing activities	**-107.6**	**-107.2**	**-0.4**
Total cash flows of the year	**4.2**	**-133.1**	**137.3**
CLOSING CASH AND INTERCOMPANY CURRENT ACCOUNT	**15.1**	**10.9**	**4.2**

Change in net financial position

In millions of euros	2006	2005
OPENING NET FINANCIAL INDEBTEDNESS	**-1,865.5**	**-1,600.5**
Cash flows generated by/(used in) operating activities	**809.3**	**436.7**
Investments in property, plant and equipment	-318.5	-259.4
Investments in intangible assets	-26.5	-4.1
Sales (acquisitions) of investments	-371.6	9.8
Other changes in non-current assets	19.1	-208.9
Cash flows generated by/(used in) investing activities	**-697.5**	**-462,6**
Dividends distributed/collected	-266.0	-240.0
Other changes in equity	14.0	0.9
Self-financing flows	**-252.0**	**-239.1**
Change in financial indebtedness	-140.2	-265.0
CLOSING NET FINANCIAL INDEBTEDNESS	**-2,005.7**	**-1,865.5**

The cash flows generated by operating activities during the year amounted to approximately euros 809.3 million and are due to self-financing (profits for the year, amortization and depreciation and accruals totalling euros 544.7 million) and the contribution of cash flows (euros 264.6 million) generated by the management of working capital.

Investing activities used net financial resources of approximately euros 697.5 million in relation to various changes, particularly investments in property, plant and equipment and intangible assets of the year (euros 345 million), the capital injection in RTL (euros 416.8 million) for the acquisitions of RTM1 and RTM2 and the decrease of euros 44, 3 million in the carrying amount of the investment in the Brazilian subsidiary Terna Participações following its stock market listing.

Cash outflows for self-financing were mainly due to the distribution of dividends to shareholders (final dividend of 2005 and 2006 interim dividend) during the year.

Accordingly, total cash flows used by investing activities and self-financing generated a total requirement for the year of euros 949.5 million, which was mostly covered (euros 809.3 million) by cash flows generated by operating activities and residually (euros 140.2 million) by new indebtedness.

Net financial indebtedness

The following table details net financial indebtedness (euros 2,005.7 million) at year end with an analysis of timing:

In millions of euros	2006	2005	Change
A) MEDIUM AND LONG-TERM INDEBTEDNESS			
Bonds [1]	1,406.6	1,498.4	-91.8
EIB loans [1]	540.9	370.5	170.4
Derivative financial instruments [2]	-5.8	-77.0	71.2
Total A	**1,941.7**	**1,791.9**	**149.8**
B) SHORT-TERM INDEBTEDNESS (FUNDS)			
Bond (current portion)	0.0	0.0	0.0
EIB loans (current portion)	29.5	29.5	0.0
Short-term loans [3]	50.0	55.0	-5.0
Net balance of intercompany joint accounts			
RTL Group [4]	0.2	4.9	-4.7
Cash and cash equivalents [5]	-15.3	-15.8	0.5
Short-term loan to Terna Participações [6]	-0.5	0.0	-0.5
Total B	**64.0**	**73.6**	**-9.6**
NET FINANCIAL INDEBTEDNESS TOTAL A + B	**2,005.7**	**1,865.5**	**140.2**

In the financial statements of Terna SpA:

[1] the balance is included in “Long-term loans”;
[2] this corresponds to “Non-current financial assets” for the net fair value of FVH derivatives and trading derivatives (euros 12 million) and “Non-current financial liabilities”;
[3] the balance is included in “Short-term loans”;
[4] this corresponds to the algebraic sum of the balance of the intercompany current account held with the subsidiary RTM1 (euros 20.8 million), included in “Cash and cash equivalents” and the balances of the intercompany current accounts held with the subsidiaries RTL and RTM2 (euros 21.0 million), included in “Short-term loans”;
[5] the balance is included in “Cash and cash equivalents”; The balance is included in “Non-current financial assets”.

In carrying out its operations, Terna is exposed to the risk of fluctuations in interest rates. Its main source of interest rate risk relates to items of net financial indebtedness that generate interest expenses. Terna’s strategy for financial indebtedness is to focus on long-term loans, which reflect the useful life of Group assets. It pursues an interest rate risk hedging policy that aims to combine this choice with the regulatory context, which every four years establishes the cost of debt as part of the formula to set Regulatory Asset Based - RAB remuneration.

Accordingly, the hedging instruments used, at various maturity dates, include both derivatives that transform fixed rates into variable rates (fair value hedges) and derivatives that transform variable rates into fixed rates (cash flow hedges and trading).

With the aim of reducing the amount of financial indebtedness exposed to the risks of fluctuations in interest rates and reducing the cost of funding, two types of plain vanilla derivatives have been used, interest rate swaps and interest rate collars. At year end, considering the transactions in derivatives, 66.1% of Terna SpA's gross indebtedness bears interest at fixed rates, while net indebtedness bearing interest at fixed rates amounts to 67.2%.

All derivative contracts have a notional value and maturity date less than or equal to that of the underlying financial liability, so that any change in the fair value and/or projected cash flows of the contracts is offset by a corresponding change in the fair value and/or projected cash flows of the underlying position.

In terms of liquidity risk, considering that there is normally a negative difference between interest received on loans granted and interest paid on loans received, financial optimization activities are geared towards minimizing liquidity positions in line with the company's needs.

The following table provides the notional amount and fair value of derivatives, net of accruals, at 31 December 2006. The fair value of derivatives is measured by discounting estimated cash flows at market interest rates at the reporting date.

	NOTIONAL AMOUNT		FAIR VALUE	
In millions of euros	2006	2005	2006	2005
Derivatives hedging the fixed rate bond	1,400.0	1,280.0	11.3	106.1
Derivatives hedging variable rate loans	186.3	269.0	-6.2	-17.8
Other hedging derivatives	1,150.0	850.0	0.7	-11.2
TOTAL	**2,736.3**	**2,399.0**	**5.8**	**77.1**

The fair value of the two bonds (euros 600 million maturing in 2014 and euros 800 million maturing in 2024) was also measured by discounting estimated cash flows at market interest rates at the reporting dates, for a total of euros 1,406.6 million, net of accruals.

RESEARCH AND DEVELOPMENT

Research and development

Terna focuses on research and development with the aim of introducing technological solutions for plants, instruments and methods in order to boost the reliability of plants and, consequently, service quality, while making company processes more efficient.

A group of experts works in the field of engineering by carefully monitoring the functioning of equipment, with the support of a specialized IT system (MBI). This group constantly looks for improvements to be made to the equipment.

In particular, in 2006, the following projects were identified and implemented, or are being implemented:

- improvement of seals to reduce SF6 gas leaks (and reduce faults in equipment as well as gas emissions);
- use of containers made of composite materials (silicones) to replace porcelain, to reduce the effects of faults and, accordingly, damage to people and things;
- specification of new machinery to regulate voltage (reactors and capacitors) and to regulate flows (PSTs - Phase Shift Transformers);
- introduction of new compact integrated high voltage equipment systems to reduce the amount of space they occupy, as well as construction and management costs;
- new diagnostic methods for line insulators;
- new types of line conductors to increase transmission capacity;
- new station design software.

These activities were carried out by internal resources also operating in work groups - to encourage the spread of knowledge throughout the company - and with the specialized assistance of builders, universities and especially the associate Cesi SpA.

The following projects are planned for 2007:

- online equipment monitoring to continuously monitor the status of equipment integrity and localize faults;
- specification, inspection and installation of new equipment that is highly reliable, has higher shortcircuit voltage and is anti-seismic;
- optimization of the station design criteria;
- installation of new line design software.

Information Technology

During the year, Terna worked in various areas to better support its business and improve operational efficiency in the ICT field. In particular, it worked to:

- improve tools supporting core processes and, in particular, the security of the electrical system;
- boost the strength and efficiency of telecommunications systems;
- revise the sourcing strategy for IT systems managed by ENEL under a long-term service agreement.

Improvement of tools supporting core processes and the security of the electrical system

The most significant projects of the year were developed/launched in relation to the control, conduction and defense of the electrical system. In this respect, technological solutions were consolidated, the reliability of and recovery capacity of the system was improved and functions were expanded, as follows:

- The electricity grid control system (SCTI) was fully launched in Italy, with all its key functions. This will enable the company to achieve efficiencies and operating benefits in relation to the use of the same technological platform used by the conduction and dispatching processes, following the Terna and TSO integration;
- For the defense systems, various projects were carried out and significant innovation projects were commenced and will be completed in the next few years:
  - new remote release systems for electric power plants that operate in production groups limited by security restrictions were completed, to enable the softening of those restrictions;
  - loads served by lightening systems (EDA) were increased;
  - operations began on the construction of the new emergency measure system (BME) to interrupt widespread supply;
- The consolidation of geographic disaster recovery solutions is underway on control and conduction systems in relation to the Power Exchange for which the new data processing center has already been created. It is slated for completion in 2007;
- The functions of systems supporting the Power Exchange have been improved and updated to the new regulatory recommendations.

Strength and efficiency of telecommunications systems

Terna worked with the aim of strengthening its telecommunications system for management purposes and to support core processes and improve security and reliability, while taking advantage of the use of new technologies to significantly recover efficiency:

- it created a new Intranet using MPLS technology, enabling the company to unbundle its data networks from ENEL's and increase the available band width available for data transmission;
- it strengthened network and periphery security systems as part of a long-term programme that will be completed for both the management networks and those to support core processes;
- it completed testing on the power line communications and put them into use in Sicily and Sardinia to increase redundancies and, accordingly, the level of availability of the control and conduction grid for Terna-owned plants;
- the architecture and management of technical telephony was rationalized to increase operating efficiency.

Sourcing strategy for IT systems managed by ENEL under a long-term service agreement

The sourcing strategy for management systems (e.g., ERP) and office automation managed by ENEL under a service agreement was reviewed to take advantage of economies of scale and expertise arising from the integration with the TSO business activity. The integrated entity has a basic infrastructure and expertise that enable it to create supporting technologies at its own DPCs and have more efficient control over third parties.

These projects were substantially completed in the fourth quarter of 2006 and the expected benefits should be fully seen in 2007.

ORGANIZATION AND HUMAN RESOURCES

New organizational structure

The company's new organizational structure has been operative since 1 January 2006, as follows:

Audit Department, reports directly to the Chairman Departments reporting directly to the CEO:

- Procurement and Tenders;
- Administration, Finance and Control;
- Communications and External Relations;
- Regulatory Affairs;
- Institutional Affairs;
- Personnel and Organization;
- Corporate office and Legal Affairs (where an Authorization and Compulsory Purchase Procedure Management Office was subsequently created to carry compulsory purchase procedures);
- Systems and Technologies;
- International and Business Development;
- Italian Operations, which includes the following departments:
    - Grid Planning and Development;
    - Engineering (in which the Compulsory Purchase and Control Office was subsequently created to carry out compulsory purchase procedures);
    - Dispatching and Conduction;
    - Plant Maintenance;

    The Risk Management and Operating Process Business Continuity Departments report to the Director of Italian Operations.

The Investor Relations Department reports to the CEO.

The roles and responsibilities that go along with the individual activities are detailed as part of the organization. During the year, the company followed up on activities to complete organizational, process and systems initiatives, with the project to determine how to organize the dispatching and conduction process, through the integration of former Terna and former GRTN processes. The aim was to heighten the level of quality and security of the electrical system and improve operating efficiency.

The organizational model will enable the company to manage on a process-basis, while guaranteeing that operating objectives are in line with strategies. This will prevent activities that logically belong to the same

process from being spread out among more than one unit. It will also entail the assignment of clear-cut responsibilities for all stages of the process, preventing the scattering and inefficient use of skills and resources.
The processes affected by the new organizational model are: Real Time (control and remote conduction), System Engineering (defence and protection system planning and checks), Planning (production and grid structures) and Technologies and Process Systems (including Telecommunications and Metering).
The structure of the International and Business Development Department was reviewed with effect from 1 October 2006 and the Subsidiaries Coordination Department was eliminated. The organizational structure of Terna Participações was also reviewed at the same time.

ISO 9001 certification

In June, the accredited independent certification inspector (CSQ) conducted the surveillance and extension inspection for certification. This inspection entailed assessing whether the quality management system implemented had been maintained fully effective with respect to the requirements of the regulations. Moreover, it allowed the company to extend ISO 9001 - 2000 certification to the activities acquired with the integration of Terna and the business activity from GSE SpA (formerly GRTN).

Human resources

Changes in the number of Terna SpA employees are shown below.

	TERNA		
Change in the workforce	31.12.2006	31.12.2005	Change
Managers	71	74	-3
Junior managers	431	403	28
White collars	1,816	1,813	3
Blue collars	1,049	1,098	-49
TOTAL	**3,367**	**3,388**	**-21**

The figures for both years are net of retirement with effect from 31.12 (43 at 31.12.2006 and 59 at 31.12.2005).

The number of employees is slightly below that in the plan, which provides for the selective replacement of outgoing personnel to create a younger workforce and strengthen the organizational units involved in meeting the requirements of the investment, along with efficiency recoveries.

During the year, the company continued to pursue its commitment to consolidating and developing the expertise essential to its core business with specialized training, particularly for line personnel.

At the same time, to support the post-Terna/GSE SpA (formerly GRTN) business activity integration phase, Terna launched a plan of initiatives to develop/consolidate “soft” managerial and professional skills, in view of aligning the organizational culture and expertise of specific areas: Economics, Teamworking, People Management and Communications.

The plan targeted middle managers, team leaders and professionals, specifically adapted for each group in area and scope.

All of middle management was involved in an initiative focused on the creation of value.

Continuing programmes launched in 2005, newly hired employees were involved in initiatives aimed at helping them acquire specialized and soft skills to support their collaboration with the company, as well as speed up the development process.

2,928 employees participated in at least one training course. In particular, 2,689 employees participated in at least one traditional course, while 820 took part in online training, using the company’s remote training platform.

At the end of 2006, in the field of internal communications, the first “People Satisfaction Survey” was planned for early 2007. It will involve all company employees. The aim is to obtain guidelines for measures to improve the organizational environment, a key factor in the company’s ongoing improvement and growth.

Long-term incentive plans

Long-term managerial incentive schemes include an MBO plan for senior and middle management, with particularly challenging company objectives.

In addition, the company launched the 2006 stock option plan (approved on 21 December 2005), for Terna Group managers in key positions with respect to the achievement of strategic group results. The beneficiaries of the plan include the CEO as company manager.

Reference should be made to the notes for the features of this stock option plan.

A long-term cash-based incentive plan based on the achievement of challenging long-term objectives has been set up for managers not benefiting from the stock option plan.

Relationships with the unions

During the year, talks with the unions led to the development of negotiations to renew the national labor contract of 24 July 2001 for employees in the electricity sector, which expired on 30 June 2005.

The agreement for this renewal was signed on 18 July 2006 by Assoelettrica, Federutility, Enel SpA, Terna SpA, GSE SpA and Sogin SpA.

In particular, with respect to the economic part of the agreement covering the two years from 1 July 2005 to 30 June 2007, the average increase in the minimum contractual remuneration amounts to euros 111.00, with the payment of a lump-sum average of euros 328.00 for the period from 01 July 2005 to 31 December 2005.

RELATED PARTY TRANSACTIONS

Related party transactions carried out by the company during the year included those with its subsidiaries, the associate Cesi SpA and the employee pension funds FONDENEL and FOPEN.

The company's corporate governance rules, which are detailed in the specific section of this report, to which reference should be made, establish the necessary conditions to ensure that related party transactions are carried out correctly, in terms of procedure and substance and at the same conditions that would be applied to transactions with third parties.

Related party transactions are indicated in the notes to the individual financial statements captions. Reference should be made to the summary included in "Related party transactions".

Moreover, transactions carried out with members of the parent's Board of Directors and Board of Statutory Auditors, specifically with respect to fees, bonuses and other incentives, are detailed in the notes to the caption "Services".

Shares held by Directors, Statutory Auditors, General Managers and Key Managers

As required by the provision of Article 79 of Consob Resolution no. 11971/99, the following table lists the shares of Terna SpA and the companies under its control held by Directors, Statutory Auditors, General Managers and Key Managers, in addition to their spouses (unless legally separated) and minor children, either directly or indirectly through subsidiaries, trustees or nominees, as per the shareholders' book, communications received or other information obtained from the members of the Boards of Directors and Statutory Auditors, General Managers and Key Managers. These include all those persons who, in 2006, filled the office of Director, Statutory Auditor, General Manager and Key Managers.

DISCLOSURE ON THE SHARES HELD BY DIRECTORS AND THE STATUTORY AUDITORS

	Company in which investment is held	Number of the shares at the end of the previous year (2005)	Number of shares acquired in 2006	Number of shares sold in 2006	Number of shares held at the end of the current year (2006)	Type of ownership (1)
Luigi Roth	Terna SpA	0	0	0	0	-
	Terna Participações	-	1	0	1	ownership
Flavio Cattaneo	Terna SpA	0	0	0	0	-
	Terna Participações	-	1	0	1	ownership
Luigi De Paoli	Terna SpA	7,805 (2)	1,536	0	9,,341(3)	ownership
Mario Garraffo	Terna SpA	0	0	0	0	-
Claudio Machetti (4)	Terna SpA	0	0	0	0	-
Salvatore Machì	Terna SpA	0	0	0	0	-
Carmine Macrì	Terna SpA	0	0	0	0	-
Piero Giuseppe Maranesi	Terna SpA	0	0	0	0	-
Vittorio Rispoli (5)	Terna SpA	0	0	0	0	-
Franco Smurro	Terna SpA	0	0	0	0	-
Massimo Ponzellini (6)	Terna SpA	2,000	0	0	2,000	ownership
Massimo Romano (7)	Terna SpA	13,200	0	0	13,200	ownership
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	ownership
Vito Di Battista	Terna SpA	0	0	0	0	-
Bruno Franceschetti	Terna SpA	0	0	0	0	-

(1) This column - which is in addition to the format provided by appendix 3C) of Article 79 of Consob Resolution no. 11971/99 to indicate the information required - is shown if the investment is held as a result of ownership, a pledge, beneficial ownership, on deposit, as collateral, etc...
(2) including: 5,204 personally and 2,601 held by his spouse.
(3) including: 6,740 personally and 2,601 held by his spouse.
(4) In office since 21 March 2007.
(5) In office since 13 July 2006.
(6) In office up to 3 July 2006.
(7) In office up to 16 March 2007.

CORPORATE GOVERNANCE

SECTION I:
THE CORPORATE GOVERNANCE STRUCTURE

Introduction

Terna complies with the new Code of Conduct for listed companies published by Borsa Italiana in March 2006. It has approved updates to the corporate governance system in place to meet its commitments arising therefrom, as described below.

The Corporate Governance system in place at Terna is in line with the principles of the Code of Conduct for listed companies, Consob recommendations in this respect and, more generally, international best practices. This corporate governance system is mainly based on creating value for shareholders, taking into account the social significance of the group's activities and the resulting need to adequately consider all stakeholders in the performance of those activities.

Additional steps taken to improve the corporate governance system are underway and others will be considered as part of Terna's constant updating to best practices.

Shareholding structure

The company's share capital is comprised exclusively of ordinary shares, which are fully paid-up and bear voting rights at both the ordinary and extraordinary shareholders' meetings.

On the basis of the shareholders' book, communications received pursuant to Consob Resolution no. 11971/99 and available information, the following investors hold more than 2% of the share capital: Cassa Depositi e Prestiti SpA (public limited company in which the Italian Ministry of Economy and Finance owns 70%) with 29.999%; Pictet Asset Management SA with 5.15%; Enel SpA with 5.119%; Assicurazioni Generali with direct and indirect investments of 4.928%; Barclays Global Investors N.A. with 2.031 %; and Barclays Global Investors Ltd with 2.009%.

No other investors own more than 2% of Terna SpA's share capital and the company is not aware of the existence of any shareholders' agreement relating to company shares.

Company organization

In accordance with the provisions of Italian legislation concerning listed companies, the company's organization includes the following:

- a Board of Directors responsible for company management;
- a Board of Statutory Auditors responsible for monitoring: (I) that the company complies with the Law, the memorandum of association and the principles of correct administration in performing company activities, (II) the adequacy of the company's organizational structure, internal control system and administrative/accounting system. It is also responsible for carrying out all duties assigned to the Board of Statutory Auditors by Law and the Code of Conduct for listed companies;
- the shareholders, called for ordinary and extraordinary meetings to resolve on, *inter alia*, (I) the appointment and revocation of members of the Boards of Directors and Statutory Auditors and their fees and duties, (II) the approval of the financial statements and allocation of the profits for the year, (III) the purchase and sale of treasury shares, (IV) amendments to the by-laws, and (V) the issue of convertible bonds.

Auditing activities are conferred on a specialized company registered with Consob, which is specifically appointed by the shareholders with the prior approval of the Board of Statutory Auditors.

Terna's auditors also have similar engagements with its main subsidiaries. Under the provisions of the managerial and administrative model adopted by the company pursuant to Legislative Decree no. 231/01, which was recently updated, the company engaged to audit the financial statements of the company and any of its group companies, as well as the consolidated financial statements, cannot provide any advisory services to Terna or any other group company. This restriction applies to the audit company's entire network, and includes its shareholders, Directors, members of the control bodies and employees of the audit company and other companies that are members of the same network. Terna is currently verifying the amendments necessary to update its by-laws to recent legislation concerning listed companies that was introduced by Law no. 262 of 28 December 2005 and Corrective Decree no. 303 of 29 December 2006, as well as Consob Regulations currently implementing that legislation.

SECTION II:
IMPLEMENTATION OF THE PROVISIONS OF THE CODE OF CONDUCT FOR LISTED COMPANIES AND ADDITIONAL INFORMATION

Board of Directors

Role and functions

The company's Board of Directors fills a crucial role in its organization. It has strategic and organizational functions and responsibilities with respect to the company and group.

It is also responsible for verifying that the necessary controls are in place to monitor the performance of the company and its subsidiaries.

In this context and in accordance with the Law and the provisions of specific resolutions, the Board of Directors:

- delegates and revokes powers to one or more Directors, defining the content, limitations and methods of such powers. The current structure of the Board of Directors provides for only one CEO. The powers currently conferred on him give the CEO the widest ranging powers for administration of the company, except for those conferred by the law or the by-laws or reserved of the Board of Directors by resolution thereof;
- receives, similarly to the Board of Statutory Auditors, constant and exhaustive updates from the CEO on activities performed during the year in accordance with powers in specific quarterly reports. In particular, with respect to all significant transactions carried out by the company and its subsidiaries (including any related party transactions which do not require approval by the Board of Directors) the CEO reports to the Board of Directors on their (I) features, (II) the parties involved and their relationship with the company or its subsidiaries;
- determines the remuneration of the CEO and other Directors with special duties on the basis of proposals made by the specific committee and with the approval of the Board of Statutory Auditors;
- evaluates the adequacy of the general organizational, administrative and accounting structure of the company and its subsidiaries that hold strategic importance (in accordance with the Board's Resolution of 22 February 2007, these are: a) subsidiaries listed on regulated markets and b) subsidiaries that have a significant foreign market share in the group's core business), with specific reference to the internal control system and management of conflicts of interest;
- examines and approves strategic, business and financial plans. In this respect, the current structure of company powers provides that, in particular, the Board of Directors approves the company's annual

budget and long-term plans (which include the combined annual budgets and long-term plans of the subsidiaries) prepared by the CEO;

- examines and approves transactions with a significant impact on the company's financial position and results, especially if they are related party transactions or could otherwise give rise to a potential conflict of interest. In particular, the following transactions, *inter alia*, are submitted to the Board of Directors in advance: (I) "significant transactions" carried out directly or through subsidiaries for which the underlying item, consideration, method or timing could have an impact on the safeguarding of company assets or the completeness and accuracy of Terna's accounting and other information and which require Terna to disclose to the public an informational document in compliance with the supervisory authorities of financial markets and/or transactions for more than euros 20 million, except for those approved in the budget and agreements relating to dispatching and all other related services; (II) related party transactions carried out directly or through subsidiaries for more than euros 2,000,000 each, except for those approved in the budget and agreements relating to dispatching and all other related services;
- arranges for the exercise of voting rights at the shareholders' meetings of subsidiaries and other investees;
- assesses the general performance of company operations, with specific reference to situations of conflict of interest, on the basis of the information received from the CEO and Internal control committee, periodically checking that planned results have been achieved;
- at least once a year, evaluates the size, composition and functioning of the Board of Directors and its committees;
- reports to the shareholders.

Appointment, composition and term of office

In accordance with the provisions of the company's by-laws, the Board of Directors is made up of seven to thirteen members who are appointed for a period not longer than three years. They may be reappointed at the end of their term. Another Director without voting rights may be appointed by the Italian government, pursuant to privatization regulations. To date, the Italian government has not yet used this appointment power.

The company's Directors must meet certain integrity and professionalism requirements, similar to those required of the Statutory Auditors of listed companies.

Furthermore, at least one-third of the Directors in office must meet the specific independence requirements of Article 15.4 of the by-laws pursuant to Article 3 of the Prime Minister's Decree of 11 May 2004. Lastly, considering the particular activities performed by the company, the independence requirements of Article 10 of Directive no. 2003/54/EC, as specified in Article 15.5 of the company's by-laws, also apply to the executive Directors.

In accordance with privatization regulations, the requirements of the Prime Minister's Decree of 11 May 2004 and Italian legislation concerning listed companies, the by-laws also require that the entire Board of Directors be appointed using the list system, to ensure that three-tenths of the Directors to be appointed (rounding up in the event of small fractions) are from minority lists. In line with the provisions of Article 4 of Decree Law no. 332 of 31 May 1994, converted into Law no. 474-94 (privatization law), this system provides that the lists of candidates can be presented by the outgoing Board of Directors or shareholders that, alone or jointly with other shareholders, hold at least 1% of the share capital. Moreover, the lists are filed at the registered offices and published in national newspapers suitably far in advance of the date of the shareholders' meeting; at least 20 days in advance if the list is submitted by the outgoing Board of Directors and at least 10 days in advance if the lists are submitted by shareholders. This ensures that the procedure for the appointment of the Board of Directors is transparent, in accordance with the provisions of the privatization law.

Thorough information on the personal and professional background of the candidates should be given, along with an indication of whether they are eligible to qualify as independent on the basis of the requirements of the Law, the Code of Conduct and the by-laws, when the candidatures are submitted at the registered offices along with the lists. In addition, they should be immediately published on the company's website, on the basis of a specific reference included in the notice calling the shareholders' meeting.

Lastly, in implementation of the requirements of the Prime Minister's Decree of 11 May 1994 for electricity sector operators, the by-laws set a limit of 5% of share capital for the exercise of voting rights for the appointment of Directors.

A specific appointment committee within the Board of Directors has not yet been created, as the shareholders have not had any difficulties in submitting suitable candidatures that constitute a board in line with the recommendations of the Code of Conduct for listed companies.

The shareholders establish the fees of each Director.

A portion of the executive Directors' fees is linked to the company's results and the achievement of specific objectives that the Board of Directors specifies in advance.

Non-executive Directors receive fees commensurate with the commitment required of each of them, considering their participation on one or more committees. Fees are not linked to the company's results. Non-executive Directors are not beneficiaries of sharebased incentive plans.

In accordance with the shareholders' resolution passed during the ordinary meeting held on 2 November 2005, the Board of Directors currently in office is comprised of ten members, whose term will lapse with the approval of the financial statements as of and for the year ended 31 December 2007. Following the resignation of two Directors, during the meetings of 13 July 2006 and 21 march 2007, the Board of

Directors resolved to coopt Vittorio Rispoli and Claudio Machetti, respectively. Following those appointments, the Board is currently comprised of the members listed below. A brief description of their professional background is also provided:

- *Luigi Roth, 66 years old - Chairman*

  With a degree in Business Administration from Università Bocconi, Milan, since 2001, Mr. Roth has serviced as Chairman of the Fondazione Fiera Milano and has been Deputy Chairman of Cassa Depositi e Prestiti SpA since 2004. Currently, he also serves as Director of Telecom Italia SpA. He was appointed Deputy Chairman of Terna Participações SA, a subsidiary of Terna SpA in May 2006.

  Mr. Roth began his career as a business manager with the Pirelli Group, handling activities in Italy and abroad. He then jointed Metropolitana Milanese as Director of Planning. Since 1980, he has managed mid-sized companies in the manufacturing and real estate sectors, in the positions of General Manager and CEO. From 1986 to 1993, he served as CEO of Ernesto Breda SpA; from 1993 to 2001 he was Chairman and CEO of Breda Costruzioni Ferroviarie SpA; From April 1996 to January 1998, he was Chairman of Società Ferrovie Nord Milano SpA; from December 1996 to January 1998, Chairman of Società Ferrovie Nord Milano Esercizio SpA; from May 1998 to December 2000 he was CEO of Ansaldo Trasporti SpA and transmission agent for Finmeccanica SpA.

- *Flavio Cattaneo, 43 years old - CEO*

  With a degree in Architecture from the Milan Politecnico, Mr. Cattaneo has also specialized training in business management. He has been Chairman of Terna Participações SA, a subsidiary of Terna SpA, since March 2006. He has filled important managerial and administrative positions in various Italian companies in the radio and television service, new technologies, building, public service and facilities sectors. He became head of the former Ente Autonomo Fiera Internazionale di Milano as Extraordinary Commissioner in 1999 and went on to oversee its stock market listing as Fiera di Milano SpA, serving as Chairman and CEO until 2003. He has been Director of many energy companies (from 1999 to 2001), including AEM SpA of Milan (as Deputy Chairman), Serenissima Gas, Triveneta Gas SpA, Seneca Srl and Malpensa Energia. He was appointed head of Italy's public television network RAI SpA in April 2003, in the position of General Manager, which he held until August 2005. He also oversaw the merger with Rai Holding and the unbundling of accounts.

- *Luigi De Paoli, 57 years old - Director*

  With a degree in Engineering from the Milan Politecnico, Mr. De Paoli is a Professor of Applied Economics (economy of energy and the environment) and Director of the Master's in Economics and Environmental Management at Università Bocconi of Milan.

  He was appointed Director of Sogin SpA in February 2007 and Cesi SpA - Centro Elettrotecnico Sperimentale Italiano SpA in April 2006. He is also Director of the "Economia delle fonti di energia e dell'ambiente" (Economics of energy sources and the environment) magazine and a member of the scientific council of Gaz de France and Director of AIEE, the Italian association of energy economists.

  He has filled various teaching positions with universities in Italy and abroad. From June 1999 to May 2002, he was Director of ENI SpA. Mr. De Paoli is also on various ministerial commissions for the development of the Italian energy sector, the reorganization of the electricity sector, public utilities and tariff regulation. He is the author of many publications in the economics and energy fields.

- *Mario Garraffo, 69 years old - Director*

  With a degree in Business Administration from Università Bocconi, Milan, he has filled many increasingly important managerial and administrative positions in various Italian companies. He served as Controller and Development Manager of La Centrale Finanziaria Generale from 1960 to 1970; Investment Manager of the IFI Group from 1970 to 1980; CEO of IFIL-Finanziaria di Partecipazioni from 1980 to 1985; Chairman of IFINT (now EXOR) from 1985 to 1993; CEO of Lazard Italia from 1993 to 1998 and UNIM-Unione immobiliare from 1998 to 2000; and Chairman of General Electric Italia from 2000 to 2004. He is currently an independent Director and member of the Executive committee and Remuneration committee of Recordati SpA, as well as independent Director of Pirelli & C. SpA and CIS Holding (Interporto Campano) of Naples. He is also a Director of RCN Finanziaria and Virtus Holding SpA and trustee of the Johns Hopkins School for Advanced International Studies (SAIS) of Bologna.

Lastly, he is on the Board of Directors of the Fondazione Donna Javotte Bocconi (founding body of the Università Bocconi).

- *Claudio Machetti, 48 years old - Director*

Mr. Machetti has a degree in Statistics from the Rome's Università "La Sapienza". He was appointed CFO of Enel SpA in March 2000. Within the Enel Group, he also serves as Chairman of the Board of Directors of Enel.Factor SpA and Enel Investment Holding BV and Director of Enel Finance International SA, Enel Ireland Finance Ltd, Enel Green Power International SA, Enel.Re Ltd, Enel Trade SpA, Enel.NewHydro Srl, Enel Capital Srl, and Enel Energy Europe Srl.

He began his career as business manager in 1983 in the Financial Department of Banco di Roma. From 1992 to 2000, he held various positions with Ferrovie dello Stato SpA (assistance to the CFO, head of the Financial Markets Central Service, Operating Finance Manager) taking over Fercredit SpA in the FS Group as CEO in 1997. From April 2004 to November 2005 he was Director of Terna SpA.

- *Salvatore Machì, 69 years old - Director*

He holds a degree in Electronic Engineering and has received specialized training at the Istituto Superiore di Telecomunicazioni, in addition to his professional experience with Esso and IBM. He joined Enel in 1965 and filled various positions up to 1999, including Manager of the Transmission Department, Italian manager of Thermoelectrical Energy Generation and Purchase and Tender Manager.

He was CEO (from July 1999 to April 2000) and Chairman (up to July 2003) of the Gestore della Rete di Trasmissione Nazionale SpA, and Director of Gestore del Mercato Elettrico SpA during that time. He has been on the Board of Directors of Cesi - Centro Elettrotecnico Sperimentale Italiano SpA since March 2003, where he previously (from July 1999 to October 2001) served as CEO. He is currently Director of Api Energia SpA and, since September 2004, a Director of Terna SpA as well.

- *Carmine Macrì, 57 years old - Director*

  With a degree in Law from Rome's Università degli Studi "La Sapienza", he is a lawyer before the Court of Cassation, Italy's highest court.

  Since 1996, he has been a Professor of Bank Law and Legislation with the Business Administration Department of Rome's II Università "Tor Vergata", after having held various academic positions since 1986. From 1997 to 2003, he was Director of Italgas SpA.

  He provided advisory services for eight years to the association of Italian savings and loans banks (ACRI).

  In the autumn of 2004, he became Director of Sudgest Scarl, a company that is owned by the Ministry of Public Services through "Formez".

- *Piero Giuseppe Maranesi, 65 years old - Director*

  With a degree in Physics, he is a Professor of Electronics with Milan's Università degli Studi, Director of a research laboratory and Master's in Electronics and Digital Systems course of study.

  He has also taught at Milan's Politecnico and the Parma and Brescia universities and has worked in research laboratories in the United States and Japan. He has filled various management positions at the Institute of Electrical and Electronic Engineers (IEEE) of which he is a Fellow Member, including Director of the Power Electronics Society from 1990 to 1996, He was founding chairman of Transparency International Italia in 1995. From 1997 to 2001, he has served as Councillor for the Province of Como, with duties relating to the university and tourism.

  He is specialized in the static conversion of electrical power and published two printed volumes and over 100 scientific papers.

- *Vittorio Rispoli, 47 years old - Director*

  With a degree in Law from Rome's Università degli Studi "La Sapienza", he is a lawyer and a registered auditor. He has been Deputy General Manager of Assicurazioni Generali SpA since April 2003, independent Director of Autostrada Torino-Milano SpA and Director of Toro Assicurazioni SpA, Emittenti Titoli SpA, SARA Assicurazioni SpA, SARA Vita SpA, FATA Assicurazioni Danni SpA, FATA Vita SpA, Generali Properties SpA, Generali Properties Asset Management SpA, UMS Generali Marine SpA, Immobiliare Diciannove SpA, Prunus SpA and the Fondazione Assicurazioni Generali (for which he serves as general secretary).

  He has filled increasingly important managerial positions in the field of legal and corporate affairs with leading industrial and insurance groups. He has been with Sofin since 1984 and Alitalia since 1990, where he served as secretary of the Board of Directors and Executive committee as well as manager of "corporate insurance and security" for that group and with Alinsurance (since 1995). He has also held various positions as Director and/or Statutory Auditor of the investees. He has worked for INA SpA since 1997, where in 1999, he was also appointed secretary of the Board of Directors and the Executive committee. Since 2001, he has been central manager of Assicurazioni Generali SpA and secretary of the Board of Directors, the Executive committee, the General board and the Internal control and Remuneration committees. He is also on Generali's Supervisory board, created in accordance with Legislative Decree no. 231/01 and serves as Chairman of that board for some of its subsidiaries.

• *Franco Smurro, 49 years old - Director*

Mr. Smurro holds a degree in Education from Rome's Università degli Studi "La Sapienza". After doing academic work for the II Chair of Special Education with Rome's Università "La Sapienza" in 1986/1987, he began his managerial career with Telecom Italia SpA in External Relations from 1987 to 1997. From 1997 to 2001, he provided advisory services to the Anti-Trust Authority for the Communications Sector and, until 2002, for Nortel Networks SpA and Bull SpA up to 2004. He was appointed Director of Asteimmobiliari SpA in May 2005.

All the Directors accept their appointment to office when they believe they can devote the necessary time to the diligent performance of their duties - also considering the positions they hold outside the company in other companies listed on regulated markets (in Italy and abroad), financial companies, banks, insurance companies and significantly large companies - and to devote the necessary time to the diligent performance of their duties, as they are well aware of the responsibilities of the office held.

To this end, during the meeting of 22 February 2007, the Board of Directors approved its own guidelines regarding the maximum number of positions as Director or Statutory Auditor in significantly large companies that can be held and still enable the efficient performance of the duties as Director of Terna SpA.

For this purpose, "significantly large companies" were defined as:

a) companies with shares listed on regulated markets, in Italy or abroad;

b) Italian or foreign companies with shares not listed on regulated markets, and operating in the insurance, banking, brokerage, asset management or financial sectors. With respect to the latter, financial companies are only those subject to prudent supervision by the Bank of Italy and registered with the special list provided for by Article 107 of Legislative Decree no. 385/1993 (i.e., "Consolidated banking act"); foreign companies are evaluated on the basis substantial equivalents;

c) other Italian or foreign companies with shares not listed on regulated markets, not operating in the sectors listed in letter b) but that exceed at least two of the following parameters: they have 250 employees or workers, annual turnover of euros 50 million or an annual financial statements total of euros 43 million; companies that prepare consolidated financial statements.

The Board has identified general criteria for the different commitments required of each role (executive Director, non-executive and/or independent Director and standing Statutory Auditor), considering the nature and size of the company in which the positions are held and whether they are part of the Terna Group or are Terna's investees. A "weight" was assigned to each type of position for the purposes of assessing the commitment required, and the Directors also established that the role of executive Director of Terna is incompatible with the same role of another significantly large company.

Where more than one position is held within the same group, including employment by one of the group companies, only the position with the greatest "weight" is considered.

All the Directors hold a number of positions that is compatible with the guidelines set by the Board.

The summary of each Director's background includes information on the positions they hold. The number of positions in significantly large companies is determined on the basis of the criteria indicated in the procedure described. The total number of positions held is provided in the attached tables.

The relevant company functions constantly update the Directors on important changes to legislation and regulations affecting the company and the performance of its functions.

The Directors meet regularly and carry out their duties autonomously with full knowledge of the facts, pursuing the objective of creating value for shareholders, with the awareness of social significance of the group's activities and the resulting need to adequately consider all stakeholders in the performance of those activities.

Evaluation of the functioning of the Board of Directors

For the first time, Terna's Board of Directors assessed its size, composition and functioning, as required by the Code of Conduct published by Borsa Italiana. The Board drew on the assistance of a specialized independent consultant to ensure the utmost objectivity of its evaluations.

The independent consultant's analysis, which was conducted on the basis of in-depth individual interviews with each Director and the subsequent quantitative and qualitative analysis of the information gathered, focused on many aspects relating to: a) the size, composition and level of functioning and efficiency of the Board and its committees; b) the identification of elements that could prevent or improve the functioning and efficiency of the Board and its committees.

Based on the findings of these analyses, the Board of Directors' evaluation of its size, composition and the functioning of the Board and its committees was positive overall.

In particular, the Board emphasized the main aspects that make it possible to carry out its duties in an informed and knowledgeable manner. They are: direct and open discussion during meetings; respect for the contribution of each member; everyone's constructive willingness to reach consensual solutions; expertise and access to executive management; transparency and timeliness of information prepared by the CEO before Board meetings and that presented verbally during meetings; and Board discussions.

Board meetings and the Chairman's role

During the year, the Board met 14 times, with the Directors regularly participating and each meeting lasting an average of two hours. The Board of Statutory Auditors also attended.

The Chairman coordinates the activities of the Board of Directors. He calls the Board meetings, establishes the agenda and leads the meetings, ensuring that the Directors have been provided with the necessary documentation and information in a timely manner - except in urgent circumstances - so that they may knowledgeably discuss the issues submitted for their examination. The Chairman also verifies that Board resolutions are implemented, heads the shareholders' meetings and, along with the CEO, is the legal representative of the company.

Furthermore, on the basis of the Board's Resolution of 2 November 2005, the Chairman is responsible for (I) handling the company's relationships in Italy and abroad with institutions, public and administrative, national and international, central and local bodies and entities, as well as financial institutions, banks, insurance companies and social security institutions, private bodies, individuals and companies, and also oversees international relations, in collaboration with the CEO, in addition to (II) supervising internal auditing activities.

Non-executive Directors

The majority of the members of the Board of Directors are non-executive. Their number, reputation and available time ensures that their judgment has a significant impact on Board decisions.

Non-executive Directors contribute their specific expertise to Board discussions, in order to encourage an examination of the matters in question from different standpoints, ensuring that resolutions passed have been thoroughly and knowledgeably considered and are in line with the company's interests.

Except for the CEO, all other nine members of the Board of Directors (Luigi Roth, Luigi De Paoli, Mario Garraffo, Claudio Machetti, Salvatore Machì, Carmine Macrì, Piero Giuseppe Maranesi, Vittorio Rispoli and Franco Smurro) are non-executive.

In this respect, not even the Chairman has an executive role within the company. His significant functions, described above, within the group - in connection with his role and conferred on him by the by-laws, as guarantor of the application of correct corporate governance rules within the Board of Directors, in addition to the duties conferred on him by the Board and those he carries out in the supervision of internal auditing activities - are not specific management duties.

Independent Directors

A suitable number, also with respect to their expertise, of non-executive Directors are also independent. On 21 March 2007, the Board of Directors - having defined the criteria for non-executive Directors to be qualified as independent in advance, in line with those provided for by the Code of Conduct and on the basis of the information given by the individuals concerned - announced that the following seven Directors met the independence requirements: Luigi De Paoli, Mario Garraffo, Salvatore Machì, Carmine Macrì, Piero Giuseppe Maranesi, Vittorio Rispoli and Franco Smurro.

At that time, the Board of Statutory Auditors verified that the criteria defined and the procedures adopted by the Board had been correctly applied.

Although independence of judgement characterizes the activity of all executive and nonexecutive Directors, the presence of Directors who can be qualified as "independent", in accordance with the above criteria, and whose role on the Board and its committees is significant, suitably ensures adequate consideration of all members' interests.

The evaluation carried out by the Board confirmed that the seven independent Directors met the independence requirements provided for by Article 15.4 of the by-laws, which states, in particular, that one-third of the Directors in office may not:

(I) directly, indirectly or on behalf of third parties carry out, or recently have carried out, significant transactions with the company, its subsidiaries, executive Director or majority shareholder that would influence his/her personal judgement;

(II) directly, indirectly or on behalf of third parties own investments such that would enable him/her to exercise control or significant influence over the company, including through shareholders' agreements;

(III) be a close relative of an executive Director or any of the parties listed in points (I) and (II).

Committees

Remuneration committee

In 2004, the Board of Directors set up the Remuneration committee, responsible for making proposals to the Board (I) for the remuneration of the CEO and other Directors with special duties and (II) for determining the remuneration criteria of top management of the company and its subsidiaries, on the basis of indications provided by the CEO.

Following the renewal of the Board of Directors, during the meeting held on 16 November 2005, the committee was reconstituted and its members were appointed.

The Remuneration committee is currently composed of Vittorio Rispoli (as coordinator), Mario Garraffo, Carmine Macrì, Luigi Roth and Franco Smurro, all non-executive Directors and most of whom are also independent.

During the year, the Remuneration committee held three meetings, with the regular participation of all members. The meetings lasted an average of one and a half hours each. None of the Directors participated in the committee meetings in which proposals regarding their remuneration were put forward to the Board of Directors.

As part of its duties, the Remuneration committee has a key role in implementing specific stock options plans for management. These are incentive and loyalty plans aimed at attracting and motivating resources at the right levels and with adequate experience, increasing their sense of belonging and ensuring they are constantly focused on creating value.

Furthermore, with respect to the remuneration of the CEO and other Directors with special duties, during the year, the committee made specific proposals to the Board of Directors that provided for a portion of the executive Director's fees to be based on the company's results and the achievement of specific objectives indicated in advance by the Board. In addition, during the meetings held in 2006, the Remuneration committee made proposals to the Board of Directors concerning the incentive plans for management of the company and its subsidiaries.

Minutes were prepared for all of the committee's meetings.

During the meeting of 24 January 2007, the Board of Directors evaluated the duties and functioning of the committee and adopted - after the committee's examination - a specific "Organizational regulation for the remuneration committee of Terna SpA" identifying the criteria for its composition, duties and responsibilities, in accordance with the provisions of Articles 5 and 7 of the new Code of Conduct, as well as how the committee's meetings should be held. The committee was given the power to access information and company functions necessary and hire independent experts in order to carry out its duties. Adequate financial resources were allocated to the committee for this purpose.

Internal control committee

In 2004, the Board of Directors also created a specific Internal control committee, with advisory and proposal-making functions.

Following the renewal of the Board of Directors during the meeting of 16 November 2005, the Internal control committee was reconstituted and its members were appointed.

The committee was assigned the following duties, in particular:

- assisting the Board of Directors in establishing internal control system guidelines and periodically checking the adequacy and effective functioning thereof;
- evaluating the work plan prepared by the Internal control manager and receiving regular reports therefrom;
- evaluating the adequacy of the accounting policies applied and their consistency for the purposes of the consolidated financial statements, along with the company's administrative managers and the independent auditors;
- evaluating the independent auditors' proposals to obtain the audit engagement, as well as the work plan prepared for the audit and the findings expressed in the auditors' report and management letter;
- report to the Board of Directors at least twice a year on the activities performed and the adequacy of the Internal control system;
- carry out any other duties requested by the Board of Directors, especially in relation to the independent auditors.

The Internal control committee is currently comprised of Mario Garraffo (as coordinator), Luigi De Paoli, Salvatore Machì and Piero Giuseppe Maranesi, who are all non executive and independent Directors. At least one member has adequate accounting and financial experience.

During the year, the Internal control committee met seven times, with the regular participation of all members. Each meeting lasted an average of one and a half hours, and the Chairman of the Board of Statutory Auditors or another Statutory Auditor appointed thereby was present at each meeting, given the Board's specific supervisory functions with respect to the internal control system, as required by current legislation concerning listed companies.

In particular, during the year, the Internal control committee examined the guidelines for the internal control system and audit activities, and also met with the independent auditors. In addition, the committee examined the integrations and updates to the organizational and management model adopted pursuant to Legislative Decree no. 231/01, submitted to the Board of Directors.

Minutes were prepared for all of the committee’s meetings.

During the meeting of 24 January 2007, the Board of Directors evaluated the duties and functioning of the committee and adopted - after the committee’s examination - a specific “Organizational regulation for the Internal control committee of Terna SpA” identifying the criteria for its composition, duties and responsibilities, in accordance with the provisions of Article 5 of the new Code of Conduct. In the regulation, the Board also identified the roles and responsibilities of the committee in accordance with the provisions of Article 8 of the new Code of Conduct, in line with the guidelines for the Terna Group’s internal control system, as defined by the Board on 21 December 2006.

The committee was assigned additional specific duties under the organizational model adopted by Terna pursuant to Legislative Decree no. 231/01 and Terna’s new Code of Ethics.

The committee was given the power to access information and company functions necessary and hire independent experts in order to carry out its duties. Adequate financial resources were allocated to the committee for this purpose.

Board of Statutory Auditors

In accordance with the provisions of the company’s by-laws, the Board of Statutory Auditors is comprised of three standing auditors and two alternate auditors, who are appointed for a period of three years and may be re-appointed at the end of their term.

All members of the Board of Statutory Auditors must meet the integrity and professionalism requirements required by special legislation for statutory auditors of listed companies, as an integration to the specific provisions of the Italian Civil Code.

Moreover, in accordance with the by-laws, they may not be standing auditor of five or more companies that have issued securities listed on regulated markets.

In line with that provided for with respect to the Board of Directors, the by-laws require that the entire Board of Statutory Auditors be appointed using the list system, to ensure that the Board includes one standing auditor and one alternate auditor from minority lists.

This system provides that the lists of candidates can be presented by shareholders that, alone or jointly with other shareholders, hold at least 1% of the share capital, in line with the privatization law. Moreover, the lists are filed at the registered offices and published in national newspapers at least 10 days before the date of the shareholders’ meeting. To ensure that the procedure for the appointment of the Board of Directors is transparent, exhaustive information on the personal and professional background of the candidates is submitted to the registered offices along with the lists, and is immediately published on the company’s website, on the basis of a specific reference included in the notice calling the shareholders’ meeting. The term of the Board of Statutory Auditors currently in office, appointed by the shareholders during the ordinary meeting of 1 April 2005, will lapse with the approval of the financial statements as of and for the year ended 31 December 2007. The standing auditors are listed below, along with a summary of their professional background:

- *Giovanni Ferreri, 72 years old - Chairman of the Board of Statutory Auditors*

  Mr. Ferreri has a degree in Law from Rome’s Università degli Studi “La Sapienza”, and became a lawyer in 1961. Since 1975, he is a barrister with the Court of Cassation, Italy’s highest court.

  He is also a registered auditor and co-owner, with Gianfranco Graziadei, of the international law firm Graziadei - Ferreri, which is based in Rome and has operations in Milan, Munich and New York. He is Deputy Chairman of AS Roma SpA.

- *Giancarlo Russo Corvace, 54 years old - Standing auditor*

  With a degree in Business Administration from Università LUISS, Rome and an MBA from the Università di Torino's Business School, he is a chartered accountant and registered auditor. Up to 1985, he worked for the Financial Affairs Department of Banca Nazionale del Lavoro and until 1988, served as CEO of Ifigest Fiduciaria Sim SpA (now Banca Ifigest).

  He has been a partner of the Graziadei - Ferreri law firm, Rome office, since 1989.

- *Roberto Tasca, 45 years old - Standing auditor*

  Mr. Tasca has a decree in Business Administration from the Università Commerciale "Luigi Bocconi". Since 2001, he has been a Professor of Financial Brokerage Economics with the Economics Department of Bologna's Università degli Studi. He became an independent Director and member of the Appointment and Remuneration committee of Esprinet SpA in April 2006. From 1992 to 2000, he held various teaching positions with the Università di Bologna and the Università Luigi Bocconi of Milan. He has written many Articles and papers on various financial brokerage issues, and teaches Masters courses at SDA Bocconi and Università di Bologna.

During the year, the Board of Statutory Auditors held nine meetings. Each lasted an average of about two hours. The standing auditors attended regularly.

On 7 March 2007 - after the criteria for evaluating the independence of its members, in line with those provided for by the Code of Conduct and adopted by Directors, and on the basis of the information provided by the individuals concerned - the Board of Statutory Auditors announced that all standing auditors met the independence requirements.

During the subsequent meeting of 16 March 2007, the Board of Statutory Auditors voluntarily applied transparency requirements similar to those of the Directors, with respect to transactions in which statutory auditors have an interest directly or on behalf of third parties.

Internal control system

With respect to internal control, on the basis of the preliminary assessment of the Internal control committee, on 21 December 2006, the Board of Directors updated the "Terna Group's internal control system" (ICS), in line with national and international best practices, as the set of rules, procedures and organizational structures which, through an adequate identification, measurement, management and monitoring process of primary risks, enable the company to correctly and consistently manage operations in line with its objectives.

With reasonably certainty, the group's ICS contributes to safeguarding company assets, the efficiency and effectiveness of company transactions, the reliability of financial statements, compliance with the law and regulations, the reliability of company and financial reporting, the safeguarding of electrical service continuity and guaranteed impartiality in concession activities. It is based on the following elements: control environment; risk management system; control activities; information and communications; and monitoring. The coordinated functioning of these elements makes the ICS effective overall.

The control environment, at the basis of all other elements consists of the group's corporate governance model and its ethics, which are set out in the Code of Ethics, which was updated and approved by the Board of Directors during the meeting of 21 December 2006. The group's managerial style, personnel management policies and all employees' conduct must be in line with this code.

The risk management system implemented by top and middle management enables the group to manage its main risks within acceptable limits, using wide-ranging risk management policies defined in specific procedures.

The control activities are carried out by management and employees to achieve specific objectives on the basis of principles, such as self-control, hierarchical control, accountability, contending interests and segregation of duties.

The communications and information processes ensure that the company's expected objectives, culture, values, roles, responsibilities and conduct are clearly disclosed internally, while guaranteeing that disclosures to stakeholders outside the company are correct and transparent.

Monitoring serves to constantly verify the effectiveness of the internal control system through continuous activities carried out by personnel in the performance of their work, and through separate assessments that are regular, but not continuous, and typical, but not exclusive, of the Audit Department.

With the support of the Internal control committee, the Board of Directors establishes the guidelines for the internal control system, so that the main risks are identified, monitored and managed on a compatible basis and in line with sound and correct management principles. The Board also evaluates the adequacy and effective functioning of the internal control system, on the basis of adequate preliminary assessments.

The CEO supervises the group's ICS functions, implementing the guidelines defined by the Board of Directors, designing and managing the system and overseeing the identification of the group's main risks, which he periodically submits to the Board of Directors.

A manager verifies that the internal control system operates effectively and is continuously efficient. Within Terna, this manager is the Internal Audit Manager, appointed by the Board of Directors on the basis of the Chairman's proposal, who supervises auditing activities, in agreement with the CEO, and decides on the manager's remuneration and, if necessary, revocation.

The Audit Manager operates separately and independently of the hierarchy and reports to the Chairman, who is responsible for his work. He reports on findings to the CEO, Internal control committee and the Board of Statutory Auditors. He also carries out auditing activities throughout the group. Internal audit activities can be performed in collaboration with the internal control functions of the subsidiaries.

The Audit function has free access to all IT systems, deeds and company information useful in forming an independent opinion of the internal control system's adequacy in attaining an acceptable risk profile. The Audit function is ensured the availability of the necessary means in performing its duties.

Audit activities may be carried out on the basis of an annual activity plan examined by the Internal control committee and approved by the Chairman, or provided for on a caseby-case basis by top management following specific information or events.

As part of its activities, the Board of Statutory Auditors can request the Audit function to carry out tests on specific operating areas or company transactions.

The Board of Statutory Auditors and the Internal control committee exchange significant information in a timely manner in the performance of their duties.

In accordance with the opinion expressed by the Internal control committee, based on the analyses conducted in 2006, Terna's Board of Directors believes that the group's internal control system is adequate in attaining an acceptable risk profile, given the sector in which it operates, its size, the organizational structure and its corporate structure.

In its report, the Internal control committee also discussed, also in relation to the report of the supervisory board appointed pursuant to Legislative Decree no. 231/01 on the implementation of the organizational model within Terna and other group companies.

Related party transactions

Even before it listed its shares on the stock exchange, Terna and its subsidiaries decided to lay the foundation for ensuring that related party transactions were carried out in compliance with the principles of procedural and substantial correctness, in its own interest and as a duty to the market.

These conditions were defined in a specific procedure that was submitted to the Internal control committee in advance and approved by the Board of Directors on 22 February 2007, in accordance with the provisions of the new Code of Conduct. To this end:

- related parties were identified in line with IFRS;
- the methods by which related party transactions are identified, approved and performed by Terna, directly or through its subsidiaries, were specified;
- the methods used to identify and manage situations in which a Director has an in interest, directly or on behalf of third parties, were specified.

In terms of the procedural correctness of related party transactions, the conditions provide that:

- in advance, each company function evaluates the type of transaction to be carried out and the nature of the relationship of the parties, and informs Terna's Corporate and Legal Affairs Department in due time, so that it can meet its requirements with the Board of Directors;
- significant transactions with related parties are subject to the approval of Terna's Board of Directors, with the consultancy of the Internal control committee;
- in addition, related party transactions amounting to more than euros 2,000,000 each are submitted to Terna's Board of Directors, with the exception of transactions approved in the budget or in dispatching or related service contracts. Moreover, the Board of Directors should be appropriately informed on the nature of the relationship, the operating methods, the timing and economic terms and conditions of the transaction, the measurement procedure applied, underlying interests and reasons and any risks that could arise for Terna and its subsidiaries in connection with the transaction;
- the Board of Directors and Board of Statutory Auditors should receive specific periodic reporting on transactions other than the above, with the exception of related party transactions totalling less than euros 50,000 which are excluded from the Board of Directors authorization and reporting requirement;
- Directors who have an interest (including potential or indirect interests) in the transaction:
  - are required to inform the Board of Directors and Board of Statutory Auditors in due time of the existence of the interest, specifying its nature, terms, origin and scope;
  - are required to leave the Board meeting or abstain from voting at that time, unless the Board specifically authorizes participation in the related discussions and/or vote;

- Directors are required to inform the Board of their positions at the time of their appointment and regularly update the Board on them.

In addition, Board resolutions passed in relation to intercompany transactions should be adequately justified and advantageous for the relevant company.

In terms of substantial correctness - for the purposes of ensuring the fairness of related party transaction conditions and where required by the nature, value or other characteristics of the individual transaction - the Board of Directors may draw on the assistance of independent experts in evaluating the economic conditions and/or executive and technical methods of the transaction. The choice of expert should be based on reputable professionalism and expertise (banks, audit companies, law firms and other experts with specific technical skills) whose independence is recognized and in which there are no conflicts of interest with respect to the transaction.

Treatment of confidential information

In accordance with measures on the treatment of privileged information aimed at preventing insider trading and the provisions of Article 4 of the new Code of Conduct and paragraph 1, Article 114 and Article 181 of Legislative Decree no. 58/98, during the meeting of 21 December 2006, the company's Board of Directors approved a specific regulation for the management and treatment of confidential information, which also contained the procedures for disclosing documents and information on the company and its subsidiaries outside the company, with specific reference to the confidential information provided for by paragraph 1, Article 114 of Legislative Decree no. 58/98 (Consolidated Finance Act).

This regulation constitutes an update to the measures in this respect contained in the regulation that Terna approved in April 2004, with specific reference to price sensitive information. It aims to maintain the secrecy of confidential and privileged information while at the same time ensuring the disclosure of correct, complete, adequate, timely and objective company information to the market. The regulation also sets the guidelines for the subsidiaries, so that they will provide Terna with all the necessary information for it to meet the disclosure requirements of the law. The Directors and statutory auditors of Terna and its subsidiaries are required to comply with the provisions of this regulation and, in any case, keep all documents and information acquired in the performance of their duties, as well as the content of any discussions during Board meetings, confidential.

The regulation generally entrusts the company's CEO and the delegated functions of the subsidiaries with management of confidential information for which they are responsible, providing that such information on individual subsidiaries should be disclosed with the prior authorization of the company's CEO.

Moreover, the regulation establishes specific procedures to be followed when disclosing company documents and information outside the company, with particular focus on the disclosure of privileged information. It also scrupulously governs the way in which members of the company should deal with the press and other means of mass communication (i.e., financial analysts and institutional investors).

Lastly, the new regulation has introduced specific "measures for persons who commit infractions" of the regulation's provisions.

In accordance with the provisions of Article 115 *bis* of Legislative Decree 58/98 (Consolidated Finance Act) and the regulatory measures issued by Consob, Terna's Board of Directors created a specific list of people with access to privileged information within Terna. It also prepared a specific regulation to govern how the list is held and updated. The same regulation requires that the subsidiaries also create their owns lists.

In April 2004, the company's Board of Directors also approved the internal dealing code of conduct, in compliance with the regulatory measures laid down by Borsa Italiana SpA, establishing the market transparency requirement for listed companies with respect to significant transactions, transactions involving the financial instruments of the company or its subsidiaries, those carried out by people with significant decision-making powers in the company and with access to price sensitive information ("relevant persons"). In accordance with the legislative measures that governed the reporting obligation to Borsa Italiana and Consob on transactions involving the financial instruments of the company carried out by "relevant persons" within the same company or closely related people (paragraph 7, Article 114 of Legislative Decree no. 58/98 and Article 152-*sexies*, *septies* and *octies* of Consob's Issuer Regulation, during the meeting of 15 March 2006, the Board of Directors, adopted a specific internal procedure with effect from 1 April 2006, replacing the previous Internal dealing code of conduct, in which "relevant persons" were identified as Terna's Directors and standing auditors, managers of Terna's functions (reporting directly to the CEO or Chairman), as they have regular access to privileged information and may take management decisions that could affect the outlook and future development of Terna.

This procedure includes the following qualifying elements, which are considered adequate in heightening the qualitative content:

- application of internal dealing transparency obligations to 23 "relevant persons" within the company and its subsidiaries (in addition to the Directors and standing auditors of Terna). To ensure adequate flexibility in the scope of "relevant persons", the procedure also provides for the possibility of extending the transparency obligations to other people, with the separate approval of the Chairman and CEO of the company;
- "relevant persons" are not permitted to carry out transactions (other than the exercise of options) 30 days before the approval of the draft financial statements and half year report by Terna's Board of Directors. Moreover, the Board can establish additional blocking periods during the year, following specific events;
- an adequate penalty system was created for "relevant persons" identified as in violation of the measures of this procedure.

Relationships with institutional investors and shareholders

Since its listing on the stock exchange, the company has believed that forging constant dialogue with shareholders and institutional investors is both in its best interest and a duty to the market. This dialogue is based on the mutual understanding of roles and is in compliance with the procedures for the disclosure of documents and information outside the company and the principles contained in the "Guide for market disclosures" and recent regulatory measures and regulations on market disclosure.

To this regard, and also considering the company's size, it decided that this dialogue should be facilitated by the creation of specific company structures.

Accordingly, the company has set up the (I) Investors Relations Department, which currently reports to the CEO and (II) a department for relationships with general shareholders under the Corporate and Legal Affairs Department.

Furthermore, the company has further encouraged dialogue with investors by creating a specific section for its website (www.terna.it), where they can find financial information (financial statements, half year and quarterly reports and presentations to the financial community) and updated information and documents of interest to shareholders (press releases, the company officers, the by-laws and the regulation for shareholders' meetings, corporate governance information and documents, the Code of Ethics and the organizational and management model pursuant to Legislative Decree no. 231/2001).

Shareholders’ meetings

The Code of Conduct establishes that the shareholders’ meetings should be used as special occasions to initiate fruitful dialogue between shareholders and the Board of Directors (despite the wide-ranging diversification of the communications methods used by listed companies with their shareholders, institutional investors and the market). This was carefully evaluated and fully approved by the company, which believed it necessary to adopt specific measures to enhance the meetings adequately, in addition to guaranteeing the participation of its Directors.

Also in the wake of special legislation enacted as expected in relation to listed companies, Terna introduced into its by-laws a specific regulation aimed at facilitating the gathering of voting proxies for shareholders who are employees of the company and its subsidiaries, so as to involve them in the decision-making process at the shareholders’ meetings.

Furthermore, during the meeting of 3 March 2004, the shareholders resolved to implement a specific regulation for the company, aimed at ensuring the ordered and functional running of shareholders’ meetings, with detailed rules for the various sectors, in accordance with each shareholders’ fundamental right to request clarifications on the various issues being discussed, express an opinion and make proposals.

Although this regulation is not included in the by-laws, it was approved during the ordinary meeting under the specific power given to the shareholders by the by-laws. The contents of the regulation have been aligned to the most sophisticated models prepared by trade associations (Assonime and ABI) for listed companies.

In addition, in view of the shareholders’ meetings, the Board of Directors provides the shareholders with adequate information in a timely manner, so they may pass resolutions with full knowledge of the facts.

Code of Ethics

In May 2002, Terna's Board of Directors resolved to adopt the Code of Ethics (updated in March 2004), as it was aware of the social and environmental impact of the company's activities, and given the importance of cooperating with stakeholders and maintaining its good reputation (both internally and externally).

During the year, the company updated the Code of Ethics to equip Terna with a set of rules and policies to follow, in its changed context resulting from its transformation to an independent operator on the energy transmission market.

The new Code of Ethics, which was approved by the Board of Directors on 21 December 2006, attempts to explain in ethical terms, Terna's uniqueness, by both detailing its peculiarities and sharing the values and universal policies that all companies should have at the heart of their operations, to encourage trust in their stakeholders. It is a series of rules of conduct for an organization and a governance tool for relationships. It is broken down into five sections, which discuss, in this order:

- Terna's fundamental ethical policies, which are organized into general ethics (legality, honesty and accountability), which are base broad and transversal values for all conduct at all times within the company, and four main policies that Terna believes are particularly important, given its activities and nature (good management, respect, fairness and transparency);
- the conduct required, especially of employees, based on three transversal elements: loyalty to the company, conflicts of interest and the integrity of company assets;
- general instructions for the conduct to follow in relationships with stakeholders, broken down into eight groups in which Terna requires consistent conduct;
- Terna's commitment to compliance with the Code and the conduct required with respect to certain stakeholders;
- the rules implementing the Code and the relevant people responsible for updating it and gathering reports, who should be contacted for any clarifications.

The Code of Ethics was approved in December 2006. All of sections 1 (policies) and 2 (conflicts of interest, company loyalty and the integrity of company assets) and the initial guidelines for the conduct to the followed with the individual categories of stakeholders of section 3 (relationship with stakeholders) apply to all Terna Group subsidiaries.

To complete the Code of Ethics and the commitments that it makes therein, Terna decided to prepare a sustainability report to illustrate its work in the field of ethics and social responsibility. The first edition was published in November 2006, in relation to the activities carried out in 2005 and the first half of 2006.

The report illustrates how Terna's sense of accountability for the social and environmental impact of its activities affects its management, and translates into programmes, projects and initiatives to create and maintain trust in others. Terna's relationships with stakeholders, and generally with the context in which its operates, are discussed from three standpoints: financial, environmental and social. A specific section is dedicated to the electricity service, its core business, but also a field in which Terna feels especially accountable to the public.

Managerial and administrative model

In December 2002, Terna's Board of Directors resolved to adopt a managerial and administrative model that met the requirements of Legislative Decree no. 231 of 8 June 2001, which introduced into Italian law a system of administrative (and criminal) liability for companies with respect to certain types of crimes committed by their Directors, managers or employees in the company's interest or to its benefit. The model was updated in June 2004, after the company's shares were listed.

On 21 December 2006, Terna's Board of Directors resolved to update and integrate the "Managerial and administrative model pursuant to Legislative Decree no. 231 of 8 June 2001" at 1 January 2007 to reflect new legislation enacted and the integration of the National Transmission Grid management activities, as well as the experience and legal guidelines. This project went hand-in-hand with the Code of Ethics, as the company believed that the adoption of this model - regardless of the regulations that made it optional rather than mandatory - was a valid tool in increasing the awareness of everyone who operates in the name and on behalf of Terna and its group, so that they would conduct themselves correctly and transparently in the performance of their activities, so as to prevent the risk of the crimes provided for by the Decree from being committed.

The model is currently organised into six sections:

- a general section which describes, *inter alia*, the content of Legislative Decree no. 231/2001, the objectives of the model and how it functions, the duties of the supervisory board required to monitor the functioning and compliance of the model, information flows and the penalty system;
- special section "A", which covers crimes committed in dealings with the public administration;
- special section "B", which discusses corporate crimes;
- special section "C", which deals with crimes of terrorism or subversion of the democratic order;
- special section "D", on crimes against individuals;
- special section "E", concerning market abuse offences.

The content of this model is consistent with the guidelines prepared for this purpose by trade associations. It is also in line with best practices, and constitutes the final step towards complete accuracy, transparency and accountability in internal and external relations, while offering shareholders a guarantee of efficient and correct management.

Additional updates and integrations to the model are currently underway in relation to subsequent legislation, which extended the scope of crimes provided for by Legislative Decree no. 231/2001 or amended other relevant legislation.

The following three tables summarise the most significant information of section two of this document.

TERNA'S BOARD OF DIRECTORS AND COMMITTEES

BOARD OF DIRECTORS						
Term of office	Members	Executive	Non-executive	Independent	(8)	Number of other positions (9)
Chairman	Luigi Roth		●		100%	2
CEO	Flavio Cattaneo	●			100%	-
Director	Luigi De Paoli		●	●	85.7%	1
Director	Mario Garraffo		●	●	92.8%	5
Director	Claudio Machetti [1] [2]		●			1
Director	Salvatore Machì [2]		●	●	100%	1
Director	Carmine Macrì		●	●	85.7%	-
Director	Piero Giuseppe Maranesi		●	●	100%	-
Director	Vittorio Rispoli [2] [5]		●	●	85.7% [5]	3
Director	Franco Smurro		●	●	57.1%	-
Director	Massimo Ponzellini [2] [6]		●	●	85.7%	-
Director	Massimo Romano [2] [7]		●		64.2%	2

Quorum required to present lists for the appointment of the Board of Directors:
1% of the share capital

Number of meetings held during 2006:
Board of Directors: 14 Internal control committee: 7
Remuneration committee: 3 Appointment committee: N.A. Executive committee: N.A.

INTERNAL CONTROL COMMITTEE		REMUNERATION COMMITTEE		POTENTIAL APPOINTMENT COMMITTEE		POTENTIAL EXECUTIVE COMMITTEE	
(10)	(8)	(10)	(8)	(10)	(8)	(10)	(8)
		●	100%	Inexistent		Inexistent	
●	85.7%						
●	85.7%	●	100%				
●	85.7%						
●[3]	100%	● [4]					
●	85.7%						
		● [5]	100% [5]				
		●	60%				
		● [6]	100% [6]				
		●	33%				

[1] This Director was co-opted to replace a Director appointed from the minority list. In office since 21 March 2007.
[2] Director appointed from a minority list.
[3] Member of the Internal control committee until 21 March 2007.
[4] Member of the remuneration committee since 21 March 2007.
[5] This Director was co-opted to replace a Director appointed from the minority list. In office since 13 July 2006.
[6] In office up to 3 July 2006.
[7] In office up to 16 March 2007.
[8] These columns indicate each Director's percentage of participation in the Board and committee meetings. All absences were suitably justified.
[9] This column indicates the number of positions as Director or statutory auditor held by the person in other companies listed on regulated markets, including those abroad, in addition to financial, banking, insurance or significantly large companies. Other positions do not include any held in Terna's indirect or direct subsidiaries or other companies in which it holds an investment. Where more than one position is held within the same group, including where the person concerned is an employee, only the most important position is considered.
[10] These columns are marked with an "●" to indicate whether the Director is a member of the committee.

TERNA'S BOARD OF STATUTORY AUDITORS

Term of office	Members	Percentage of participation in meetings [2]	Number of other positions [3]
Chairman	Giovanni Ferreri	100%	1
Standing auditor	Giancarlo Russo Corvace	100%	-
Standing auditor	Roberto Tasca [1]	100%	1
Alternate auditor	Bruno Franceschetti	N.A.	-
Alternate auditor	Vito Di Battista [1]	N.A.	-

Quorum required to present lists for the appointment of the Board of Statutory Auditors: **1%** of the share capital
Number of meetings held during 2006: **9**

(1) Statutory auditor appointed from a minority list.
(2) All absences were suitably justified.
(3) This column indicates the number of positions as Director or statutory auditor held by the person in other companies listed on regulated markets, including those abroad, in addition to financial, banking, insurance or significantly large companies.

OTHER PROVISIONS OF THE CODE OF CONDUCT

	YES	NO
SYSTEM OF POWERS AND RELATED PARTY TRANSACTIONS		
Has the Board of Directors delegated powers with the definition of the following:		
(a) limitations	•	
(b) methods of exercise	•	
(c) frequency of reporting?	•	
Does the Board of Directors reserve the right to examine and approve transactions with a significant impact on the income statement, balance sheet and financial position (including related party transactions)?	•	
Has the Board of Directors established guidelines and parameters for the identification of significant transactions?	•	
Have these guidelines and parameters been described in the report?	•	
Has the Board of Directors established specific procedures for examining and approving related party transactions?	•	
Are the procedures for the approval of related party transactions described in the report?	•	
PROCEDURES FOR THE MOST RECENT APPOINTMENT OF DIRECTORS AND STATUTORY AUDITORS		
Are candidatures for the office of Director submitted at least ten days in advance?	•	
Are candidatures for the office of Director submitted along with thorough background information?	•	
Do candidatures for the office of Director include indication of whether the candidate is eligible for qualification as independent?	•	
Are candidatures for the office of statutory auditor submitted at least ten days in advance?	•	
Are candidatures for the office of statutory auditor submitted along with thorough background information?	•	
SHAREHOLDERS' MEETINGS		
Has the company approved rules for the shareholders' meetings?	•	
Are the rules attached to the report (or is indication given of where they can be obtained/downloaded)?	•	
INTERNAL CONTROL		
Has the company appointed an internal control manager?	•	
Is the internal control manager hierarchically independent of the managers of the operating areas?	•	
Organizational role of the internal control manager	(1)	
INVESTOR RELATIONS		
Has the company appointed an Investors relations manager?	•	
Organizational unit and person responsible for Investor relations	(2)	

(1) Internal audit manager
(2) The Investor Relations department is responsible for handling institutional investor relations.
Investor Relations - Via Arno 64 00198 Rome - Tel. 06.8313 8145 - Fax 06.8313 8389
E-mail: www.investor.relations@terna.it
Legal Affairs and the Corporate Office are responsible for handling retail investor relations
Corporate Office - Via Arno 64 00198 Rome - Tel. 06.83138136 - 06 8313 8376 - Fax 06.8313 8317
E-mail: www.azionisti.retail@terna.it

SUBSEQUENT EVENTS

2007-2011 strategic plan

On 31 January 2007, Terna presented financial analysts with its 2007-2011 business plan, approved by the company's Board of Directors.

The Terna Group's 2007-2011 business plan focuses on three main guidelines:

- Development of the National Transmission Grid (RTN): the investment plan provides for total expenditure of euros 2.7 billion from 2007 to 2011, with a 35% increase on the previous plan. Development investments account for 80% of total investments, up from euros 1.4 billion to euros 2.2 billion.
- Cost cutting with an increase in profits margins: in particular, by rationalizing costs for regulated activities in Italy. The plan provides for a reduction of approximately euros 60 million in total Terna Group costs in the years covered on a like-for-like basis.
- Guaranteed high security of the electrical system and reliability of the domestic transmission grid with average service interruption times of less than 1 minute/year and network availability of over 99%.

Credit rating confirmation

On 31 January 2007, Standard & Poor's Ratings Services confirmed its ratings for Terna SpA, following the Italian utility company's presentation of its 2007-2011 business plan: long-term rating of AA- and short-term rating of A-1+ with a stable outlook.

New dispatching and conduction organization

The new organizational structure for the Dispatching and Conduction Department was implemented on 1 March 2007, to complement the work performed on processes following the acquisition of the GSE SpA (formerly GRTN) business activity. This new structure enables process-based management, while ensuring that operating and strategic objectives are aligned, preventing the scattering of similar activities within the same process to more than one unit. In addition, a portion of the resources formerly under the Systems and Technology Department (which is now the Technology and Management Systems Department), has come under the Technologies and Process Systems Function reporting to the Dispatching and Conduction Department.

Similarly, work groups have begun identifying further measures to take to optimize in detail the processes related to real time management.

Fibre optics

On 4 April 2007, an agreement was signed with the Wind Telecomunicazioni Group to acquire the exclusive right to use optical fibre pairs owned by the Wind Group for 20 years. The pairs run for a total length of approximately 11,000 km throughout all of Italy.

The agreement amounts to euros 43.5 million.

The data transmission infrastructure is a crucial element of the security and efficiency of control, conduction and protection processes for the high voltage grid, as it makes it possible to improve grid supervision and carry out work on Terna plants, while allowing the development of advanced solutions to protect the electricity system.

This transaction will enable Terna to further boost the security of the system and is included in the investments provided for by the 2007-2011 business plan.

Merger of RTM1 and RTM2 into RTL

On 18 April 2007, the shareholders of Rete di Trasmissione Locale Società per Azioni (RTL), "Rete Trasmissione Milano 1 Società per Azioni" (RTM1) and "Rete Trasmissione Milano 2 Società per Azioni" (RTM2) met and approved the plan for the merger of RTM1 and RTM2 into RTL, on the basis of the companies' financial statements as of and for the year ended 31 December 2006, with the cancellation of all shares of RTM1 and RTM2, in accordance with the methods set out in the plan and, accordingly, without RTL increasing its share capital or provided for a share exchange ratio or cash consideration.

The merger will take effect from the date of registration of the merger deed with the company registrar, or a subsequent date indicated in the merger deed.

Pursuant to point 6), Article 2501-*ter* of the Italian Civil Code, referred to by Article 2504 *bis* of the Italian Civil Code and paragraph 9, Article 172 of Presidential Decree no. 917 of 22 December 1986, the transactions carried out by companies to be merged will be recognized in the financial statements of the merging company and the merger will take effect for accounting and tax purposes from midnight on the first day of the year in which the merger takes effect.

In particular, the purpose of the transaction is to improve the Terna Group companies' operations, by expanding synergies through a Group reorganization in order to streamline the investment chain and pursue increased management efficiency, while reducing administrative costs. To this end, all companies in the same sector will be merged together.

Acquisition of AEM Trasporto Energia Srl Torino

On 20 April 2007, through RTL, the Terna Group signed an agreement with Iride Energia to acquire 100% of AEM Trasporto Energia Srl (“AEM TE”) and the 220-kV electrical substation in Moncalieri (Turin), which is part of the National Transmission Grid (“RTN”).

The consideration totalled euros 49.4 million, including euros 38.8 million to acquire the 100% investment in AEM TE, euros 2.8 million for the company’s net financial position at 31 December 2006 and euros 10.6 million to acquire the Moncalieri (Turin) substation. The acquisition agreement provides for an adjustment to the consideration in relation to the change in AEM TE’s equity between 31 December 2006 and the date the transaction is concluded.

AEM TE owns approximately 220 km of triads and four electrical substations in Piedmont, which are part of the National Transmission Grid (Martinetto, Rosone, Sud Ovest and Villa).

At 31 December 2006, AEM TE reported revenues of euros 7.6 million, EBITDA of euros 4.3 million and a profits for the year of euros 1.7 million. Net invested capital amounted to approximately euros 25.7 million, including property, plant and equipment totalling roughly euros 27.1 million. Equity amounted to around euros 28.6 million. The transaction is subject to authorization from the Anti-Trust Authority before it can be concluded.

Control of Terna SpA held by Cassa Depositi e Prestiti

On 19 April 2007, Cassa Depositi e Prestiti SpA, which owns 29.99% of Terna SpA, notified the company that it had verified that it controlled Terna SpA. This assessment was based on the following elements:

- the composition and breakdown of the shareholding structure;
- events at particularly significant shareholders’ meetings;
- the composition of the Board of Directors.

OUTLOOK

The Group will continue to pursue compliance with the provisions of the Prime Minister's Decree of 11 May 2004 in 2007, with specific focus on the unification of the National Transmission Grid through the acquisition of additional portions of the grid owned by others.

Furthermore, to optimize company operations, the group will merge RTM1 and RTM2 into RTL.

The parent will continue to seek investment opportunities abroad, with particular focus on profitability and low risk profiles.

In terms of regulations applicable to Terna, in 2007, the Electricity and Gas Regulator is expected to adopt certain measures that could have a direct impact on the parent.

Firstly, as anticipated in Resolution no. 208/06 launching the procedure for the creation of tariff measures, in 2007, the Regulator will establish new tariff regulations with effect for the third regulatory period from 2008 to 2011.

Secondly, as the Regulator announced in the 32/06 consultation document issued in late 2006, 2007 could see the start-up of experimental incentives for Terna in the procurement of dispatching resources and their use.

Human Resources

The company also plans to integrate all of the subsidiaries RTM1's and RTM2's personnel into the local organizational structures of Terna SpA in the first half of 2007.

With respect to the development of human resources, the main areas on which the company will focus in 2007 are directly related to its strategic guidelines for sustainable internal growth, i.e., managerial and technical excellence with specific attention to environmental issues, as well as growth by seeking opportunities abroad.

The company will also focus particularly on innovating its techniques, with a close link between evaluation processes and those relating to the preparation of personalized development/training plans for individuals and/or groups.

OTHER INFORMATION

Approval of the financial statements

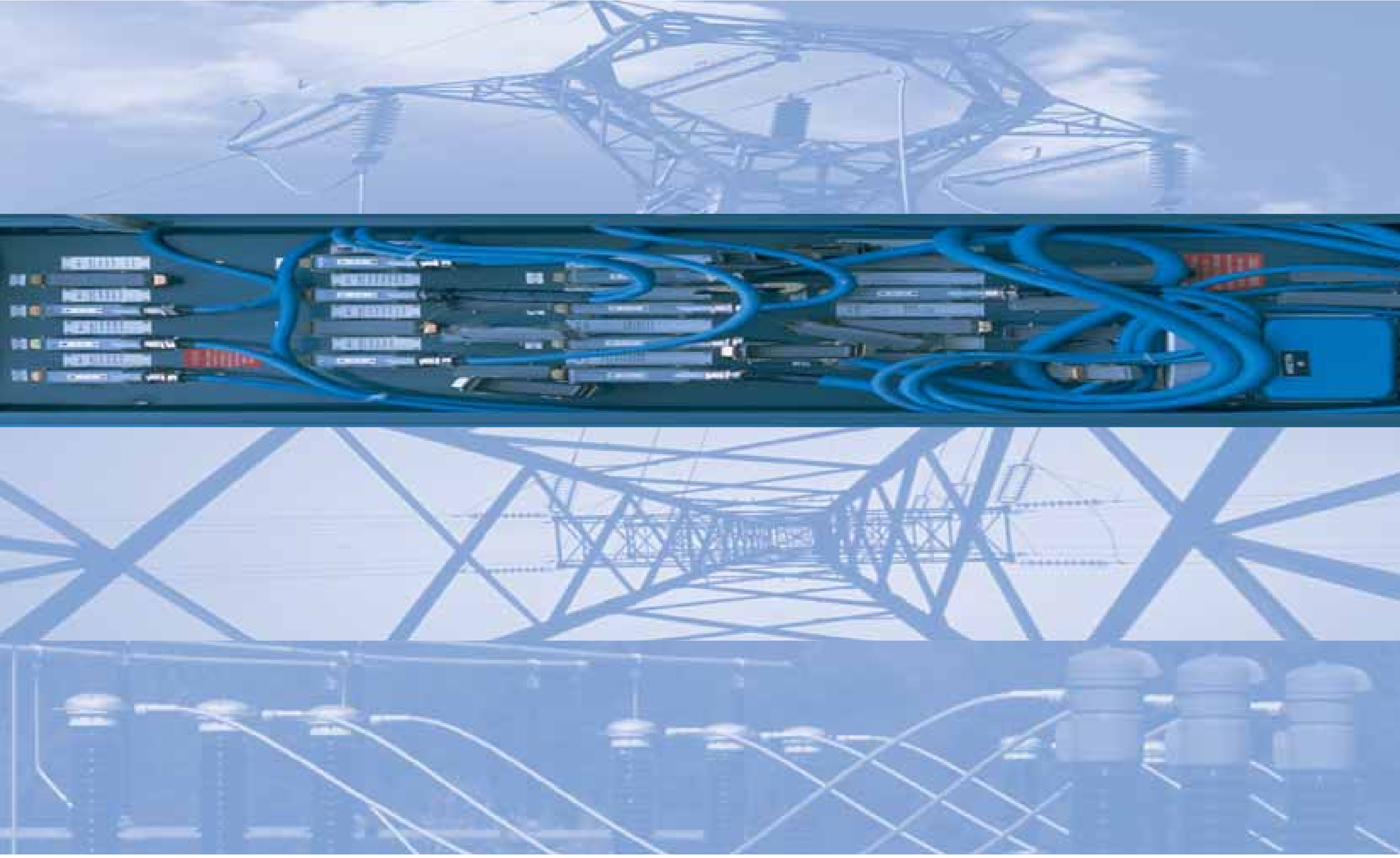
In accordance with Article 9.2 of the company's by-laws, the ordinary shareholders' meeting is called within six months of the year end to approve the financial statements. This term is applied in lieu of the ordinary 120-term, as permitted by paragraph 2, Article 2364 of the Italian Civil Code, given that the company is also required to prepare consolidated financial statements.

Personal data protection code (Legislative Decree no. 196 of 30 June 2003)

Terna SpA prepared the personal data protection document in 2003 and updated it in 2006, in accordance with Presidential Decree no. 318/1999.
It will next be updated at 31 March 2007, within the term provided for by Legislative Decree no. 196 of 30 June 2003.

Treasury shares

The company does not hold any treasury shares, nor has it acquired or sold any during the year, either directly or indirectly.



FINANCIAL STATEMENTS

INCOME STATEMENT

In millions of euros	Note	at 31.12.2006	at 31.12.2005	Change
A) REVENUES				
Revenues from sales and services	1	1,083,495,744	887,800,824	195,694,920
of which from related parties		2,010,860	359,880	1,650,980
Other revenues	2	26,716,824	22,477,792	4,239,032
of which from related parties		185,944	190,417	-4,473
Total revenues		**1,110,212,568**	**910,278,616**	**199,933,952**
B) OPERATING EXPENSES				
Raw materials and consumables	3	18,138,373	23,883,920	-5,745,547
Services	4	123,699,941	106,665,630	17,034,311
of which to related parties		865,350.0	1,695,315.0	-829,965.0
Personnel expenses	5	236,964,485	198,630,562	38,333,923
of which to related parties		1,653,877	1,321,418	332,459
Amortization, depreciation and impairment losses	6	202,185,248	157,102,804	45,082,444
Other operating expenses	7	15,035,562	19,912,335	-4,876,773
Capitalized internal work	8	-36,578,279	-26,460,510	-10,117,769
Total expenses		**559,445,330**	**479,734,741**	**79,710,589**
A+B OPERATING PROFITS		**550,767,238**	**430,543,875**	**120,223,363**
C) FINANCIAL INCOME/EXPENSES				
Financial income	9	92,296,109	52,521,450	39,774,659
of which from related parties		40,138,958.0	39,255,622.0	883,336.0
of which non-recurring		38,372,363.0	0.0	38,372,363.0
Financial expenses	9	-76,221,756	-63,262,125	-12,959,631
of which to related parties		-243,128	-22,131	-220,997
D) PROFITS BEFORE TAXES		**566,841,591**	**419,803,200**	**147,038,391**
E) INCOME TAXES	**10**	**211,084,064**	**154,187,587**	**56,896,477**
F) PROFITS FOR THE YEAR		**355,757,527**	**265,615,613**	**90,141,914**
Basic earnings per share	11	0.178	0.133	0.045
Diluted earnings per share	11	0.177	0.132	0.045

BALANCE SHEET ASSETS

In millions of euros	Note	at 31.12.2006	at 31.12.2005	Change
A) NON-CURRENT ASSETS				
Property, plant and equipment	12	4,148,983,318	4,020,358,009	128,625,309
Intangible assets	13	159,220,967	151,489,122	7,731,845
Deferred tax assets	14	54,593,067	51,751,945	2,841,122
Non-current financial assets	15	676,644,564	399,147,843	277,496,721
Other non-current assets	16	5,335,162	5,916,612	-581,450
Total non-current assets		**5,044,777,078**	**4,628,663,531**	**416,113,547**
B) CURRENT ASSETS				
Inventories	17	7,740,090	7,175,172	564,918
Trade receivables	18	1,163,743,876	985,668,657	178,075,219
of which from related parties		1,778,030	509,880	1,268,150
Current financial assets	15	2,624,109	4,420,462	-1,796,353
of which from related parties		452,739	0	452,739
Cash and cash equivalents	19	36,094,437	15,791,228	20,303,209
of which from related parties		20,760,682	0	20,760,682
Other current assets	16	17,300,730	50,410,630	-33,109,900
of which from related parties		0	27,209,963	-27,209,963
Total current assets		**1,227,503,242**	**1,063,466,149**	**164,037,093**
TOTAL ASSETS		**6,272,280,320**	**5,692,129,680**	**580,150,640**

BALANCE SHEET LIABILITIES

In millions of euros	Note	at 31.12.2006	at 31.12.2005	Change
C) EQUITY				
Share capital		440,000,000	440,000,000	0
Other reserves		813,472,188	804,906,014	8,566,174
Retained earnings		398,436,016	387,362,409	11,073,607
Interim dividend		-106,000,000	-100,000,000	-6,000,000
Profits for the year		355,757,527	265,615,613	90,141,914
Total equity	**20**	**1,901,665,731**	**1,797,884,036**	**103,781,695**
D) NON-CURRENT LIABILITIES				
Long-term loans	21	1,947,525,103	1,868,912,841	78,612,262
Termination benefits and other employee-related provisions	22	161,837,391	168,144,528	-6,307,137
Provisions for contingencies and charges	23	54,255,480	35,675,117	18,580,363
Deferred tax liabilities	24	453,450,800	464,094,893	-10,644,093
Non-current financial liabilities	21	6,195,323	29,047,521	-22,852,198
Other non-current liabilities	25	170,789,453	176,191,033	-5,401,580
Total non-current liabilities		**2,794,053,550**	**2,742,065,933**	**51,987,617**
E) CURRENT LIABILITIES				
Short-term loans	21	70,993,113	59,849,295	11,143,818
of which from related parties		20,993,114	4,849,295	16,143,819
Current portion of long-term loans	21	29,545,200	29,540,000	5,200
Trade payables	26	1,282,947,226	936,156,512	346,790,714
of which to related parties		16,352,852	3,514,536	12,838,316
Tax liabilities	26	72,245,270	14,387,553	57,857,717
Current financial liabilities	21	14,054,106	14,463,931	-409,825
Other current liabilities	26	106,776,124	97,782,420	8,993,704
of which to related parties		1,076,703	773,595	303,108
Total current liabilities		**1,576,561,039**	**1,152,179,711**	**424,381,328**
TOTAL LIABILITIES AND EQUITY		**6,272,280,320**	**5,692,129,680**	**580,150,640**

STATEMENT OF CHANGES IN EQUITY

In millions of euros	Share capital	Legal reserve	Retained earnings	Other reserves	Interim dividend	Profits for the year	Equity
	TERNA SPA SHARE CAPITAL AND RESERVES						
AT 1 JAN. 2005	**440.0**	**84.5**	**608.2**	**728.7**	**-90.0**	**0.0**	**1,771.4**
ALLOCATION OF PROFITS FOR 2004						-	
reserves		3.5	-3.5				-
2004 interim dividend			-90.0		90.0		-
2004 final dividend			-140.0				-140,0
Other changes			12.7	-11.8			0,9
Profits for the year						265.6	265,6
2005 interim dividend					-100.0		-100,0
AT 31 DEC. 2005	**440.0**	**88.0**	**387.4**	**716.9**	**-100.0**	**265.6**	**1,797.9**

In millions of euros	Share capital	Legal reserve	Retained earnings	Other reserves	Interim dividend	Profits for the year	Equity
	TERNA SPA SHARE CAPITAL AND RESERVES						
AT 31 DEC. 2005	**440.0**	**88.0**	**387.4**	**716.9**	**-100.0**	**265.6**	**1,797.9**
ALLOCATION OF PROFITS FOR 2005							-
Retained earnings			5.6			-5.6	-
2005 interim dividend					100.0	-100,0	-
2005 final dividend						-160.0	-160.0
Other changes			5.4	8.6			14.0
Profits for the year						355.8	355.8
2006 interim dividend					-106.0		-106.0
AT 31 DEC. 2006	**440.0**	**88.0**	**398.4**	**725.5**	**-106.0**	**355.8**	**1,901.7**

STATEMENT OF RECOGNIZED INCOME AND EXPENSES

In millions of euros	2006	2005
Effective portion of changes in the fair value of cash flow hedges	7.8	0.7
Exercise of stock options	0.8	0.2
Actuarial gains on defined benefit plans	5.4	-
Income and expenses recognized directly in equity	**14.0**	**0.9**
Profits for the year	355.8	265.6
Income and expenses recognized in the financial statements	369.8	266.5

CASH FLOW STATEMENT*

In millions of euros	31.12.2006	31.12.2005	Change
Profits for the year	**355.8**	**265.6**	**90.1**
ADJUSTMENTS FOR			
Amortization, depreciation, impairment losses/(reversals of impairment losses) on property, plant and equipment and intangible assets, net of grants related to plant taken to profits or losses for the year	178.0	146.9	31.1
Accruals to provisions (including employee-related provisions) and impairment losses	47.4	38.7	8.7
Gains/losses on disposals of property, plant and equipment	1.1	2.5	-1.4
Financial (income)/expenses	-16.1	50.0	-66.1
Income taxes	211.1	159.8	51.3
Cash flows generated by/(used in) operating activities, before changes in net working capital	**777.3**	**663.5**	**113.8**
Decrease in provisions (including employee-related and tax provisions)	-31.3	-33.9	2.6
(Increase)/decrease in inventories	-0.6	2.9	-3.5
(Increase)/decrease in trade receivables and other current assets	-112.7	-840.2	727.5
Increase/(decrease) in other non-current liabilities	-4.5	26.9	-31.4
(Increase)/decrease in other non-current assets	-102.4	-149.3	46.9
Increase/(decrease) in trade payables and other liabilities	454.8	682.2	-227.4
Interest income and other financial income received	106.7	98.9	7.8
Interest expenses and other financial expenses paid	-104.5	-51.8	-52.7
Income taxes paid	-226.6	-173.8	-52.8
Acquisition of TSO business activity	0.0	154.1	-154.1
Cash flows generated by/(used in) operating activities [a]	**756.2**	**379.5**	**376.7**
Investments in property, plant and equipment, net of recognized grants	-304.9	-248.0	-56.9
Revenues from sale of property, plant and equipment	4.0	1.8	2.2
Investments in intangible assets	-26.5	-1.6	-24.9
(Increase)/decrease in investments	-415.9	0.0	-415.9
Revenues from sale of non-current financial assets	82.7	0.0	82.7
Acquisition of TSO business activity	0.0	-225.5	225.5
Cash flows generated by/(used in) investing activities [b]	**-660.6**	**-473.3**	**-187.3**
Changes in reserves	6.2	0.2	6.0
Dividends paid	-266.0	-240.0	-26.0
Changes in medium/long-term financial payables (including short-term portions), net of fair value hedges	173.4	145.5	27.9
Changes in short-term financial payables and term credit lines	-5.0	55.0	-60.0
Cash flows generated by/(used in) financing activities [c]	**-91.4**	**-39.3**	**-52.1**
INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS [A+B+C+D]	**4.2**	**-133.1**	**137.3**
Opening cash and cash equivalents	**10.9**	**144.0**	**-133.0**
Closing cash and cash equivalents	**15.1**	**10.9**	**4.3**

* Reference should be made to the specific paragraph in the notes "NOTES TO THE CASH FLOW STATEMENT" for comments.

NOTES TO THE FINANCIAL STATEMENTS

A) ACCOUNTING POLICIES AND MEASUREMENT CRITERIA

Following Legislative Decree no. 38 of 28 February 2005, exercising the power granted by EEC Regulation no. 1606/2002, from 2006, companies with shares traded on regulated markets in the members states of the European Union are required to prepare their separate financial statements in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board, including interpretations issued by the International Financial Reporting Interpretation Committee (IFRIS) and the Standing Interpretation Committee (SIC), and endorsed by the European Commission (“IFRS”).

Accordingly, Terna SpA has adopted IFRS from 2006, with transition date at 1 January 2005. The last set of separate financial statements prepared in accordance with Italian GAAP are those as of and for the year ended 31 December 2005.

Comparative figures of the previous year have been restated in accordance with IFRS.

Terna SpA, which operates in the electrical energy transmission and dispatching sector, is a public limited company based in Via Arno, 64, Rome.

The Directors approved the publication of these separate financial statements as of and for the year ended 31 December 2006 on 21 March 2007.

International Financial Reporting Standards

The company’s separate financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and the interpretations of the International Financial Reporting Interpretation Committee (IFRIC) and the Standing Interpretation Committee (SIC), endorsed by the European Commission (“IFRS”) at year end, as well as with the measures issued in implementation of article 9 of Legislative Decree no. 38 of 28 February 2005.

In accordance with the provisions of IFRS 1, the paragraph on the “Transition to IFRS” provides IFRS reconciliation schedules at 1 January 2005 and 31 December 2005 to ensure the comparability with the first set of IFRS-compliant financial statements. The figures contained in the reconciliation schedules have not undergone any changes with respect to those included in the document “Transition to IFRS”, which was published with the Terna Group’s half year report at 30 June 2006.

Presentation criteria

The separate financial statements are comprised of the balance sheet, income statement, cash flow statement, statement of recognized income and expenses, statement of changes in equity and the notes thereto.

In the balance sheet, assets and liabilities are classified on a current/non-current basis, with specific mention of assets and liabilities held for sale. Current assets, which include cash and cash equivalents, are those held for realization, sale or consumption in the company's normal operating cycle. Current liabilities are those expected to be settled in the company's normal operating cycle or within one year from the balance sheet date.

The income statement is classified on the basis of the nature of costs, while the cash flow statement has been prepared using the indirect method.

The financial statements have been prepared in euros, while the figures in the notes are given in millions of euros, unless otherwise specified.

The financial statements have been prepared using the historic cost method, with the exception of captions that are recognized at fair value in accordance with IFRS, as indicated in the accounting policies for each caption.

Use of estimates

The preparation of the balance sheet and income statement in accordance with IFRS requires the use of estimates and assumptions that affect the carrying amounts of assets and liabilities and related disclosures, in addition to contingent assets and liabilities at the reporting date. The estimates and associated assumptions are based on previous experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources. The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions of accounting estimates are recognized in the year in which the estimate is revised if the revision affects only that year, or in the year of the revision and future years if the revision affects both current and future years.

The critical areas for key estimates and assumptions used by management in applying IFRS endorsed by the European Commission that could have significant effects on the financial statements or that could give rise to risks that would entail significant adjustments to the carrying amounts of assets and liabilities in subsequent years are summarized below.

Employee benefits

The liability for employee benefits paid upon or following termination of employment in relation to defined benefit plans or other long-term benefits is recognized net of any plan assets and is measured on the basis of actuarial assumptions, estimating the amount of future benefits that employees have vested at the reporting date.

Provisions for contingencies and charges

Accruals to the provisions for contingencies and charges are recognized when, at the reporting date, there is a legal or constructive obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the effect is material, accruals are measured by discounting estimated future cash flows at a discount rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Recoverable amount of non-current assets

Property, plant and equipment and intangible assets are analyzed at least once a year to check for indications of impairment. If there is an indication that an asset may be impaired, its recoverable amount is estimated.
Recoverable amount is the higher of an asset’s fair value, net of costs to sell and its value in use, measured by discounting estimated future cash flows considering available information at the time of estimate and on the basis of subjective assessments of the performance of future variables, such as prices, costs, demand growth rates, production profiles - and discounted at a rate that reflects current market assessments of the time value of money with respect to the investment period and the risks specific to the asset.

Investments in subsidiaries and associates

Investments in subsidiaries are those over which Terna has the power to directly or indirectly govern financial and operating policies as to obtain benefits from their activities. Investments in associates are those over which Terna has significant influence.

In assessing whether or not the company has control or significant influence, potential voting rights that are presently exercisable or convertible are considered.

Investments in subsidiaries and associates are measured at cost, reduced to reflect impairment losses. If the reasons for the impairment losses no longer exist, the carrying amount of the investment reinstated within the limits of the impairment losses, and the reversal is taken to profits or losses.

In the event that an investee's losses attributable to the shareholders of the parent exceed that investments' carrying amount, the latter is written off and any excess is recognized in a specific provision, where the parent is required to meet the legal or construction obligations of the investee or, in any case, to cover its losses.

Translation of foreign currency captions

Terna SpA prepares its financial statements in euros. In these financial statements, all transactions in currencies other than the functional currency are recognized at the exchange rate ruling on the date of the transaction. Monetary assets and liabilities in currencies other than the functional currency are subsequently adjusted at the exchange rate ruling at year end. Any exchange rate differences are taken to profits or losses.

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

Business combinations

All business combinations, including acquisitions of minority interests in entities over which control is already held, are recognized using the purchase method, where purchase cost is equal to the fair value, at the date of exchange, of assets given and liabilities incurred or assumed, plus any costs directly attributable to the combination. This cost is allocated by recognizing the identifiable assets, liabilities and contingent liabilities of the acquired business at fair value. If the purchase cost exceeds the fair value of net assets acquired and attributable to the company, this excess amount is recognized as goodwill or, if negative, taken to profits or losses, after having verified once again that the current values of assets and liabilities acquired and the purchase price have been measured correctly.

Decreases in minority interests, following sale or dilution, in subsidiaries, without losing control, are accounted for accordingly. As a result, the portion of losses or gains realized on the disposal in excess of goodwill subsequently realized is taken to profits or losses.

Property, plant and equipment

Property, plant and equipment are recognized at historic cost, including directly costs attributable to putting the asset in the condition necessary for it to be capable of operating in the manner for which it was acquired. In the event of legal or constructive obligations, cost also includes the present value of the estimated cost of disposal or removal of the asset. The corresponding liability is recognized in the provisions for contingencies and charges. Borrowing costs related to loans taken out to acquire assets are taken to profits or losses in the year to which they refer. Expenses incurred after purchase are recognized as an increase in the carrying amount of the asset to which they relate if it is probable that the future benefits of that cost will flow to the company and if the cost can be reliably measured. All other costs are recognized in profits or losses when incurred.

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

Certain assets that were revalued at 1 January 2005 (transition date) or previously are recognized at the revalued amount, which is considered deemed cost at the date of the revaluation.

Property, plant and equipment are shown net of accumulated depreciation and any impairment losses, which are measured as described below. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset, which is reviewed annually, with revisions applied on a prospective basis.

The depreciation of assets under construction begins when the assets become available for use.
Liabilities associated with items of property, plant and equipment are taken to a specific provision as a balancing entry to the related asset. The amount is taken to profits or losses through the depreciation of the asset.

The main depreciation rates calculated on the basis of the related asset's useful life are as follows:

DEPRECIATION RATE

Civil and industrial buildings	2.50%
Transmission lines	2.50%
TRANSFORMATION STATIONS	
Electrical machinery	2.38%
Electrical devices and equipment	3.13%
Automated and control systems	6.70%
CENTRAL SYSTEMS FOR REMOTE CONDUCTION AND CONTROL	
Devices, electrical equipment and ancillary plants	5.00%
Electronic calculators	10.00%

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

The concession granted to the company, with effect from 1 November 2005, on a free basis by the Minister of Production Activities, to carry out electrical energy transmission and dispatching activities in Italy, runs for twenty-five years and is renewable for another twenty-five years. Under the provisions of articles 18 and 19 of the Decree issued by the Ministry of Production Activities on 20 April 2005, in the event of termination and revocation, or expiry of the concession, the Ministry has the right to purchase assets used directly for the transmission and dispatching activities included in the concession owned by the concession-holder, with the exclusion of plants (lines and stations) that make up the National Transmission Grid. If the Ministry decides to purchase the concession-holder's assets, it will pay the latter an amount, agreed upon by the parties, calculated on the basis of adequate parameters, averaging out the value of the assets with their profitability. Accordingly, the assets directly related to the transmission and dispatching activities, including plants (lines and stations) that make up the portion of the electrical energy transmission grid owned by Terna are classified as property, plant and equipment and are depreciated over their useful lives.
As specified further down, in November 2006, the International Financial Reporting Interpretation Committee ("IFRIC") issued IFRIC Interpretation 12 *Service Concession Arrangements*. The company is currently

evaluating the applicability and any effects that would arise from the adoption of this accounting policy.
Property, plant and equipment acquired under finance lease, through which the company has received substantially all the risks and rewards of ownership, are recognized as company assets at the lower of fair value and the present value of minimum lease payments due, including any amounts to be paid to purchase the asset at the end of the lease. The corresponding liability to the lessor is recognized under financial payables. Assets are depreciated using the criteria and rates described above.
Leases in which the lessor maintains substantially all the risks and rewards of ownership are classified as operating leases. Costs related to operating leases are taken systematically to profits or losses over the term of the lease.

Intangible assets

Intangible assets, which all have finite useful lives, are recognized at cost and shown net of accumulated amortization and any impairment losses, measured as described below.
Amortization is calculated on a straight-line basis over the estimated useful life of the related asset, which is reviewed annually. Any revisions are applied on a prospective basis.
Amortization begins when the asset becomes available for use.
The estimated useful lives of the main intangible assets are given in the specific notes to each caption.
Intangible assets are substantially comprised of the exclusive concession to carry out electrical energy transmission and dispatching activities and other intangible assets. In particular, the company acquired the concession for electrical energy transmission and dispatching activities in Italy on 1 November 2005 when it acquired the TSO business activity. As established in the Decree issued by the Ministry of Production Activities on 20 April 2005, this concession runs for twenty-five years from the date of effective transfer of the activities, functions, assets and legal arrangements of the concession from GSE SpA (formerly GRTN) to Terna SpA.
This intangible asset was initially recognized at cost, which reflected fair value.
Other intangible assets mainly relate to the following:

- the development and innovation of application software to manage the energy invoicing process;
- the development and innovation of application software to protect the electrical energy system;
- software applications related to the development of the power exchange, particularly relating to the registration of operators, consumption units and the development of foreign procedures.

These are amortized over their estimated residual useful lives, which are normally three years, given their rapid obsolescence.

Impairment losses

Property, plant and equipment and intangible assets with finite useful lives are tested at least once a year to check for indications of impairment. If there is an indication that an asset may be impaired, its recoverable amount is estimated.

The recoverable amount of goodwill and intangible assets with indefinite useful lives, where present, as well as intangible assets not yet available for use, is estimated annually.

Recoverable amount is the greater of fair value, net of selling costs, and value in use.

Value in use is measured considering the estimated future cash flows discounted at a pre-tax rate that reflects the time value of money for the investment period and risks specific to the asset. If the intangible asset does not generate cash inflows that are largely independent, the asset's recoverable amount is calculated as part of the cash-generating (CGU) unit to which it belongs.

An impairment loss is recognized in the income statement when the asset's carrying amount or the net invested capital of the CGU to which it belongs, is greater than its recoverable amount.

Impairment losses of CGUs are first taken as a reduction in the carrying amount of any allocated goodwill and then as a reduction in other assets of the CGU on a *pro rata* basis. Except for goodwill, impairment losses may be reversed if there is an indication that the impairment loss no longer exists or when there is a change in the methods used to measure recoverable amount.

Inventories

Inventories are stated at the lower of purchase cost and net realizable value. Cost is calculated as the weighted average cost, including related charges.

Contract work in progress

When the profits or losses of a contract can be reliably estimated, the related contract costs and revenues are recognized separately in profits or losses on a percentage of completion basis. Progress is measured based on the work carried out. Differences between the value of completed contracts and payments on account received are recognized under balance sheet assets or liabilities, considering any impairment losses on the work carried out so as to take into account the risks of customers' refusal to recognize the work performed. Expected contract losses are immediately taken to profits or losses under contract costs.
Contract costs include all those costs that relate directly to the specific contract, as well as fixed and variable costs incurred as part of normal operations.

Financial instruments

Financial assets

Financial assets that the company has the positive intention and ability to hold to maturity are recognized at the settlement date at fair value, including transaction costs. They are subsequently measured at amortized cost, using the effective interest method, net of any impairment losses, which are determined as the lower of the asset's carrying amount and the present value of estimated future cash flows, discounted using the original interest rate. The amount of impairment losses is taken to profits or losses of the year.
Financial assets are derecognized when, following their transfer or settlement, the company is no longer involved in their management and no longer holds the risks and rewards of the transferred or settled instruments.

Trade receivables

Trade receivables are initially recognized at fair value and subsequently measured at amortized cost, using the effective interest method, and net of any impairment losses due to sums considered non-recoverable, which are taken to the specific provision for bad debts. Impairment losses are calculated on the basis of the present value of estimated future cash flows, discounted using the initial effective interest rate.
Receivables with due dates that fall under normal commercial terms are not discounted.

Cash and cash equivalents

Cash and cash equivalents are stated at nominal value. They include cash on hand, i.e., amounts that are available on demand or with a very short maturity, subject to an insignificant risk and without redemption expenses.

Trade payables

Trade payables are stated at amortized cost. If their due date falls under normal commercial terms, they are not discounted.

Financial liabilities

Financial liabilities other than derivatives are stated at fair value at the settlement date, net of directly related transaction costs.
Subsequently, financial liabilities are measured at amortized cost, using the original effective interest method. If the liabilities are subject to fair value hedges, they are adjusted to reflect changes in fair value with respect to the hedged risk.

Derivative financial instruments

Derivatives are recognized at fair value at the trade date and classified as hedges if the relationship between the derivative and the hedged item is formally documented and the hedge is highly effective and ranging from 80% to 125%, as initially verified and periodically checked. When derivatives cover the risk of fluctuations in the cash flows of the hedged instruments (cash flow hedges), the effective portion of changes in the fair value is initially taken to equity and subsequently to profits or losses, in line with the effects of the hedged transaction.
The ineffective portion of fair value is taken to profits or losses.

When hedging derivatives cover the risk of fluctuations in the fair value of hedged instruments (fair value hedges), they are recognized at fair value through profits or losses. Accordingly, the hedged items are adjusted to reflect changes in the fair value associated with the hedged risk.

Fair value is measured with reference to official quotations for instruments traded in regulated markets. The fair value of instruments not traded in regulated markets is measured by discounting projected cash flows along a yield curve of interest rates at the reporting date, and by converting amounts in currency other than the Euro at the year-end exchange rate.

Employee benefits

The liability related to employee benefits payable upon or after termination of employment relates to defined benefit plans (termination benefits, additional month's pay[13], indemnity for lack of notice[14], energy discount, ASEM health benefits and other benefits) or other long-term employee benefits (loyalty bonus) is recognized net of any plan assets. It is measured separately for each plan on the basis of actuarial calculations that estimate the amount of future benefits employees have accrued at the reporting date. The liability is recognized on an accruals basis over the vesting period. It is measured by independent actuaries. Actuarial gains and losses at 1 January 2005 (date of transition to IFRS) were recognized in equity. If, after that date, unrecognized actuarial gains and losses arise in excess of 10% of the greater of the present value of the defined benefit plan obligation and the fair value of plan assets, that portion is taken to profits or losses for the average expected term of service of employees participating in the plan. Otherwise, actuarial gains and losses are not recognized.

At the reporting date, the effects of new regulations concerning termination benefits were not considered, as uncertainty remains as to whether the company has an obligation to employees who will opt to have their termination benefits managed by INPS. These employees could make up the entire workforce, if there is no participation in the management plans.

(13) "IMA"
(14) "ISP"

Share-based payments

The cost of employee service remunerated through stock option plans is measured at the fair value of the options granted to employees at the grant date. The fair value of options granted is recognized under personnel expenses over the vesting period, with a corresponding increase in equity, considering the best possible estimate of the number of options that employees will be able to exercise.
The measurement method used to calculate fair value considers all the characteristics of the options (duration, price and conditions, etc.), as well as the value of the Terna share at the grant date, the volatility of the share and the interest rate curve at the grant date, in line with the duration of the plan. The Cox-Rubinstein pricing method is used. The amount recognized as cost is adjusted to reflect the actual number of vesting options, unless the failure to meet the conditions to obtain the right is based solely on the market.

Provisions for contingencies and charges

Accruals to the provisions for contingencies and charges are recognized when, at the reporting date, the company has a legal or constructive obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the effect of the time value of money is material, accruals are measured by discounting estimated future cash flows using a pre-tax discount rate that reflects current market assessments of the time value of money and those risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as an interest expenses. Changes in estimates are taken to profits or losses in the year to which they relate.

Grants

Grants from public and private entities are recognized at fair value when it is reasonably certain that they will be received and that the conditions provided for obtaining the grants will be satisfied.

Grants received for specific expenditure are recognized under other liabilities and taken to the income statement on a systematic basis over the period in which the related costs accrue.

Grants received in relation to specific assets whose value is recognized under non-current assets are, for plants operating before 31 December 2002, recognized under other liabilities and taken to the income statement over the depreciation period of the related assets. From 2003, grants for new plants going into use are taken as a direct reduction in the value of the related asset.

Grants for operating expenses are expenses in full when the conditions for recognition are satisfied.

Revenues

Depending on the type of transaction, revenues are recognized on the basis of the following specific criteria:

- revenues from the sale of goods are recognized when the significant risks and rewards of ownership of the goods have been transferred to the buyer;
- revenues from the rendering of services are recognized with reference to the stage of completion of the transaction. If revenues cannot be reliably measured, they are recognized to the extent of recoverable costs.

In particular, revenues from fees to use the National Transmission Grid are measured based on the tariffs established by the Electricity and Gas Regulator.

Considerations collected on behalf of third parties, such as the consideration paid to other non-Terna grid owners, as well as revenues recognized for managing activities related to the balancing of the national electrical energy system, which do not increase equity, are shown net of the related costs.

Financial income and expenses

Financial income and expenses are recognized on an accruals basis in line with the interest amount of related financial assets and liabilities, using the effective interest method.

Dividends

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

Basic earnings per share

Basic earnings per share are calculated by dividing the profits for the year attributable to holders of ordinary shares by the weighted average of outstanding ordinary shares during the year.
Diluted earnings per share are calculated by dividing the profits for the year attributable to holders of ordinary shares by the weighted average of outstanding shares, adjusted to consider the effects all potential ordinary shares, which have a diluting effect.

Income taxes

Current income taxes are recognized as tax liabilities, net of advances paid, or tax assets where the net balance of the captions is positive. They are based on the estimated taxable income and in accordance with current legislation.
Deferred tax assets and liabilities are calculated on the temporary differences between the carrying amounts of assets and liabilities recognized in the consolidated financial statements and the corresponding amounts recognized for tax purposes, in application of current tax rates, or rates expected to be in effect when the temporary differences reverse, based on current rates or those that are substantially approved at the reporting date.
Deferred tax assets are recognized when their recovery is considered probable, i.e., when future taxable profits will be available against which the asset can be used. The recoverability of deferred tax assets is reviewed at each year end.
Deferred tax liabilities are recognized in any case if they exist.

New reporting standards

In 2006, no new standards or interpretations were approved and no amendments were made to the standards and interpretations in effect as from 1 January 2006, with a significant impact on the consolidated financial statements.

Regulations nos. 108/2006, 708/2006 and 1329/2006 issued by the European Commission modified certain standards and interpretations already in place, exclusively with respect to disclosure requirements. The following standards and interpretations were approved, and could become applicable to the company's financial statements in the future.

IFRS 7 - Financial instruments: additional disclosures

IFRS 7 requires additional disclosures on the relevance of financial instruments with respect to the company's performance and financial position. These disclosures incorporate certain requirements that were previously included in IAS 32 - Financial Instruments: Disclosure and Presentation. The new standard also requires information on the level of risk exposure arising from the use of financial instruments and a description of the objectives, policies and procedures implemented by management to manage such risks. IFRS 7 takes effect from years beginning on 1 January 2007 or subsequently.

IFRS 8 - Operating Segments

IFRS 8 establishes how a company should report on operating segments in the annual financial statements and, as an amendment to IAS 14 - Segment Reporting, requires the same information also in interim reports. In addition, it defines disclosure requirements with respect to products and services, the geographical areas in which the company operates and its key customers. The new standard is the result of the comparison of IAS 14 and SFAS 131 - Disclosures about Segments of an Enterprise and Related Information, as part of the IFRS and US GAAP convergence project, to reduce the discrepancies between the two.

IFRS 8 supersedes IAS 14 and is applicable to financial statements for years beginning on 1 January 2009. However, early application is allowed.

IFRIC 8 - Scope of IFRS 2

This interpretation clarifies when IFRS 2 must be applied to transactions in which the company cannot specifically identify a portion or all of the goods or services received. IFRIC 8 takes effect from years beginning on 1 May 2006 or subsequently.

IFRIC 9 - Revaluation of embedded derivatives

This interpretation requires a specific assessment so that embedded derivatives are separated from the host contract and recognized as derivatives when they become part of the contract. IFRIC 9 takes effect from years beginning on 1 June 2006 or subsequently.

Moreover, in 2006, the relevant international bodies issued the following amendments to existing standards and new interpretations, which have not yet been endorsed by the European Commission.

IFRIC 10- Interim financial reporting and impairment

This interpretation clarifies that in the preparation of annual financial statements, companies are not permitted to reverse any impairment losses recognized in previous interim financial statements in relation to the impairment of goodwill, financial investments carried at cost or investments or financial assets carried at cost.

This interpretation is applicable to financial statements for years beginning on 1 November 2006. However, early application is allowed.

IFRIC 11 - IFRS 2 Group and treasury share transactions

This interpretation clarifies the recognition methods for share-based payments (e.g., stock option plans to employees) between Group companies.

This interpretation is applicable to financial statements for years beginning on 1 March 2007. However, early application is allowed.

IFRIC 12 - Service Concession Arrangements

IFRIC 12 substantially confirms the recognition methods provided for by the previous three draft interpretations (D12, D13 and D14) concerning assets (freely transferable assets), liabilities (reclamation provisions), revenues and costs in connection with service concession arrangements between a public body and a private company. It excludes concessions between private companies.

This interpretation is applicable to financial statements for years beginning on 1 January 2008. However, early application is allowed. The company is evaluating the impact that all of the amendments and new standards and interpretations could have on the financial statements, considering the date they take effect.

As described below, certain balances of the financial statements at 31 December 2005 have been reclassified, for the purpose of a more correct presentation. However, equity figures as of 31 December 2005 and income statement figures for 2005 have not been modified.

Risk Management

Interest rate risk

In carrying out its operations, Terna is exposed to the risk of fluctuations in interest rates. Its main source of interest rate risk relates to items of net financial indebtedness that generate interest expenses. Terna's strategy for financial indebtedness is to focus on long-term loans, which reflect the useful life of company assets. It pursues an interest rate risk hedging policy that aims to combine this choice with the regulatory context, which every four years establishes the cost of debt as part of the formula to set Regulatory Asset Based (RAB) remuneration.

Accordingly, the hedging instruments used, at various maturity dates, include both derivatives that transform fixed rates into variable rates (fair value hedges) and derivatives that transform variable rates into fixed rates (cash flow hedges and trading).

With the aim of reducing the amount of financial indebtedness exposed to the risks of fluctuations in interest rates and reducing the cost of funding, two types of plain vanilla derivatives have been used, i.e. interest rate swaps and interest rate collars. At year end, considering the transactions in derivatives, 66.1% of Terna SpA's gross indebtedness bears interest at fixed rates, while net indebtedness bearing interests at fixed rates amounts to 67.2%.

All derivative contracts have a notional amount and maturity date less than or equal to that of the underlying financial liability, so that any change in the fair value and/or projected cash flows of the contracts is offset by a corresponding change in the fair value and/or projected cash flows of the underlying position.

In terms of liquidity risk, considering that there is normally a negative difference between interest received on loans granted and interest paid on loans received, financial optimization activities are geared towards minimizing liquidity positions in line with the company's needs.

The following table provides the notional amount and fair value of derivatives, net of accruals, at 31 December 2006. The fair value of derivatives is measured by discounting estimated cash flows at market interest rates at the reporting date.

	NOTIONAL AMOUNT		FAIR VALUE	
In millions of euros	2006	2005	2006	2005
Derivatives hedging the fixed rate bond	1,400.0	1,280.0	11.3	106.1
Derivatives hedging variable rate loans	186.3	269.0	-6.2	-17.8
Other hedging derivatives	1,150.0	850.0	0.7	-11.2
TOTAL	**2,736.3**	**2,399.0**	**5.8**	**77.1**

The fair value of the two bonds (euros 600 million maturing in 2014 and euros 800 million maturing in 2024), was also measured by discounting estimated cash flows at market interest rates at the reporting dates, for a total of euros 1,406.6 million, net of accruals.

The notes to the balance sheet provide the notional amount and fair value of derivatives in place at year end, grouped by current and non-current financial assets and liabilities.

Sensitivity to interest rate risk

If the Eurozone interest rate curve were to rise or drop 50 bps at 31 December 2006, the average cost of Terna SpA debt would fluctuate by approximately 35 bps, for a total of roughly euros 7 million.

Credit risk

Terna provides its services exclusively to counterparties considered solvent by the market, i.e., they have high credit ratings. Moreover, the company does not have concentrations of credit risk.

Credit risk arising from open positions in derivative financial instruments is considered marginal, since the counterparties are leading Italian and international banks with high ratings and the management of these transactions is fractioned off, in compliance with specific concentration limits.

Exchange rate risk

The company carries out transactions with counterparties residing in non-EU countries. It has marginal exposure to the risk of fluctuations in the US$/R$ exchange rate. The company evaluates the individual transactions and sets up hedges where necessary and in compliance with financial risk management policies.

B) SEGMENT REPORTING

The segments were identified and Terna's primary and secondary segments were determined considering the organizational structure and internal reporting system. In particular, since the risks and rewards of the company's investments are exclusively affected by differences in the services provided, the primary reporting segment is based on the activities performed (transmission/dispatching/metering), while the activities are not reported geographically, since they are performed mainly in Italy. Specific allocation parameters have been established for income and expenses and assets and liabilities not specifically attributable to individual sectors (in particular, financial assets and liabilities, tax assets and liabilities and deferred tax assets and liabilities). They are indicated separately.

In addition, intersegment transfers are measured at current market conditions.

Reporting by business segment is provided below for 2005 and 2006:

2005

	REGULATED ACTIVITIES - ITALY				
In millions of euros	Transmission	Dispatching	Metering	Unregulated activities	Total
Revenues	830.2	17.7	1.5	60.9	910.3
Segment revenues	**458.5**	**-2.3**	**1.5**	**27.1**	**484.8**
Unallocated expenses					54.3
Operating profits					**430.5**
Financial income/(expenses)					-10.7
Income taxes					154.2
Profits for the year					**265.6**
OTHER INFORMATION					
Segment assets	4,285.4	1,090.4	2.2	314.1	5,692.1
Segment liabilities	2,802.2	837.9	-	254.1	3,894.2
Investments	257.8	3.2	-	-	261.0
Amortization, depreciation and impairment losses	150.9	6.2	-	-	157.1
Other non-monetary expenses	0.9	-	-	-	0.9

2006

In millions of euros	Regulated activities - Italy: Transmission	Dispatching	Metering	Unregulated activities	Total
Revenues	943.2	105.0	9.3	52.7	1,110.2
Segment revenues	**631.4**	**1.4**	**8.0**	**20.3**	**661.1**
Unallocated expenses					110.3
Operating profits					**550.8**
Financial income/(expenses)					16.1
Income taxes					211.1
Profits for the year					**355.8**
OTHER INFORMATION					
Segment assets	4,656.7	1,345.0	10.4	260.2	6,272.3
Segment liabilities	2,770.3	1,309.4	2.0	288.9	4,370.6
Investments	324.2	20.7	0.1	-	345.0
Amortization, depreciation and impairment losses	167.7	34.1	0.4	-	202.2
Other non-monetary expenses	0.2	-	-	-	0.2

C) NOTES TO THE INCOME STATEMENT

Revenues

1) REVENUES FROM GOODS AND SERVICES - euros 1,083.5 million

The table below details revenues of the year:

In millions of euros	2006	2005	Change
Grid transmission consideration	947.0	786.8	160.2
Adjustments for prior year grid transmission consideration	47.3	34.8	12.5
Other energy revenues	41.9	6.9	35.0
Other revenues from goods and services	47.3	59.3	-12.0
TOTAL	**1,083.5**	**887.8**	**195.7**

Grid transmission consideration

This is revenues from the company's core business. It is the consideration paid to the company for use of the National Transmission Grid, and also includes the additional portion of the grid transmission consideration (AEEG Resolution no. 15/2005) paid to Terna with the integration of the TSO business activity (euros 71.0 million).

The euros 160.2 million increase on 2005 is mainly due to the following two factors:

- increased revenues relating to the remuneration of the national electricity grid (up euros 101.3 million), in Italy, especially following the new tariffs, which took effect in 2006, as well as to the higher volumes of transmitted energy (up 2.2%); during 2005 the AEEG adjusted tariffs (as detailed in the paragraph below), therefore also affecting 2006 tariffs;
- the grid transmission consideration arising from the merger of the TSO business activity (euros 58.9 million) from GSE SpA, recognized for only two months in 2005, since the acquisition took effect on 1 November 2005.

Adjustments for prior year grid transmission consideration

These relate to revenues earned by the company (euros 47.3 million) in accordance with AEEG Resolution no. 162/06 of 27 July 2006, which established the offsetting of the tariff deficit for transmission services provided in 2005 with payment to all owners of portions of the National Transmission Grid.

In 2005, this caption included adjustments from GSE SpA for the grid transmission consideration of previous years (euros 19.8 million) and revenues from the release of the provision for contingencies which had been accrued for doubtful grid transmission considerations (Cip 6 - autoproducers litigation - euros 15.0 million). At 31 December 2005, these amounts totalled euros 34.8 million and were stated under “Other revenues and income”.

Other energy revenues

This caption relates to the consideration due to the company by operators for metering activities (MIS component - euros 9.3 million) and to the consideration for the acquisition of resources necessary for dispatching requirements (DIS component - euros 32.3 million). In 2005, these items related to only the last two months of the year, that is from the acquisition date of the business activity from GSE (1 November 2005).

The caption also includes the consideration as per AEEG Resolution no. 34/05 (euros 0.3 million) to cover the administrative and management costs incurred to withdraw energy from renewable sources producers with a power not exceeding 10 MVA and similar connected to the National Transmission Grid.

Other energy items - energy in transit revenues/costs

This caption includes the cost and revenues of energy in transit (the balance is nil) arising from daily purchases and sales with operators on the electricity market to carry out transmission and dispatching activities. The components of these transactions are detailed below. Those related to 2005 refer only to the last two months of the year:

In millions of euros	2006	2005	Change
REVENUES - POWER EXCHANGE			
procurement of resources on the ancillary services market	1,502.4	217.3	1,285.1
unbalancing and others	1,313.1	270.5	1,042.6
sale of energy on the day-ahead market, adjustment market, ancillary services market and others	885.1	106.2	778.9
foreign market - exports	2.9	0.3	2.6
other items - Power exchange	3.5	0.4	3.1
Total revenues - Power Exchange	**3,707.0**	**594.7**	**3,112.3**
REVENUES FROM OUTSIDE THE POWER EXCHANGE			
revenues under Laws no, 168/04 - 237/04 and others	820.0	117.5	702.5
revenue from grid transport considerations of other owners and portion of GRTN CIP/6	113.0	16.9	96.1
other items (returns, CBT)	389.5	11.7	377.8
Total revenues from outside the Power Exchange	**1,322.5**	**146.1**	**1,176.4**
TOTAL REVENUES FROM ENERGY IN TRANSIT	**5,029.5**	**740.8**	**4,288.7**
COSTS - POWER EXCHANGE			
to provide the dispatching service	2.800.6	450.2	2,350.4
for unbalancing	478.5	39.0	439.5
on the day-ahead and adjustment markets	323.3	64.0	259.3
on the foreign market - imports	91.7	39.7	52.0
Electricity market operator fees	8.0	1.4	6.6
other items	4.9	0.4	4.5
Total costs - Power Exchange	**3,707.0**	**594.7**	**3,112.3**
COSTS FROM OUTSIDE THE POWER EXCHANGE			
costs under Laws no, 168/04 - 237/04 and others	820.0	117.5	702.5
fees to be paid to National Transmission Grid owners, GRTN and others	113.0	16.9	96.1
other items (returns, CBT)	389.5	11.7	377.8
Total costs from outside the Power Exchange	**1,322.5**	**146.1**	**1,176.4**
TOTAL EXPENSES FOR ENERGY IN TRANSIT	**5,029.5**	**740.8**	**4,288.7**

Other revenues from goods and services

Other revenues from goods and services amounted to euros 47.3 million (2005: euros 59.3 million) and mainly relate to revenues from a variety of specialized high and extra high voltage services, which the company provides to third party customers:

- revenues from Enel Distribuzione SpA (euros 16.1 million) arising from the maintenance agreement for the high-voltage lines owned by that company (down euros 4.4 million on 2005);
- revenues from the Wind Group (Enel.net/Wind: euros 7.1 million) for the operating, maintenance and

development of the optical fibre owned by Wind Group on Terna SpA plants (safety cables);

- a variety of specialized services in the maintenance of high-voltage plants owned by third parties for several customers (euros 20.7 million);
- requests to connect to the National Transmission Grid as per AEEG Resolution no. 281/05 (euros 1.4 million);
- revenues from RTL Group subsidiaries (euros 2.0 million) for:
  - management fee services (euros 0.6 million) and high-voltage plant operating and maintenance services (euros 1.0 million) provided to RTL SpA;
  - high-voltage line operating and maintenance services (euros 0.4 million) provided to RTM1 SpA.

2) OTHER REVENUES - euros 26.7 million

Other revenues and income

Other revenues is detailed as follows:

In millions of euros	2006	2005	Change
Third party contributions for highvoltage connections	12.1	10.2	1.9
Other revenues	9.7	7.0	2.7
Gains on the sale of plant parts	1.7	0.8	0.9
Prior year income	3.2	4.5	-1.3
TOTAL	**26.7**	**22.5**	**4.2**

This caption includes, in particular, portions of third party contributions for connections to the National Transmission Grid pertaining to the year (euros 12.1 million), rental income (euros 6.8 million, including invoices of the year, relating to second half of the year only, issued to the Wind Group in connection with the housing of optical fibre on the company's grids - euros 4.7 million), other sales (euros 1.0 million), insurance compensation for damage to plants (euros 0.5 million), prior year income (euros 3.2 million) and gains on the sale of plant parts to third parties (euros 1.7 million). The prior year income for adjustments from GSE SpA on the grid transmission consideration of previous years (euros 19.8 million) and the release of the provision for contingencies already accrued for the grid transmission consideration (euros 15.0 million) recognized in 2005, were reclassified to "Revenues from goods and services".

Operating Expenses

3) RAW MATERIALS AND CONSUMABLES - euros 18.1 million

In millions of euros	2006	2005	Change
Inventory procurement	10.7	10.7	-
Supply of materials and equipment	5.3	8.4	-3.1
Other supplies	2.7	1.9	0.8
Change in inventories	-0.6	2.9	-3.5
TOTAL	**18.1**	**23.9**	**-5.8**

This caption includes costs incurred to purchase materials and sundry equipment used in ordinary operations and plant maintenance. It also includes the change in inventories during the year.

4) SERVICES - euros 123.7 million

In millions of euros	2006	2005	Change
Tenders on plants	22.3	20.1	2.2
Sundry services	48.3	34.3	14.0
Insurance	3.9	4.7	-0.8
Remote transmission and telephone	18.2	21.4	-3.2
IT services	12.9	13.5	-0.6
Use of third party assets	18.1	12.7	5.4
TOTAL	**123.7**	**106.7**	**17.0**

This caption increased by euros 17.0 million on 2005 mainly because the company was fully operative as TSO integrated operator for the entire year. These costs related to the last two months of 2005 only.

This caption mainly includes the costs of maintenance and repairs in relation to tenders and services for ordinary maintenance activities, as well as maintaining the efficiency of plants (euros 22.3 million). It also relates to remote transmission and telephone services (euros 18.2 million), IT services (euros 12.9 million), leases, rentals (euros 18.1 million) and general services. It includes the fees paid to the members of the Board of Statutory Auditors for the year (euros 0.2 million).

The following table summarizes fees paid to Terna SpA Directors and Statutory Auditors. It shows their term of office and has been prepared on an accruals basis.

Surname and Name	Position	Term of office	Expiry	Fees	Bonuses and other incentives **	Total
Roth Luigi	Chairman/Director	Jan-06/Dec-06	Approval of the 2007 financial statements	254,999.98		254,999.98
Cattaneo Flavio	CEO	Jan-06/Dec-06	Approval of the 2007 financial statements	233,333.34	16,666.67	250,000.01
De Paoli Luigi	Director	Jan-06/Dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Garaffo Mario	Director	Jan-06/Dec-06	Approval of the 2007 financial statements	95,000.00		95,000.00
Machì Salvatore	Director	Jan-06/Dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Macrì Carmine	Director	Jan-06/Dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Maranesi Piero Giuseppe	Director	Jan-06/Dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Rispoli Vittorio	Director	July-06/Dec-06	Approval of the 2007 financial statements	16,250.00		16,250.00
Smurro Franco	Director	Jan-06/Dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Romano * Massimo	Director	Jan-06/Dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Ponzellini Massimo	Director	Jan-06/July-06	Approval of the 2007 financial statements	32,500.00		32,500.00
Total fees - Directors				**962,083.32**	**16,666.67**	**978,749.99**
Ferreri Giovanni	Chairman of the Board of Statutory Auditors	Jan-06/Dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Corvace Giancarlo	Standing auditor	Jan-06/Dec-06	Approval of the 2007 financial statements	45,000.00		45,000.00
Tasca Roberto	Standing auditor	Jan-06/Dec-06	Approval of the 2007 financial statements	45,000.00		45,000.00
Total fees - Statutory Auditors				**145,000.00**		**145,000.00**
TOTAL				**1,107,083.32**	**16,666.67**	**1,123,749.99**

* With respect to the positions held, fees totalling euros 55,000.00 were transferred to Enel SpA.
** This amount relates to the variable portion of the fee for 2005, approved and disbursed in 2006.

5) PERSONNEL EXPENSES - euros 237.0 million

In millions of euros	2006	2005	Change
SHORT-TERM EMPLOYEE BENEFITS			
wages and salaries	155.8	126.9	28.9
social security contributions	48.5	32.1	16.4
other	3.3	2.6	0.7
directors	1.1	1.1	-
POST-EMPLOYMENT BENEFITS			
Defined benefit plans			
electricity discount	2.5	8.8	-6.3
asem-acem	0.6	1.7	-1.1
Defined contribution plans			
fopen	1.3	1.1	0.2
fondenel	0.4	0.2	0.2
EMPLOYEES' TERMINATION BENEFITS			
leaving incentives	13.1	15.2	-2.1
Employees' stock option plans	0.8	0.2	0.6
Termination benefits	9.6	8.7	0.9
TOTAL	**237.0**	**198.6**	**38..4**

This caption includes the cost of wages and salaries, social security contributions and other costs incurred by the company for leaving incentives, as well as benefits paid to employees who stay with the company and termination benefits provided for by the current national labour contract for the electrical energy sector. Personnel expenses increased by euros 38.4 million, mainly due to the costs following the acquisition of the TSO business activity and the addition of its personnel (wages, salaries, social security contributions and termination benefits up euros 39 million on 2005). The main changes were as follows:

- additional social security contributions borne by the company for CIG and CIGS (euros 9.8 million);
- lower termination benefits (down euros 7.7 million) mainly related to the electricity discount which decreased, *inter alia*, following the reorganization of the criteria for eligible parties;
- financial effects (euros 2.4 million) of the renewal of employees' labour contract which was signed in July 2006.

The following table shows the number of employees by category at year end and the average number for the year:

	Average number 2006	Average number 2005	Number at 31.12.2006	Number at 31.12.2005
Managers	72	43	71	74
Junior managers	419	248	431	403
White collars	1,810	1,532	1,816	1,813
Blue collars	1,069	1,143	1,049	1,098
TOTAL	**3,370**	**2,966**	**3,367**	**3,388**

The net change with respect to 31 December 2005 is a decrease of 21 employees.

Reference should be made to paragraph "22) Termination benefits and other employee-related provisions" for the reconciliation of the opening and closing present value of the liability for employee benefits and the main assumptions used in the actuarial estimate.

6) AMORTIZATION, DEPRECIATION AND IMPAIRMENT LOSSES - euros 202.2 million

These relate to accruals during the year calculated on the basis of amortization and depreciation rates that reflect the useful lives of the company's plant, property and equipment and intangible assets. This caption increased by euros 45.1 million on 2005, mainly following the acquisition of the TSO business activity (euros 13.3 million) and the new plants that began operating during the year (euros 6.0 million), as well as the redetermination of the residual useful lives of certain plants (euros 6.9 million).

The caption also includes accruals to the provision for bad debts of euros 12.1 million, relating to receivables due to the company for energy items which are reasonably unlikely to be collected.

7) OTHER OPERATING EXPENSES - euros 15.0 million

In millions of euros	2006	2005	Change
Local taxes and duties	4.5	10.5	-6.07
Prior year expenses	2.4	3.5	-1.1
Losses on the sale/disposal of plants	2.8	3.2	-0.4
Other operating expenses	5.3	2.7	2.6
TOTAL	**15.0**	**19.9**	**-4.9**

This caption mainly includes indirect local taxes, as well as losses on the disposal of plants and other residual operating expenses. The euros 4.9 million decrease on 2005 is mainly due to:

- the registration tax for the acquisition of the TSO business activity paid in 2005 (down euros 2.8 million);
- taxes on interest on equity paid abroad in 2005 which are not deductible in Italy (down euros 3.7 million);
- contractual penalties for services and use of third party assets paid by the company (up euros 2.1 million).

8) CAPITALIZED INTERNAL WORK - euros -36.6 million

Capitalized expenses relate to personnel expenses (euros 27.5 million) and the consumption of materials and equipment in inventories (euros 9.1 million) for plants under construction. The euros 10.1 million increase is fully attributable to personnel expenses.

Financial income and expenses

9) NET FINANCIAL INCOME/(EXPENSES) - euros 16.1 million

This caption is detailed as follows:

In millions of euros	2006	2005	Change
FINANCIAL INCOME			
Interest income on former intercompany current account with Enel SpA	-	3.3	-3.3
Financial income from subsidiaries	40.1	39.3	0.8
Income on trading derivatives	8.8	-	8.8
Value changes of the hedged bond	-	3.7	-3.7
Other financial income	43.4	1.9	41.5
Exchange rate gains	-	4.4	-4.4
Total income	**92.3**	**52.6**	**39.7**
FINANCIAL EXPENSES			
Interest expenses on medium/long-term loans	-64.6	-55.3	-9.3
Financial expenses from subsidiaries	-0.8	-	-0.8
Expenses on trading derivatives	-	-2.0	2.0
Value changes of the hedged bond	-2.6	-	-2.6
Discounting of termination benefits and other employee-related provisions	-6.6	-5.9	-0.7
Other financial expenses	-	-0.1	0.1
Exchange rate losses	-1.6	-	-1.6
Total expenses	**-76.2**	**-63.3**	**-12.9**
TOTAL INCOME/(EXPENSES), NET	**16.1**	**-10.7**	**26.8**

Net financial income of the year amounts to euros 16.1 million, up euros 26.8 million on 2005. The change is due to the combined effect of a variety of factors. In particular:

- an increase in other financial income (euros 41.5 million) mainly related to the gain on the sale of 17.4% of Terna Participações shares. The sale was carried out by launching an IPO on the São Paulo Stock Exchange in Brazil (euros 38.4 million);
- the net positive effects of the fair value adjustment of the bond and related hedges, as well as additional derivative instruments in the company's portfolio (up euros 4.5 million);
- an increase in financial expenses due to medium/long-term indebtedness (up euros 9.3 million) mainly following the rise in interest rates with repercussions on the bond and the related hedges (up euros 11.0 million) and the EIB loans bearing interests at variable rates and the related hedges (down euros 1.6 million).
- exchange rate losses recognized in 2006 (euros 1.6 million), compared to the exchange rate gains recognized in 2005 (euros 4.4 million) due to the appreciation of the Brazilian real against the euro;

- higher financial expenses due to the discounting of employee benefits (euros 0.7 million);
- lower financial income (down euros 3.3 million) in relation to the intercompany current account, which was still open in 2005 with Enel SpA and closed on 15 September 2005.

10) INCOME TAXES - euros 211.1 million

Income taxes of the year amount to euros 211.1 million, with an impact on profits before taxes of 37.80% (net of tax adjustments relating to previous years). This figure is in line with the 37.57% of 2005, when income taxes amounted to euros 154.2 million.

Income taxes of the year are detailed as follows:

In millions of euros	2006	2005	Change
INCOME TAXES			
Current taxes:			
- IRES	194.7	136.6	58.1
- IRAP	39.6	28.6	11.0
Total current taxes	**234.3**	**165.2**	**69.1**
Temporary differences:			
- deferred tax income	-13.7	-9.5	-4.2
- deferred tax expenses	9.2	30.7	-21.5
Reversal of temporary differences:			
- deferred tax income	2.6	10.6	-8.0
- deferred tax expenses	-18.1	-37.2	19.1
Total deferred tax income	**-20.0**	**-5.4**	**-14.6**
Adjustments to income taxes of previous years	-3.2	-5.6	2.4
TOTAL	**211.1**	**154.2**	**56.9**

Current taxes

The increase in current taxes (up euros 69.1 million), mainly due to the significant growth in the profits for the year, was also a result of the following factors:

- recognition of the tax gain (IRES - article 110 of the Consolidated Income Tax Act) arising from the contribution of investments in the Brazilian operating companies TSN and Novatrans to the Brazilian subsidiary Terna Participações (euros 7.8 million). The transaction was completed in June 2006;
- recognition of the gain arising from the IPO of Terna Participações on Brazil's São Paulo stock exchange, corresponding to the portion in excess of the tax amount already released upon contribution of the shares (euro 1.3 million);
- increased non-deductible depreciation (euros 2.4 million);
- non-deductible accruals to the provisions for contingencies and the provision for bad debts (up euros 13.0 million);
- application of Decree Law no. 262/06, with effect from the year, which establishes the total non deductibility of all costs related to company cars (up approximately euros 1.1 million);
- taxes of euros 3.1 million on the fair value of derivative financial instruments not for hedging purposes and relevant for tax purposes (article 112 of the Consolidated Income Tax Act);
- change in the average IRAP rate of the year (4.72%) with respect to that calculated at 31 December 2005 (4.43%) (up euros 1.9 million).

Deferred tax income and expenses

Deferred tax income and expenses (-euros 20.0 million) decreased by net euros 14.6 million, mainly as a result of the following events:

- deferred tax income, net (euros 11.1 million) recognized in connection with temporary differences which arose during the year for accruals for personnel incentives (leaving incentives and bonuses) and the provision for bad debts in excess of the tax-deductible portion;
- the net utilization of deferred taxes (euros 5.4 million) mainly related to the effects of the introduction of Italian Law no. 266 of 23 December 2005, which introduced limitations on the tax deductibility of depreciation;
- the realignment of deferred tax expenses to the new average IRAP rate (up euros 3.5 million), as a result of the best estimate of the rate that will be in force when the deferred tax expenses is released.

Adjustments to income taxes of previous years were also recognized, generating income of euros 3.2 million.

For a better presentation of the differences between the theoretical and actual tax rates, the table below reconciles the profits before taxes with the taxable base for IRES purposes:

In millions of euros	Taxable base	Tax
Profits before taxes	566.8	-
Theoretical tax charge	-	187.0
Change in provisions	19.5	6.4
Incentives and employee benefits	7.7	2.5
Dividends - non-taxable portion	-40.0	-13.2
Tax recovery of excess and accelerated depreciation	51.5	17.0
Excess and accelerated depreciation	-18.9	-6.2
Other increases/decreases	3.3	1.1
TOTAL IRES (33%)	**589.9**	**194.7**

The table below shows the differences between the theoretical and actual IRAP tax rates:

In millions of euros	Taxable base	Tax
Operating profits	550.8	-
Theoretical tax charge	-	26.0
Personnel expenses	211.4	10.0
Provision for bad debts	12.1	0.6
Tax recovery of excess and accelerated depreciation	51.5	2.4
Excess and accelerated depreciation	-18.9	-0.9
Other increases/decreases	31.4	1.5
TOTAL IRAP (4.72%)	**838.3**	**39.6**

11) EARNINGS PER SHARE

Basic earnings per share amount to euros 0.178, in which the numerator and denominator amount to euros 355.8 million and euros 2,000 million, respectively.

Diluted earnings per share amount to euros 0.177, in which the numerator and denominator amount to euros 355.8 million and euros 2,010 million, respectively.

D) NOTES TO THE CONSOLIDATED BALANCE SHEET

Assets

12) PROPERTY, PLANT AND EQUIPMENT - euros 4,149.0 million

Property, plant and equipment amount to euros 4,149.0 million (euros 4,020.4 million at 31 December 2005). They may be broken down as follows:

In millions of euros	Land	Land related to buildings	Buildings	Plant and machinery	Industrial and commercial equipment	Other assets	Leasehold improvements	Assets under construction and payments on account	Total
Cost at 31.12.2005	**20.6**		**566.1**	**6,758.9**	**42.0**	**30.7**	**0.0**	**375.6**	**7,793.9**
Investments	2.2		18.4	105.0	2.3	13.6		177.0	318.5
Reclassifications	1.9		20.6	153.0		2.5		-178.0	0.0
Disposals	0.1		-0.3	-26.0	-0.1			-0.6	-26.9
Other changes			-0.9	-12.7					-13.6
Reclassifications			-0.8	2.5		-1.7			0.0
Cost at 31.12.2006	**24.8**		**603.1**	**6,980.7**	**44.2**	**45.1**		**374.0**	**8,071.9**
Accumulated depreciation and impairment losses at 31.12.2005	**-**		**-213.2**	**-3,510.8**	**-29.3**	**-20.2**	**0.0**	**0.0**	**-3,773.5**
Depreciation of the year			-13.6	-151.1	-2.3	-4.4			-171.4
Impairment losses									0.0
Disposals			0.2	21.7	0.1				22.0
Other changes				-					0.0
Reclassifications			0.2	-0.5		0.3			0.0
Accumulated depreciation and impairment losses at 31.12.2006	**-**		**-226.4**	**-3,640.7**	**-31.5**	**-24.3**	**0.0**	**0.0**	**-3,922.9**
Carrying amount									
AT 31 DECEMBER 2006	**24.8**		**376.7**	**3,340.0**	**12.7**	**20.8**		**374.0**	**4,149.0**
AT 31 DECEMBER 2005	**20.6**		**352.9**	**3,248.1**	**12.7**	**10.5**		**375.6**	**4,020.4**

The caption “plant and machinery” includes the electrical energy transmission grid and the transformation stations, the central systems for remote conduction and the national electrical energy control system.

A summary of changes in property, plant and equipment during the year is provided in the table below:

in million of euros

Investments:	
- Transmission lines	120.1
- Transformation stations	148.8
- Other	49.6
Total investments	**318.5**
Depreciation	-171.4
Disposals and other changes	-18.5
TOTAL	**128.6**

Investments of the year mainly include the completion of the Laino-Feroleto-Rizziconi (euros 3.8 million), Turbigo-Rho (euros 15.9 million) and Sardinia-Corsica (euros 2.9 million) long distance lines and the construction of the underwater long distance line SAPEI (euros 34.7 million).
Investments also include the development of the Matera-S.Sofia line (euros 8.2 million) and the Casellina-S.Barbara line (euros 5.9 million). Other investments include the purchase of company cars (euros 16.7 million) and the building in via della Marcigliana (euros 7.2 million).

In terms of assets under construction and payments on account, the main grid development and repowering projects, worth more than euros 5 million, are listed below:

in million of euros

Transmission lines	
KV 380 MATERA - S.SOFIA	80,133,093
SAPEI - DC underwater link	33,230,166
380 kV transformation stations	
FRATTA	8,133,254
CARPI FOSSOLI	6,627,750
CASELLINA	6,503,128
SORGENTE	6,370,000
B. PIGNICELLE	5,205,158
220 kV transformation stations	
MAGENTA	6,245,833

13) INTANGIBLE ASSETS - euros 159.2 million

Changes during the year in intangible assets are detailed below:

in million of euros	Concessions	Other assets	Assets under development and payments on account	Total
BALANCE AT 31.12.2005	134.5	11.3	5.7	151.5
Investments	0.0	16.1	10.4	26.5
Increases on capitalized internal work	0.0	0.5	-0.5	0.0
Amortization	-5.6	-13.2	0.0	-18.8
BALANCE AT 31.12.2006	**128.9**	**14.7**	**15.6**	**159.2**
BALANCE AT 31.12.2005				
Cost	135.4	53.6	15.6	204.6
Accumulated amortization	-6.5	-38.9	0.0	-45.4
Accumulated impairment losses				
BALANCE AT 31.12.2006	**128.9**	**14.7**	**15.6**	**159.2**

Intangible assets amount to euros 159.2 million (euros 151.5 million at 31 December 2005). The increase of the year (euros 7.7 million) is due to changes in investments (euros 26.5 million) and amortization (euros 18.8 million). The caption mainly includes the concession for electrical energy transmission and dispatching activities in Italy which was initially recognized in 2005, at fair value (euros 135.4 million) and subsequently measured at cost.

Other intangible assets mainly relate to the following:

the development and innovation of application software to manage the energy invoicing process;

the development and innovation of application software to protect the electrical energy system;

software applications related to the development of the power exchange, particularly relating to the registration of operators, consumption units and the development of foreign procedures.

These software applications are amortized over their estimated residual useful lives, which are normally three years, given their rapid obsolescence.

14) DEFERRED TAX ASSETS - euros 54.6 million

Deferred tax assets relate to the following captions:

		IMPACT RECOGNIZED IN PROFITS OR LOSSES		
in million of euros	31.12.2005	Accruals	Utilization	31.12.2006
Provision for contingencies and charges	10.4	5.2	-0.8	14.8
Provision for bad debts	0.0	2.1	0.0	2.1
Termination benefits and other employee related provisions	30.5	7.4	-7.2	30.7
CFH and trading derivatives	9.6	0.0	-3.9	5.7
Other	1.3	0.0	0.0	1.3
DEFERRED TAX ASSETS	**51.8**	**14.7**	**-11.9**	**54.6**

The net increase (euros 2.8 million) on 2005 is mainly due to the combined effect of the following:

- the recognition of receivables of euros 5.2 million relating to the non-deductible accruals to the provisions for contingencies;
- the recognition of receivables of euros 2.1 million relating to the non-deductible portion of the accruals to the provision for bad debts;
- the utilization of receivables of euros 3.9 million for the year-end fair value adjustments of cash flow hedge financial instruments.

The change in this caption (euros 2.8 million) does not include the impact of the tax effects on profits or losses of some items, such as the adjustment of cash flow hedge derivatives (euros -3.8 million).

15) FINANCIAL ASSETS

The following table details financial assets recognized in Terna SpA's financial statements:

	CARRYING AMOUNT		
in million of euros	31.12.2006	31.12.2005	Change
FVH derivatives	11.3	106.1	-94.8
Trading derivatives	0.7	0.0	0.7
Investments in subsidiaries	660.0	288.4	371.6
Investments in associates	4.6	4.6	0.0
Non-current financial assets	**676.6**	**399.1**	**277.5**
Deferred assets on FVH derivative contracts	1.5	4.4	-2.9
Other non-current financial assets	1.1	0.0	1.1
Current financial assets	**2.6**	**4.4**	**-1.8**
TOTAL	**679.2**	**403.5**	**275.7**

The carrying amount shown in the table is equal to the fair value of the financial assets recognized in the financial statements.

Non-current financial assets amount to euros 676.6 million, up euros 277.5 million on 2005, mainly due to the following:

- increase in the carrying amount of the investment in the subsidiary RTL SpA following the capital injection by Terna SpA (24 November 2006) for euros 416.8 million, to cover the cost of acquiring AEM Trasmissione SpA and Edison Rete SpA;
- Terna SpA's contribution of the investments in TSN and Novatrans to the Brazilian subsidiary Terna Participações in early June. This transaction did not affect the total balance of investments in Brazilian subsidiaries;
- reduction of euros 44.3 million in the carrying amount of the Brazilian subsidiary Terna Participações following its IPO on the São Paulo stock exchange;
- euros 94.8 million decrease in fair value hedge derivatives due to the rise in the interest rate curve.

The following table shows Terna SpA's financial assets subject to interest rate risk, broken down by due date:

In millions of euros	Maturity	31.12.2005	31.12.2006	Average interest rate
FVH derivatives	2014-2024	106.1	11.3	1.30%
Trading derivatives	2007-2008	0	0.7	0.36%
TOTAL		**106.1**	**12.0**	

Trading derivatives have an impact on the income statement, while fair value hedge derivatives offset the impact of the change in the fair value of the bond. Fair value was calculated using the same method applied in 2005, that is by discounting estimated future cash flows to the market interest rate curve at the balance sheet date.
The increase in the interest rate curve generated an increase in the fair value (up euros 11.9 million) of trading derivatives (a euros 0.7 million increase in non-current financial assets and a euros 11.2 million decrease in non-current financial liabilities) and a decrease (euros 94.8 million) in fair value hedge derivatives. The caption "Investments in associates" entirely relates to the 24.4% investment in Cesi SpA, which amounts to euros 4.6 million, as there is no change with respect to 31 December 2005. This company operates in the construction and management of laboratories and plants for tests, inspections, studies and experimental research relating to the general electro-technical field and its technical and scientific progress.
The following table summarizes Terna SpA's direct investments in subsidiaries and associates at 31 December 2006, compared to the last set of approved financial statements.

Company	Registered offices	Business activity	Share capital	Currency	% of ownership
SUBSIDIARIES					
Terna Participações SA	Rio de Janeiro (Brazil)	Holding company of investments in other companies active in the transmission of electrical energy	1,309.403,148	real	66%
RTL Rete Trasmissione Locale	Rome	Construction and maintenance of electrical energy transmission grids	20,600,000	euro	100%
ASSOCIATES					
Cesi SpA	Milan	Experimental electro-technical research	8,550,000	euro	24.4%

Current financial assets amount to euros 2.6 million (euros 4.4 million at 31 December 2005) and mainly relate to the following:

- a 12-month intercompany financing agreement signed by Terna SpA and Terna Participações (on 6 June 2006) for a maximum of real 20 million (approximately euros 7.1 million at 31 December 2006). The agreement is renewable by Terna SpA for an additional 12 months. Interest accrues on the amount utilized at an annual rate equal to the daily average of the CDI plus a spread of 1.5%. At 31 December 2006, real 1.3 million (euros 0.5 million) had been utilized. The financing was repaid in advance on 20 February 2007, when Terna SpA collected the residual debt of approximately euros 0.5 million.
- deferred assets on FVH derivative contracts, which are entirely related to interest accrued and not yet received at the balance sheet date in connection with the derivative contracts (swaps) agreed to hedge the bond issued.

16) OTHER ASSETS

In millions of euros	31.12.2006	31.12.2005	Change
Receivables due from others:			
- loans and advances to employees	4.6	4.2	0.4
- assets on deposit with third parties	0.2	0.2	0.0
- tax advance on termination benefits	0.5	1.5	-1.0
Other non-current assets	**5.3**	**5.9**	**-0.6**
Receivables from subsidiaries	0.0	27.2	-27.2
Receivables due from others:			
- employees	0.5	0.6	-0.1
- other	16.8	22.6	-5.8
Other current assets	**17.3**	**50.4**	**-33.1**

Non-current assets, detailed above, have not undergone any changes with respect to the previous year.

Other current assets amount to euros 17.3 million (euros 50.4 million at 31 December 2005) and mainly relate to the following:

- receivables from the Greek tax authorities for indirect taxes (VAT of euros 9.1 million) in relation to the activities carried out by Terna's branch in Greece;
- assets in relation to portions of costs for insurance premiums already paid but pertaining to the subsequent year (euros 1.6 million);

- other deferred costs (euros 2.2 million) mainly attributable to charges on contracts to use assets, which Terna took over following the transfer of plants from Enel Distribuzione;
- sundry advances to employees and third parties (euros 0.7 million).

17) INVENTORIES - euros 7.7 million

Inventories under current assets include materials and devices used in the operating, maintenance and construction of plants of euros 7.7 million (euros 7.2 million at 31 December 2005). The euros 0.5 million increase is mainly due to the ordinary maintenance requirements of plants.

18) TRADE RECEIVABLES - euros 1,163.7 million

Trade receivables are composed as follows:

In millions of euros	31.12.2006	31.12.2005	Change
Trade receivables			
- subsidiaries	1.7	0.4	1.3
- third parties	265.2	225.7	39.5
Energy-related receivables	896.8	759.6	137.2
TRADE RECEIVABLES	**1,163.7**	**985.7**	**178.0**

Trade receivables amount to euros 1,163.7 million, up euros 178.0 million on 2005. The increase is due to electrical energy transmission and dispatching activities carried out by Terna in 2006 (in 2005 these activities had an impact for only two months following the acquisition of the transmission and dispatching business activity from GSE SpA in November 2005).

Energy-related receivables are measured net of impairment losses relating to items considered uncollectible and recorded as an adjustment in the provision for bad debts (euros 13.1 million).

Trade receivables - euros 266.9 million

These mainly relate to the grid transmission consideration (euros 218.7 million) and related fees paid to the company for use of the National Transmission Grid by distributors (under article 17 of AEEG Resolution no. 5/04 and subsequent modifications) and producers (under article 19 of AEEG Resolution no. 5/04 and subsequent modifications) of electrical energy. In particular, under Resolution no. 5/04, the receivable mainly relates to the fee pertaining to the last two months of 2006, which was collected in full at the end of February 2007 (euros 185.0 million). The residual portion (euros 33.7 million) relates to the residual amount of the additional remuneration of 2005 paid under AEEG Resolution no. 162/06. It will be invoiced and collected by 31 July 2007.

Other trade receivables include receivables due from Italian customers (euros 39.5 million), Enel Group companies (euros 5.4 million) and receivables for contract work in progress (euros 1.8 million) relating to long-term work that the company is carrying out for third-party customers:

In millions of euros	Payments on account	Contract value	Balance at 31.12.2006	Payments on account	Contract value	Balance at 31.12.2005
Other	-6.1	7.9	1.8	-4.4	6.0	1.6
TOTAL	**-6.1**	**7.9**	**1.8**	**-4.4**	**6.0**	**1.6**

Energy-related receivables - euros 896.8 million

Energy items mainly include receivables in relation to energy in transit items arising on the dispatching of electrical energy and which do not create profits margins for the company. This caption also includes receivables for considerations payable by market operators for dispatching activities (DIS consideration as per AEEG Resolution no. 237/04) and metering activities (MIS consideration as per AEEG Resolution no. 05/04).

This caption also includes deferred charges of euros 62.6 million relating to the signing of ETSO-CBT (European Transmission System Operators - Cross Board Trade) agreements governing the offsetting of energy in transit costs on foreign electricity grids. Under Resolution no. 15/2005, the AEEG ensured the coverage of the above charges and established that repayment terms will be set out in a specific provision.

19) CASH AND CASH EQUIVALENTS - euros 36.1 million

At 31 December 2006, Terna SpA’s cash and cash equivalents amounted to euros 36.1, including bank current account deposits of euros 15.2 million (bearing interest at an average rate of 3.58%), euros 20.8 million in the intercompany current account held with the subsidiary RTM1 (bearing interest at an average rate of 3.39%) and euros 0.1 million in cash on hand for operating areas.

Liabilities

20) EQUITY - euros 1,901.7 million

Share capital - euros 440.0 million

The share capital of Terna SpA is comprised of 2,000,000,000 ordinary shares with a nominal value of euros 0.22 each.

Legal reserve - euros 88 million

The legal reserve is equal to 20% of the company's share capital.

Other reserves - euros 725.5 million

Other reserves underwent a net increase of euros 8.6 million, mainly as a result of the following:

fair value adjustment of derivatives hedging EIB loans - cash flow hedge derivatives, (up euros 11.6 million), net of the related tax effect (euros -3.8 million);

the recognition of the cost of stock options described below (up euros 0. 8 million).

Retained earnings - euros 398.4 million

Retained earnings mainly relate to the reserve as per the Vietti Law (euros 421.3 million), which was set up at 31 December 2004 and IFRS FTA reserves (euros -53.9 million). Changes of the year mainly relate to the allocation of the residual 2005 profits for the year (euros 5.6 million).

2006 interim dividend

After receiving the report of the auditors as per article 2433 bis of the Italian Civil Code, the company's Board of Directors, on 6 September 2006, approved the distribution of an interim dividend of euros 106 million, equal to 0.053 per share which was paid beginning from 23 November 2006.

The following table shows individual equity captions at the balance sheet date, indicating their origin, availability and possibility of distribution:

In millions of euros

Description	Amount	Possibility of use	Available portion
Share capital	440.0	-	-
Legal reserve	88.0	B	-
Other reserves:			
- equity-related	396.1	A,B,C	396.1
- income-related	329.4	A,B	329.4
Retained earnings	398.4	A,B,C	398.4
interim dividend	-106.0	-	-
Profits for 2006	355.8	-	-
Total	**1,901.7**		
		TOTAL	**1,123.9**
		Unavailable portion	710.4
		Residual available portion	413.5

Key: **A** - to increase share capital **B** - to cover losses **C** - to be distributed to shareholders

The unavailable portion is mainly related to income-related reserves and retained earnings not yet subject to taxation.

Stock option plans

On 21 December 2005, based on the proposals put forth by the Remuneration committee, the Board of Directors resolved to adopt a 2006 stock option plan for Terna managers who hold the most important roles in terms of achieving the company's strategic targets.

This plan is aimed at giving Terna - in line with international best practice and that of the leading publicly listed Italian companies - a management incentive and loyalty tool, capable of giving key resources a sense of corporate belonging, while ensuring they are constantly focused on creating value, so as to bring shareholders' and management's interests together.

The 2006 stock option plan may be analyzed as follows:

Regulation governing the 2006 stock option plan (Resolution dated 21 December 2005)

The plan provides for the distribution of a maximum of 10,000,000 options to approximately 20 Terna managers, who hold the most important roles in terms of achieving the company's strategic targets, including the CEO, as a senior manager of the company.

Under the approved regulation governing the stock option plan:

1. the strike price of each share shall be determined as the arithmetic mean of the reference prices of Terna ordinary shares as identified by the computer system of Borsa Italiana SpA in the period ranging between the date of the offer and the same day on the previous calendar month;
2. the exercise of the options and consequently, the right to subscribe newly-issued Terna ordinary shares depends on two performance parameters. In particular:
   (a) Terna EBITDA for the grant year (2006), must be greater than that shown in the budget approved by the Board of Directors;
   (b) the 2006 performance of each beneficiary must be positively assessed by the CEO, forecasting a 50% reduction in the options that the individual beneficiary can exercise, should this second condition not be met;
3. if the conditions underlying the exercise are met, individual beneficiaries can exercise their options by 31 March 2010 and up to the following maximum quantities:
   - up to 30% of exercisable options, beginning from the date disclosed in the notice communicating the fact that the conditions underlying the exercise have been met;
   - up to 60% of exercisable options, beginning from the first day of the first calendar year subsequent to the year in which the conditions underlying the exercise are met;
   - up to 100% of exercisable options, beginning from the first day of the second calendar year subsequent to the year in which the conditions underlying the exercise are met. Options can be exercised only when the stock exchange is open during the last 10 days of each month.

The 2006 stock option plan entailed the granting, on 21 December 2005, of 9,992,000 options with a strike price of euros 2.072, to 17 managers of the company. The Board of Directors will verify that the conditions for exercise are met when it approves the financial statements at 31 December 2006.

The options granted under this plan at 31 December 2006 are all outstanding and none may be exercised at that date.

	Plan 2006
Outstanding at 1 January	9,992,000
Granted during the year	-
Unopted during the year	9,992,000
Exercised during the year	-
Matured during the year	-
Outstanding at 31 December 2006	9,992,000
Exercisable at 31 December 2006	-

The table below shows the residual life of options at 31 December 2006 and their fair value:

	Options granted (at 21 December 2005)	End of vesting period	Fair value at grant date (in euros)
Plan 2006	2,997,600	2007	0.126
	2,997,600	2008	0.121
	3,996,800	2009	0.115
TOTAL	**9,992,000**		

* factor of probability (100%)

The Cox-Rubinstein pricing method is used, which considers the value of the Terna share at the grant date, the volatility of the share, the interest rate curve at the grant date and throughout the duration of the plan. The pricing parameters applied are the following:

- Closing price (underlying or spot price) of the share at the grant date (source: Bloomberg) of euros 2.058;
- Strike price of euros 2.072;
- Interest rate curve for the calculation of the discount factor at the grant date (source: Reuters);
- Historic volatility of the share recorded at the grant date (source: Bloomberg) of 14.860%.

The following table is provided in accordance with disclosure requirements for stock options granted to members of the Board of Directors, General Managers and Key Managers:

Name and Surname	Position	Number of options
Flavio Cattaneo	CEO	2,115,000

Other information on the stock option plan in place

Other beneficiaries of the stock option plan	7,877,000

In this respect, as indicated above, all the options relate to the 2006 plan, were held at the beginning of the year and are, at 31 December 2006, still outstanding. None may be exercised at that date.

21) LOANS

The following table details loans and financial liabilities recognized in Terna SpA's financial statements at 31 December 2006.

	CARRYING AMOUNT		
In millions of euros	31.12.2006	31.12.2005	Change
Bond	1,406.6	1,498.4	-91.8
Bank loans	540.9	370.5	170.4
Long-term loans	**1,947.5**	**1,868.9**	**78.6**
CFH derivatives	6.2	17.8	-11.6
Trading derivatives	0.0	11.2	-11.2
Non-current financial liabilities	**6.2**	**29.0**	**-22.8**
Short-term loans	50.0	55.0	-5.0
intercompany current account with subsidiaries	21.0	4.8	16.2
Current portion of long-term loans	29.5	29.5	0.0
Short-term loans and current portion of medium/longterm loans	**100.5**	**89.3**	**11.2**
TOTAL	**2,054.2**	**1,987.2**	**67.0**

The carrying amount of the bond has been measured by adjusting the amortized cost to reflect the change in the fair value of the risk hedged, between the date of inception of the hedge and the balance sheet date. Official Luxembourg stock exchange quotations for Terna bonds are as follows:

- bond maturing in 2024; price at 31/12/2006 103.56(*) and at 31/12/2005 109.68;
- bond maturing in 2014; price at 31/12/2006 99.77(*) and at 31/12/2005 105.43.

The carrying amount shown in the table is equal to the fair value of the financial liabilities recognized in the financial statements.

(*) Source: Bloomberg

Long-term loans

The following table shows the carrying amount of medium/long-term indebtedness and the repayment plan at 31 December 2006, broken down by loan type, including amounts falling due within one year.

In millions of euros	Maturity	31.12.2005	31.12.2006	Due within one year	Due after one year	2008	2009	2010	2011	After
Bonds	2014-2024	1,498.4	1,406.6	0.0	1,406.6	0.0	0.0	0.0	0.0	1,406.6
Total fixed rate		**1,498.4**	**1,406.6**	**0.0**	**1,406.6**	**0.0**	**0.0**	**0.0**	**0.0**	**1,406.6**
EIB no. 20271	2014	61.4	54.6	6.8	47.8	6.8	6.8	6.8	6.8	20.6
EIB no. 21159	2016	238.6	215.8	22.7	193.1	22.7	22.7	22.7	22.7	102.3
EIB no. 22947	2020	100.0	100.0	0.0	100.0	0.0	4.6	9.1	9.1	77.3
EIB no. 22947	2018	0.0	200.0	0.0	200.0	0.0	10.5	21.1	21.1	147.4
Total variable rate		**400.0**	**570.4**	**29.5**	**540.9**	**29.5**	**44.6**	**59.7**	**59.7**	**347.5**
TOTAL		**1,898.4**	**1,977.0**	**29.5**	**1,947.5**	**29.5**	**44.6**	**59.7**	**59.7**	**1,754.0**

Bonds are recognized at their fair value at 31 December 2006, calculated as described above. The repayment of nominal euros 1,400.00 million provides for the settlement of euros 600.00 million at 28 October 2014 and euros 800.00 million at 28 October 2024.

All other financial indebtedness items are stated at nominal value with the related repayment plan.

Terna SpA's total loans at 31 December 2006 amount to euros 1,977.0 million, including medium/long-term loans of euros 1,947.5 million.

The following table illustrates medium/long-term indebtedness, broken down by currency and average interest rate, including amounts due within one year.

In millions of euros	Maturity	Original currency	31.12.2006	Due within one year	Due after one year	Average interestrate at 31.12.2006
Bonds	2014-2024	euro	1,406.6	0.0	1,406.6	4.62%
Fixed rate			**1,406.6**	**0.0**	**1,406.6**	
EIB no. 20271	2014	euro	54.6	6.8	47.8	2.93%
EIB no. 21159	2016	euro	215.8	22.7	193.1	3.03%
EIB no. 22947	2020	euro	100.0	0.0	100.0	3.07%
EIB no. 22947	2018	euro	200.0	0.0	200.0	3.70%
Variable rate			**570.4**	**29.5**	**540.9**	
TOTAL			**1,977.0**	**29.5**	**1,947.5**	

Considering the implicit rate of hedges, the average interest rate on the bond is currently 3.6%. With respect to the two EIB loans, which are hedged against interest rate risk, considering the effect of cash flow hedge derivatives whose cost has been classified as current liabilities, the EIB no. 20271 loan has an average rate of 4.7%, while the EIB no. 21159 loan has an average rate of 4.4%.

The hedges in place to protect the company against the risk of fluctuations in interest rates ensure that the volatility of the cost of financial indebtedness remains limited.

The following table shows changes in medium and long/term indebtedness during the year:

In millions of euros

Type of debt	Notional debt at 31.12.05	Carrying amount at 31.12.05	Repayments and capitalizations	New issues	Exchange rate differences	Delta Fair Value 31.12.05 31.12.06	Notional debt at 31.12.06	Carrying amount at 31.12.06
Listed fixed rate bonds	1,400.0	1,498.4	0.0	0.0	0.0	(91.8)	1,400.0	1,406.6
Total bonds	**1,400.0**	**1,498.4**	**0.0**	**0.0**	**0.0**	**(91.8)**	**1,400.0**	**1,406.6**
Variable rate bank loans	400.0	400.0	(29.6)	200.0	0.0	0.0	570.4	570.4
Total bank loans	**400.0**	**400.0**	**(29.6)**	**200.0**	**0.0**	**0.0**	**570.4**	**570.4**
TOTAL FINANCIAL INDEBTEDNESS	**1,800.0**	**1,898.4**	**(29.6)**	**200.0**	**0.0**	**(91.8)**	**1,970.4**	**1,977.0**

Medium and long-term indebtedness shows a euros 78.6 million increase on 31 December 2005, due to the drop in the fair value of bonds (euros 91.8 million), the net increase in EIB loans (euros 170.4 million) (decrease of euros 29.6 million following the repayment of portions and increase of euros 200.0 million for new issues).

At 31 December 2006, Terna SpA has available credit lines of euros 1,569 million, including hot money of euros 819 million and the five-year revolving credit line of euros 750 million. The latter was renegotiated on 10 April 2006, and the amount, maturity and terms were redefined. The total amount of the credit line was increased from euros 500 million to euros 750 million through the extension of portions of the banking syndicate (Banca Intesa SpA, Banca Nazionale del Lavoro SpA, Banco Bilbao Vizcaya Argentaria SA, Capitalia Gruppo Bancario, Mediobanca - Banca di Credito Finanziario SpA, Monte dei Paschi di Siena SpA, Sanpaolo IMI SpA and Unicredit Banca Mobiliare SpA. Mediobanca - Banca di Credito Finanziario SpA and Banco Bilbao Vizcaya Argentaria SA are arrangers).

The maturity was postponed from 2009 to 2011, and Terna may request a further extension to 2013. The terms were also revised and, in particular, the importance of the rating was eliminated. Moreover, the spread on both the availed and unavailed portions of the credit were reduced from 17.5 to 15 base points and from 5.25 base points (30% of the margin of use) to 4 base points, respectively.

Furthermore, on 12 July 2006 the “Euro Medium Term Note Programme” (EMTN) was signed, for a total of euros 2 billion. The programme will enable Terna to benefit from the potential financial opportunities of international capital markets through the issue of bonds with various maturities in main world currencies.

Net financial indebtedness is detailed below:

In millions of euros	Carrying amount 31.12.2006
A) Cash and cash equivalents	15.3
B) Other cash and cash equivalents (details)	0.0
C) Cash and cash equivalents (A) + (B)	**15.3**
D) Short-term loan to Terna Part	0.5
E) Current financial receivables	**0.5**
F) Current bank debt	50.0
G) Current portion of long-term debt	29.5
H) Net intercompany current account balance with the RTL Group	0.2
I) Current financial indebtedness (F) + (G) + (H)	**79.7**
J) Net current financial indebtedness (I) - (E) - (D)	**63.9**
K) Non-current bank debt	540.9
L) Bonds	1406.6
M) Derivative financial instruments	-5.8
N) Non-current net financial indebtedness (K) + (L) + (M)	**1,941.7**
O) Net financial indebtedness (J) + (N)	**2,005.7**

The contractual clauses of loans in place at 31 December 2006 include negative pledges and default events in line with market standards (and, accordingly immaterial), while there are no financial covenants on existing debt.

Non-current financial liabilities

The table below provides the maturity and average interest rate of non-current financial liabilities:

In millions of euros	Maturity	31.12.06	31.12.05	Average interest rate
CFH derivatives	2014-2016	6.2	17.8	1.85%
Trading derivatives	2007-2008	-	11.2	0.36%
TOTAL		**6.2**	**29.0**	

Non-current financial liabilities include the fair value of fair cash flow hedge derivatives at 31 December 2006. Fair value is measured by discounting estimated future cash flows on the basis of the market interest rate curve at the reporting date. The fair value of cash flow hedge derivatives is recognized in the balance sheet under financial liabilities, with a balancing entry in a specific equity reserve. Accordingly, changes in the fair value of cash flow hedge derivatives have no impact on profits or losses. The rise in the interest rate curve generated a euros 11.6 million increase for cash flow hedge derivatives and euros 11.9 million change in trading derivatives, i.e. those derivatives that do not satisfy the requirements to be recognized hedging instruments and have an impact on the income statement. The latter increase was an increase in non-current financial assets of euros 0.7 million and a decrease in non-current financial liabilities of euros 11.2 million.

Short-term loans

To meet cash requirements, in December, two short-term credit lines were used for a total of euros 50 million. These credit lines were recognized when negotiated at an average interest rate of 3.81%.

On the basis of a treasury service agreement, Terna SpA funds and uses cash on behalf of its subsidiaries. The total of the intercompany current accounts is a debit balance totalling euros 21 million, detailed as follows:

In millions of euros	31.12.06	31.12.05	Difference
Current account			
RTL	18.8	4.8	14.0
RTM2	2.2	-	2.2
TOTAL	**21.0**	**4.8**	**16.2**

Current financial liabilities

Current financial liabilities arising on financial expenses accrued but not settled in relation to financial items are substantially unchanged with respect to 31 December 2005. The following table details deferred liabilities on the basis of the financial liabilities to which they relate:

In millions of euros	31.12.2006	31.12.2005	Change
Deferred liabilities on:			
Derivative contracts			
- hedging	0.2	0.6	-0.4
- trading	0.0	0.9	-0.9
Total	**0.2**	**1.5**	**-1.3**
Bond			
- ten-year	4.5	4.5	0.0
- twenty-year	7.0	7.0	0.0
Total	**11.5**	**11.5**	**0.0**
Loans	**2.3**	**1.4**	**0.9**
TOTAL	**14.1**	**14.4**	**-0.3**

22) TERMINATION BENEFITS AND OTHER EMPLOYEE-RELATED PROVISIONS euros 161.8 million

Terna offers its employees benefits during their employment with the Company (e.g., loyalty bonus), upon termination of employment (e.g., termination benefits, additional month's pay and indemnity for lack of notice) and after termination of employment (e.g., electricity discount and the ASEM health plan).

Employee benefits (loyalty bonus) are due to company employees hired under the national labour contract (including managers) upon the achievement of specific seniority requirements (25 and 35 years of service).

Termination benefits are due to all employees, managers hired or appointed before 28 February 1999 (indemnity for lack of notice), and employees (blue collars, white collars and junior managers) hired before 24 July 2001 under the national labour contract (additional month's pay).

Post-employment benefits consist of the following:

- discount on electrical energy consumed for domestic use. This benefit is offered to all company employees hired before 30 June 1996 under the national electrical energy sector labour contract. It is referred to as the electricity discount;
- health plan in addition to national healthcare, as provided for by the national industrial labour contract for managers (ASEM health plan).

The composition of and changes in termination benefits and other employee-related provisions at 31 December 2006 are detailed below:

In millions of euros	31.12.2005	Accruals	Interest cost	Utilization and other changes	31.12.2006
Employee benefits					
Loyalty bonus	3.9	-	0.2	-0.1	4.0
Total	**3.9**	**0.0**	**0.2**	**-0.1**	**4.0**
Termination benefits					
Termination benefits	74.6	9.0	2.9	-5.2	81.3
Additional month's pay	9.2	0.5	0.4	-3.1	7.0
Indemnity for lack of notice and other similar benefits	2.3	-	0.1	1.3	3.7
Total	**86.1**	**9.5**	**3.4**	**-7.0**	**92.0**
Post-employment benefits					
Electricity discount	63.0	1.1	2.5	-13.7	52.9
ASEM	15.2	0.3	0.6	-3.2	12.9
Total	**78.2**	**1.4**	**3.1**	**-16.9**	**65.8**
TOTAL	**168.2**	**10.9**	**6.7**	**-24.0**	**161.8**

This caption amounts to euros 161.8 million at 31 December 2006 (euros 168.2 million at 31 December 2005) and shows a net decrease of euros 6.4 million compared to the previous year. This change is mainly due to the combined effect of the net accruals of termination benefits (euros 6.7 million), net utilization, transfers and other changes in the electricity discount and ASEM made by the company (euros -12.4 million).

In millions of euros	Termin. ben.	Indemnity for lack of notice	Additional month's pay	Loyalty bonus	ASEM	Electricity discount	Indemnity Electricity discount	Total
31.12.2005	**74.6**	**2.1**	**9.2**	**3.9**	**15.2**	**63**	**0.2**	**168.2**
Cost	9.0	-0.1	0.5	0.0	0.3	1.1	0.0	10.9
Interest	2.9	0.1	0.4	0.2	0.6	2.5	0.0	6.7
(Gains)/Losses	5.3	1.5	-2.0	1.4	-3.1	-11.1	0.0	-8.0
Disbursements and transfers	-10.5	-0.1	-1.1	-1.5	-0.1	-2.6	0.0	-15.9
31.12.2006	**81.3**	**3.5**	**7.0**	**4.0**	**12.9**	**52.9**	**0.2**	**161.8**

The main assumptions made in the actuarial estimate of employee benefit obligations are the following:

	2006	2005
discount rate	4.25%	4.0%
rate of increase in personnel expenses	2.0% - 4.0%	2.0% - 4.0%
rate of increase in healthcare costs	3.0%	3.0%

23) PROVISIONS FOR CONTINGENCIES AND CHARGES - euros 54.3 million

The caption at 31 December 2006 and changes therein may be analyzed as follows:

In millions of euros	Provision for disputes and litigation	Provision for contingencies and other charges	Provision for leaving incentives	Total
BALANCE AT 31.12.2005	**13.8**	**12.3**	**9.6**	**35.7**
Accruals	0.4	19.9	4.1	24.4
Utilization	-1.0	-3.0	-1.8	-5.8
BALANCE AT 31.12.2006	**13.2**	**29.2**	**11.9**	**54.3**

Provision for litigation - euros 13.2 million

This provision is substantially in line with 2005. It is accrued mainly to cover year-end liabilities which could arise on lawsuits and out-of-court litigation relating to company activities. The amount accrued takes into account the opinions of the both internal and independent lawyers. Litigation for which a positive outcome is expected and those entailing a remote, potential charge are not provided for, nor are those for which no charges can be calculated. The latter are described under “off-balance sheet items”.

Provision for contingencies and charges - other - euros 29.2 million

This caption shows a net increase of euros 16.9 million on the previous year, due to accruals of euros 19.9 million and utilizations of euros 0.3 million, including:

- euros 1.6 million for the long-term incentive plan for managers not benefiting from the stock option plan;
- euros 5.6 million for “Urban and environmental redevelopment projects” to offset the environmental impact of the construction of long distance lines;
- euros 9.8 million, reflecting the estimated cost to be incurred by the company for additional INPS contributions;

Provision for leaving incentives - euros 11.9 million

This provision reflects the estimated non-recurring charges related to the agreed early termination of the working relationship of employees who are eligible for pension.

24) TAX LIABILITIES, INCLUDING DEFERRED - euros 453.5 million

Changes in this caption are detailed as follows:

		IMPACT RECOGNIZED IN PROFITS OR LOSSES			
In millions of euros	31.12.2005	Accruals	Utilization	Other changes	31.12.2006
Land related to buildings	3.8		-0.1		3.7
Employee benefits	0.1		-0.1	-1.7	-1.7
FVH derivatives and FV bond	1.3				1.3
Amortization and depreciation	456.9	5.7	-17.9		444.7
Difference in the fair value of former TSO properties	2				2
IRAP rate adjustment	0	3.5			3.5
TOTAL	**464.1**	**9.2**	**-18.1**	**-1.7**	**453.5**

Deferred tax liabilities decreased by euros 10.6 million on 31 December 2005, mainly due to the combined effect of the following events:

- utilization (euros 17.9 million) to absorb amortization/depreciation in excess of the deductible portion.

- Accruals made by the company (euros 5.7 million) mainly related to amortization/depreciation in addition to the rates of the year;
- adjustment (euros 3.5 million) of the IRAP rate (from 4.43% in 2005 to 4.72%) applied to provisions for deferred taxation, to better reflect the rates that will be applicable when the related temporary differences reverse.

25) OTHER NON-CURRENT LIABILITIES - euros 170.8 million

This caption amounts to euros 170.8 million at 31 December 2006 and includes deferrals for grants related to plants (euros 156.4 million at 31 December 2005), as well as grid transport consideration to cover future costs of the National Transmission Grid safety plan (euros 14.4 million). The decrease on the previous year (down euros 5.4 million) is mainly due to the release of portions of grants in connection with the depreciation of the year applicable to plants.

26) CURRENT LIABILITIES

Current liabilities at 31 December 2006 are detailed as follows:

In millions of euros	31.12.2006	31.12.2005	Change
Short-term loans (*)	71.0	59.8	11.2
Current portion of long-term loans (*)	29.5	29.5	-0.0
Trade payables	1,282.9	936.2	346.7
Tax liabilities	72.3	14.4	57.9
Current financial liabilities (*)	14.1	14.5	-0.4
Other current liabilities	106.8	97.8	9.0
TOTAL	**1,576.6**	**1,152.2**	**424.4**

(*) Reference should be made to the comments in note 21) LOANS.

Trade payables - euros 1,282.9 million

Trade payables at 31 December 2006 are detailed as follows:

In millions of euros	31.12.2006	31.12.2005	Change
Suppliers			
Suppliers:			
- non-energy related payables	219.4	184.8	34.6
- energy-related payables	1,046.9	747.2	299.7
Associates - Cesi	4.4	2.7	1.7
Subsidiaries	12.0	0.9	11.1
Payables for contract work in progress			
Payables for contract work in progress	0.2	0.6	-0.4
TOTAL	**1,282.9**	**936.2**	**346.7**

SUPPLIERS

Non-energy related payables

Amounts due to suppliers relate to invoices received and to be received for tenders, services and the purchase of materials and equipment.

The increase on 2005 (euros 34.6 million) is due to greater purchases and services in the last few months of the year as part of ordinary investing activities and operations.

The caption also includes amounts due for services provided to Enel Group companies (euros 28.7 million), which mainly include the following balances:

the euros 4.1 million due to Enel Distribuzione for invoices to be received for the electricity discount (discount on energy consumed for domestic use, which is given to all Company employees hired before 30 June 1996 under the national electricity sector labour contract);

the euros 24.0 million due to Enel Servizi for personnel administration, IT services, canteen services and security.

Energy-related payables

This caption includes the effects of amounts due for energy in transit on the balance sheet, mainly in connection with the purchase of energy and the transport consideration due to the owners of other portions of the National Transmission Grid. The increase (euros 299.7 million) on 2005 is mainly due to the operations of the TSO business activity for the last two months of 2005 only, and deferred payables relating to capacity payments (euros 84 million), UESS - basic units (euros 29.8 million), interconnection (euros 18.6 million), CCT returns (euros 59.1 million) whose allocation and/or coverage is yet to be defined by AEEG.

Associates

This caption amounts to euros 12 million and relates to payables for invoices received and to be received, mainly in relation to the grid transmission consideration due to the RTL Group for the portions of the National Transmission Grid that it owns. These include the following amounts, in particular:

- euros 1.2 million to RTL for the grid transmission consideration for September/December 2006;
- euros 7.3 million to RTM1 to remunerate the portion of the National Transmission Grid owned by RTM1 in the last two months of 2006;
- euros 3.5 million to RTM2 to remunerate the portion of the National Transmission Grid owned by RTM2 in the last three months of 2006.

The euros 11.1 million increase on the previous year is mainly due to the recognition of payables to RTM1 and RTM2, acquired from the subsidiary RTL in November 2006.

Associates

This caption amounts to euros 4.4 million and relates to payables to Cesi SpA for services provided to Terna in the construction and management of laboratories and plants for tests, inspections, studies and experimental research relating to the general electro-technical field and its technical and scientific progress. This caption totalled euros 2.7 million at 31 December 2005.

Commitments with suppliers for the 2007-2012 period amount to euros 1,116.8 million and relate to the as yet unpurchased portions of contractual purchase commitments pending at year end, which do not fall under normal operations.

PAYABLES FOR CONTRACT WORK IN PROGRESS

This caption amounts to euros 0.2 million at 31 December 2006, in line with 31 December 2005 and is composed as follows:

In millions of euros	Payments on account	Contract value	Balance at 31.12.2006	Payments on account	Contract value	Balance at 31.12.2005
Other	(2.1)	1.9	(0.2)	(5.3)	4.7	(0.6)
TOTAL	**(2.1)**	**1.9**	**(0.2)**	**(5.3)**	**4.7**	**(0.6)**

Tax liabilities - euros 72.3 million

This caption includes the company's taxes of the year (euros 194.7 million for IRES and euros 39.6 million for IRAP), net of payments on account in June and November 2006, totalling euros 162 million.

Other current liabilities - euros 106.8 million

Other current liabilities are detailed below:

In millions of euros	31.12.2006	Due within one year	Due after one year	31.12.2005	Change
Payments on account	19.7	0.7	19.0	25.2	-5.5
Other tax liabilities	43.8	43.8	-	7.7	36.1
Amounts payable to social security institutions	12.0	12.0	-	11.5	0.5
Amounts payable to employees	25.1	25.1	-	21.7	3.4
Others:					
- third parties	5.9	3.6	2.3	31.7	-25.8
- subsidiaries	0.3	0.3	-	0.1	0.2
TOTAL	**106.8**	**85.5**	**21.3**	**97.9**	**8.9**

PAYMENTS ON ACCOUNT

This caption includes grants related to plants collected by the company for non-current assets still under construction at 31 December 2006.

The net decrease of euros 5.5 million on 2005 (euros 25.2 million) is mainly due to the effect of the new contributions received from third parties for connections to the National Transmission Grid (euros 15.0 million) and the decrease (euros 20.5 million) in the contributions which directly reduce the carrying amount of the related assets, which became operational during the year.

OTHER TAX LIABILITIES

Other tax liabilities, which amount to euros 43.8 million, include euros 35.5 million, mainly for the settlement of VAT in December, substitute tax withholdings (euros 5.5 million) and registration tax on the agreement for the acquisition of the TSO business activity (euros 2.8 million).

The significant increase (euros 36.1 million) is mainly due to the decreased payable to the tax authorities in 2005, when the company had a VAT credit in relation to the previous year.

AMOUNTS PAYABLE TO SOCIAL SECURITY INSTITUTIONS

This caption amounts to euros 12.0 million, substantially in line with the previous year. It relates to the amounts payable to INPS for December 2006 and settled in January 2007. The caption also includes the contributions of the year relating to employees' incentives, to be paid in the following year, and the portion of the contributions arising from the renewal of employees' labour contract which was signed in July 2006.

AMOUNTS PAYABLE TO EMPLOYEES

Amounts payable to employees amount to euros 25.1 million (euros 21.7 million at 31 December 2005) and mainly relate to termination benefits due to employees whose employment was terminated before 31 December 2006 and amounts due for employees' leaving incentives to be paid in 2007. The euros 3.4 million increase is mainly due to increased payables (up euros 2.6 million) in 2006 for incentives on the company's results.

OTHER

This caption amounts to euros 6.2 million (euros 31.8 million at 31 December 2005) and mainly relates to the following:

- euros 2.3 million for guarantee deposits made in connection with the contractual obligations undertaken by electricity market operators with respect to dispatching contracts;
- euros 1.3 million for the amount due to ACEA SpA, partly being the portion of the incentive to unify the National Transmission Grid following the sale of the grid to the company (AEEG Resolution no. 73/06);
- euros 2.1 million for deferred liabilities of a sundry nature;
- euros 0.3 million in relation to the residual payable to the subsidiary Terna Participações for expenses (taxes and banking fees) on the IPO in the OTC market,

the euros 25.6 million decrease on 31 December 2005 is mainly due to the reclassification of energy items (euros 23.5 million), which arose in 2005 in conjunction with the acquisition of the TSO business activity, to "Trade payables".

E) COMMITMENTS AND CONTINGENCIES ARISING FROM OFF-BALANCE SHEET ITEMS

Environmental litigation

Environmental litigation relates to the installation and operating of electrical systems and, in particular, the effects of electric and magnetic fields.

The company was summoned in various civil and administrative cases in which requests were made for the transfer or change in operations of allegedly damaging electrical lines, even if installed in full compliance with current legislation to this regard. Only a very small number of cases include claims for compensation for damage to health due to electromagnetic fields.

The Prime Minister's Decree of 8 July 2003, which completed outline Law no. 36 of 22 February 2001, established the amounts of the three parameters (exposure limits, warning values and quality standards), provided for by law, with which electrical systems must comply. This decree had a favourable impact on the pending litigation, as until then, the scope of the outline law had been limited to general principles only.

In terms of the decisions taken to this regard, in only a few rare cases were judgments passed against the company. Moreover, these were appealed and the appeals are still pending. However, no claims of compensation for damage to health have been upheld.

Electric and magnetic field legislation

The outline law, passed on 22 February 2001, gives the government responsibility for establishing the reference parameters (exposure limits, warning values and quality standards) with which plants must comply under specific measures.

To this end, the outline law regarding reclamation provides for a recovery mechanism for reclamation costs, calculated by the Electrical Energy and Gas Regulator pursuant to Law no. 481/95, as these are expenses incurred in the public's interest.

On 29 August 2003, the Prime Minister's Decree of 8 July 2003 for the "Establishment of exposure limits, warning values and quality standards for the protection of the population from electric and magnetic fields at the grid frequency (50 Hz) used by long distance power lines", was published in the Official Journal of the Italian Republic. It established the amounts of the three parameters provided for by the outline law.

In terms of regional regulations, certain regions have proposed laws concerning this issue, with more restrictive limits than those provided for by the Prime Minister's Decree of 1992, and the more recent decree of 8 July 2003.

However, under judgement no. 307 of the Constitutional Court, passed down on 7 October 2003, certain regional laws regarding electromagnetic fields are anti-constitutional (including the Campania Region's law no. 13 of 24 November 2001), on the basis of the principle that the limits established by the government legislation cannot be waived, not even by regional legislation, as the protection of health must be ensured consistently throughout Italy.

GSE (formerly GRTN) business activity litigation

Under the provisions of article 1 of the Prime Minister's Decree of 11 May 2004 and the transfer agreement signed by Terna and GSE on 28 February 2005, the litigation following events that occurred up to the date of the transfer of, and in relation to, the GSE business activity relating to electrical energy transmission and dispatching activities ("business activity") was not transferred. Accordingly, the former GRTN (now GSE SpA) retains all liability, charges or liabilities to be incurred as a result or in connection with the litigation. As it holds the concession for transmission and dispatching activities since 1 November 2005, Terna was summoned in certain cases appealing AEEG's and/or MAP's measures relating to the above issue. Only in those cases in which the plaintiffs claim not only defects in the measures, but also Terna's alleged violation of the rules established by such Authorities, is the company called to appear in court.

Other litigation

In addition, cases relating to urban planning and environmental issues are pending, following the construction and operating of certain transmission lines. Any unfavourable outcome to these cases could have adverse effects for the company, which cannot be foreseen to date. Accordingly, no accruals have been made in this respect.

The outcome of a limited number of cases cannot be forecast as undoubtedly positive for the company, and the possible consequences could consist of compensation for damage, as well as incurring, *inter alia*, charges to change lines and suspend their use temporarily. In any case, any unfavourable outcome would not jeopardise line operations.

The above litigation has been examined, also considering the opinion of independent legal experts, and any negative outcome is considered remote.

INPS Memorandum no. 63 of 6 May 2005 provided that, with retroactive effect from 1999, government industrial companies and public bodies carrying out industrial, privatized activities, owed contributions to CIG, CIGS and DS, as well as amounts payable for redundancy, entailing charges of approximately euros 24.8 million. Given the complexity of this issue, Terna, along with other companies operating in the electrical energy sector, initially took legal recourse before an administrative law judge, claiming the measure be suspended and declared null and void. The judge claimed it was not that court's jurisdiction, since the issue concerned solely subjective rights. To date, Terna has taken its claims before the ordinary judicial authorities to claim that it has no obligation to pay the contributions. The hearing was set for 24 April 2007. However, INPS considered it necessary to request an opinion from the Council of State, and suspended payment of these contributions until it obtained such opinion.

On 8 February 2006, the Council of State found that the contributions should not be applied retroactively, and that the Memorandum should be duly integrated and corrected.

F) BUSINESS COMBINATIONS

There were no business combinations in 2006 other than the changes in controlling investments discussed above.

G) RELATED PARTY TRANSACTIONS

Related parties are identified in accordance with the provisions of IAS 24.

A party is related to the company if:

(a) it directly or indirectly, through one or more intermediaries:
- (I) controls the company, is controlled by the company, or is jointly controlled thereby (including parents, subsidiaries and associates);
- (II) it holds an investment in the company that gives it significant influence over that company;
- (III) it jointly controls the company;

(b) the party is an associate of the company;

(c) the party is a joint venture in which the company is an investor ;

(d) the party is a member of senior management with strategic duties of the company or its parent;

(e) the party is a close relative of one of the parties described in letters (a) or (d);

(f) the party is controlled, jointly controlled or under the significant influence of one of the parties described in letters (d) or (e), or those parties directly or indirectly hold a significant portion of voting shares;

(g) the party is a pension fund for the employees of the company, or any of its related parties.

A related party transaction occurs when there is a transfer of resources, services or obligations between related parties, regardless of whether a consideration is agreed.

Related party transactions carried out by the company during the year included those with its subsidiaries, the associate Cesi SpA and the employee pension funds FONDENEL and FOPEN.

Transactions carried out by Terna with the subsidiaries of RTL SpA relate to the following:

- a lease payment due from the company, as manager of the National Transmission Grid, to use a portion of the grid owned by the subsidiaries;
- the management and coordination of all transactions relating to the administration of financial resources and cash requirements, as well as treasury services and all other related transactions (i.e., treasury agreements);
- services for ordinary operating and maintenance activities on the high-voltage lines owned by the subsidiaries to keep the plants efficient;
- an assistance and consultancy agreement for administrative, financial, legal/corporate and tax issues, as well as strategies and business coordination, specifically with RTL (i.e., a management fee agreement).

In particular, agreements with Cesi SpA in which Terna is the customer mainly relate to services and technical consultancy, studies and research, design and trials carried out on behalf of Terna. Other agreements mainly relate to the lease of laboratories and other similar structures for specific use.

Transactions with the Brazilian subsidiaries are mainly financial and relate to the dividends paid to the company during the year. In addition, transactions with Terna Participações include the financing agreement signed with Terna in June and repaid on 20 February 2007.

FONDENEL and FOPEN are pension funds in which the company’s employees participate for complementary pensions. The related transactions with an impact on the company’s balance sheet and income statement involve contributions incurred by the company, which are calculated and paid on a monthly basis.

The following table provides total costs and revenues of the year and receivables and payables at year end in millions of euros.

COMPANY	INCOME STATEMENT BALANCES			BALANCE SHEET BALANCES		
In millions of euros	Revenues	Expenses of the year	Investment expenses	Receivables	Payables	Guarantees
RTL Group:						
- RTL SpA	2.5	6.5*	-	0.4	20.0	
- RTM1 SpA	0.5	3.1*	-	21.3	7.3	
- RTM2 SpA	-	1.1*	-	0.8	5.7	
Brazilian companies:						
- Terna Participações SA	9.7	-	-	0.5	0.3	
- Novatrans Energia SA	10.4	-	-	-	-	
- Trasmissora Nordeste Sudeste SA	19.1	-	-	-	-	
Cesi SpA	0.1	0.9	7.6	-	4.4	2.0
Fondenel	-	0.4	-	-	-	
Fopen	-	1.3	-	-	0.7	
TOTAL	**42.3**	**13.3**	**7.6**	**23.0**	**38.4**	**2.0**

* Including a total of euros 10.5 million in relation to items in transit.

Guarantees relate to sureties received on contracts.

H) SIGNIFICANT NON-RECURRING TRANSACTIONS AND EVENTS AND ATYPICAL OR UNUSUAL TRANSACTIONS

With the exception of those discussed above, no significant, non-recurring, atypical or unusual transactions were carried out during the year.

I) NOTES TO THE CASH FLOW STATEMENT

The cash flows generated by operating activities during the year amounted to approximately euros 756.2 million and include operating activities before the changes in net working capital (euros 777.3 million) and cash flows used by the change in working capital (approximately euros 21.0 million).

Investing activities in property, plant and equipment and intangible assets also used net financial resources of approximately euros 327.5 million, while investments in companies used euros 415.9 million. In particular, these outflows related to the acquisition of AEM Trasmissione SpA and Edison Rete SpA through the subsidiary RTL (euros 416.8 million), net of the proceeds from the sale of a portion of the investment in the Brazilian subsidiary Terna Participações, through its IPO on the São Paulo stock exchange (euros 82.7 million). Cash outflows for self-financing were mainly due to the distribution of dividends in 2005 (euros 160 million) and the interim dividend for 2006 (euros 106 million), while medium/long-term financial indebtedness, net of the related fair value hedges, increased by approximately euros 173.4 million.

Cash flows generated by these transactions amounted to approximately euros 4.2 million.

L) SUBSEQUENT EVENTS

2007-2011 business plan

On 31 January 2007, Terna presented financial analysts with its 2007-2011 business plan, approved by the company's Board of Directors.

The Terna Group's 2007-2011 business plan focuses on three main guidelines:

- Development of the National Transmission Grid (RTN): the investment plan provides for total expenditure of euros 2.7 billion from 2007 to 2011, with a 35% increase on the previous plan. Development investments account for 80% of total investments, up from euros 1.4 billion to euros 2.2 billion;
- Cost cutting with an increase in profits margins: in particular, by rationalizing costs for regulated in Italy. The plan provides for a reduction of approximately euros 60 million in total Terna Group costs in the years covered on a like-for-like basis;
- Guaranteed high security of the electrical system and reliability of the National Transmission Grid with average service interruption times of less than 1 minute/year and grid availability of over 99%.

Credit rating confirmation

On 31 January 2007, Standard & Poor's Ratings Services confirmed its ratings for Terna SpA, following the Italian utility company's presentation of its 2007-2011 business plan: long-term rating of AA- and short-term rating of 'A-1+ with a stable outlook.

New dispatching and conduction organization

The new organizational structure for the Dispatching and Conduction Department was implemented on 1 March 2007, to complement the work performed on processes following the acquisition of the GSE SpA (formerly GRTN) business activity. This new structure enables process-based management, while ensuring that operating and strategic objectives are aligned, preventing the scattering of similar activities within the same process to more than one unit. In addition, a portion of the resources formerly under the Systems and Technology Department (which is now the Technology and Management Systems Department), has come under the Technologies and Process Systems Function reporting to the Dispatching and Conduction Department.
Similarly, work groups have begun identifying further measures to take to optimize in detail the processes related to real time management.

Fibre optics

On 4 April 2007, an agreement was signed with the Wind Telecomunicazioni Group to acquire the exclusive right to use optical fibre pairs owned by the Wind Group for 20 years. The pairs run for a total length of approximately 11,000 km throughout all of Italy.
The agreement amounts to euros 43.5 million.
The data transmission infrastructure is a crucial element of the security and efficiency of control, conduction and protection processes for the high voltage grid, as it makes it possible to improve grid supervision and carry out work on Terna plants, while allowing the development of advanced solutions to protect the electricity system.
This transaction will enable Terna to further boost the security of the system and is included in the investments provided for by the 2007-2011 business plan.

Merger of RTM1 and RTM2 into RTL

On 18 April 2007, the shareholders of Rete di Trasmissione Locale Società per Azioni (RTL), “Rete Trasmissione Milano 1 Società per Azioni” (RTM1) and “Rete Trasmissione Milano 2 Società per Azioni” (RTM2) met and approved the plan for the merger of RTM1 and RTM2 into RTL, on the basis of the companies’ financial statements as of and for the year ended 31 December 2006, with the cancellation of all shares of RTM1 and RTM2, in accordance with the methods set out in the plan and, accordingly, without RTL increasing its share capital or provided for a share exchange ratio or cash consideration.
The merger will take effect from the date of registration of the merger deed with the company registrar, or a subsequent date indicated in the merger deed.
Pursuant to point 6), article 2501-*ter* of the Italian Civil Code, referred to by article 2504 *bis* of the Italian Civil Code and paragraph 9, article 172 of Presidential Decree no. 917 of 22 December 1986, the transactions carried out by companies to be merged will be recognized in the financial statements of the merging company and the merger will take effect for accounting and tax purposes from midnight on the first day of the year in which the merger takes effect.
In particular, the purpose of the transaction is to improve the Terna Group companies’ operations, by expanding synergies through a Group reorganization in order to streamline the investment chain and pursue increased management efficiency, while reducing administrative costs. To this end, all companies in the same sector will be merged together.

Acquisition of AEM Trasporto Energia Srl Torino

On 20 April 2007, through RTL, the Terna Group signed an agreement with Iride Energia to acquire 100% of AEM Trasporto Energia Srl (“AEM TE”) and the 220-kV electrical substation in Moncalieri (Turin), which is part of the National Transmission Grid (“RTN”).

The consideration totalled euros 49.4 million, including euros 38.8 million to acquire the 100% investment in AEM TE, euros 2.8 million for the company’s net financial position at 31 December 2006 and euros 10.6 million to acquire the Moncalieri (Turin) substation. The acquisition agreement provides for an adjustment to the consideration in relation to the change in AEM TE’s equity between 31 December 2006 and the date the transaction is concluded.

AEM TE owns approximately 220 km of triads and four electrical substations in Piedmont, which are part of the National Transmission Grid (Martinetto, Rosone, Sud Ovest and Villa).

At 31 December 2006, AEM TE reported revenues of euros 7.6 million, EBITDA of euros 4.3 million and a profits for the year of euros 1.7 million. Net invested capital amounted to approximately euros 25.7 million, including property, plant and equipment totalling roughly euros 27.1 million. Equity amounted to around euros 28.6 million.

The transaction is subject to authorization from the Anti-Trust Authority before it can be concluded.

Control of Terna SpA held by Cassa Depositi e Prestiti

On 19 April 2007, Cassa Depositi e Prestiti SpA, which owns 29.99% of Terna SpA, notified the company that it had verified that it controlled Terna SpA. This assessment was based on the following elements:

- the composition and breakdown of the shareholding structure;
- events at particularly significant shareholders' meetings;
- the composition of the Board of Directors.

M) TRANSITION TO INTERNATIONAL FINANCIAL REPORTING STANDARDS (IFRS)

Introduction

Following Legislative Decree no. 38 of 28 February 2005, exercising the power granted by EEC regulation no. 1606/2002, from 2006, companies with shares traded on regulated markets in the member states of the European Union are required to prepare their separate financial statements in accordance with the International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board and endorsed by the European Commission ("IFRS").

Accordingly, Terna SpA has adopted IFRS from 2006. Its date of transition is 1 January 2005.

The last set of separate financial statements prepared in accordance with Italian GAAP is those as of and for the year ended 31 December 2005.

In this document, figures showing the effects of transition to IFRS in the reconciliation schedules required by IFRS 1, previously approved and published along with the Terna Group's consolidated half year report at 30 June 2006, have been reclassified and integrated. However, there were no changes to the effects of transition on equity at 31 December 2005 or the income statement for 2005.

The most significant accounting policies and measurement criteria applied in the preparation of the reconciliation schedules are those described in the notes to the financial statements as of and for the year ended 31 December 2006.

IFRS-compliant balance sheets as of 1 January 2005 and 31 December 2005
IFRS-compliant income statement for the year ended 31 December 2005

The balance sheets as of 1 January 2005 and 31 December 2005 and the income statement for the year ended 31 December 2005 are provided below, showing:

- Italian GAAP figures reclassified under IFRS;
- IFRS adjustments.

The functional currency used for the schedules is the Euro, and all figures are shown in euros.

RECONCILIATION OF EQUITY AT 1 JANUARY 2005

In millions of euros	Note	Italian GAAP	Effects of IFRS_IAS	IFRS_IAS
Non-current assets				
Property, plant and equipment	1	3,848,337,763	9,741,655	3,858,079,418
Deferred tax assets	2	14,837,169	36,813,758	51,650,927
Financial assets and other assets	3	311,772,738	41,971,419	353,744,157
Total non-current assets		**4,174,947,670**	**88,526,832**	**4,263,474,502**
Current assets				
Inventories		10,039,942		10,039,942
Trade receivables	4	141,742,596	543,049	142,285,645
Current financial assets		4,559,594		4,559,594
Cash and cash equivalents		144,008,296		144,008,296
Other current assets		42,260,393		42,260,393
Total current assets		**342,610,821**	**543,049**	**343,153,870**
Total assets		**4,517,558,491**	**89,069,881**	**4,606,628,372**
Loans	5	1,711,143,061	23,636,488	1,734,779,549
Termination benefits and other employee-related provisions	6	61,141,826	77,170,152	138,311,978
Provisions for contingencies and charges		40,090,796		40,090,796
Deferred tax liabilities	7	463,968,279	4,653,790	468,622,069
Non-current financial liabilities	8		31,466,262	31,466,262
Non-current liabilities		158,206,431		158,206,431
Total non-current liabilities		**2,434,550,393**	**136,926,692**	**2,571,477,085**
Current portion of long-term loans	9		18,184,650	18,184,650
Trade payables	10	177,369,586	543,049	177,912,635
Tax liabilities		12,087,213		12,087,213
Current financial liabilities		12,940,435		12,940,435
Other liabilities		42,649,296		42,649,296
Total current liabilities		**245,046,530**	**18,727,699**	**263,774,229**
Total liabilities		**2,679,596,923**	**155,654,391**	**2,835,251,314**
Share capital		440,000,000		440,000,000
Other reserves		813,174,696		813,174,696
Retained earnings	17	584,786,872	-66,584,510	518,202,362
Total equity		**1,837,961,568**	**-66,584,510**	**1,771,377,058**
TOTAL LIABILITIES AND EQUITY		**4,517,558,491**	**89,069,881**	**4,606,628,372**

RECONCILIATION OF EQUITY AT 31 DECEMBER 2005

In millions of euros	Note	Italian GAAP	Effects of IFRS_FTA	IFRS
Non-current assets				
Property, plant and equipment	1	4,004,990,509	15,367,500	4,020,358,009
Intangible assets		151,489,122		151,489,122
Deferred tax assets	2	12,105,321	39,646,624	51,751,945
Financial assets and other assets	3	296,149,846	108,914,609	405,064,455
Total non-current assets		**4,464,734,798**	**163,928,733**	**4,628,663,531**
Current assets				
Inventories		7,175,172		7,175,172
Trade receivables	4	985,033,523	635,134	985,668,657
Current financial assets		4,420,462		4,420,462
Cash and cash equivalents		15,791,228		15,791,228
Other current assets		50,410,630		50,410,630
Total current assets		**1,062,831,015**	**635,134**	**1,063,466,149**
Total assets		**5,527,565,813**	**164,563,867**	**5,692,129,680**
Non-current liabilities				
Loans	5	1,793,392,734	75,520,107	1,868,912,841
Termination benefits and other employee-related provisions	6	77,446,834	90,697,694	168,144,528
Provisions for contingencies and charges		35,675,117		35,675,117
Deferred tax liabilities	7	456,849,516	7,245,377	464,094,893
Non-current financial liabilities	8		29,047,521	29,047,521
Non-current liabilities		176,191,033		176,191,033
Total non-current liabilities		**2,539,555,234**	**202,510,699**	**2,742,065,933**
Current liabilities				
Current portion of long-term loans	9		29,540,000	29,540,000
Trade payables	10	935,521,378	635,134	936,156,512
Tax liabilities		14,387,553		14,387,553
Current financial liabilities		74,313,226		74,313,226
Other liabilities		97,782,420		97,782,420
Total current liabilities		**1,122,004,577**	**30,175,134**	**1,152,179,711**
Total liabilities		**3,661,559,811**	**232,685,833**	**3,894,245,644**
Share capital		440,000,000		440,000,000
Other reserves		816,683,476	-11,777,462	804,906,014
Retained earnings		441,278,092	-53,915,683	387,362,409
Profits for the year, net of interim dividends		168,044,434	-2,428,821	165,615,613
Total equity	**17**	**1,866,006,002**	**-68,121,966**	**1,797,884,036**
TOTAL LIABILITIES AND EQUITY		**5,527,565,813**	**164,563,867**	**5,692,129,680**

Reconciliation of profits for 2005

in euros	Italian GAAP	Effects of IFRS_FTA	IFRS
Revenues	887,800,824		887,800,824
Other revenues	22,335,615	142,177	22,477,792
Total revenues	**910,136,439**	**142,177**	**910,278,616**
Raw materials	23,883,919,8	0,0	23,883,920
Services	106,665,629,5	0,0	106,665,630
Personnel expenses	193,217,619,9	5,412,942,3	198,630,562
Amortization, depreciation and impairment losses	157,490,500,0	-387,695,9	157,102,804
Other operating expenses	22,195,841,5	-2,283,505,0	19,912,335
Capitalized expenses	-26,460,510,3	0,0	-26,460,510
Total expenses	**476,993,000**	**2,741,741**	**479,734,741**
Operating profits	**433,143,439**	**-2,599,564**	**430,543,875**
Financial income	52,521,450		52,521,450
Financial expenses	62,420,823	841,302	63,262,125
PROFITS BEFORE TAXES	**423,244,066**	**-3,440,866**	**419,803,200**
Income taxes	155,199,631	-1,012,044	154,187,587
PROFITS FOR THE YEAR	**268,044,435**	**-2,428,821**	**265,615,613**

Notes to the main IFRS adjustments made to the balance sheet captions as of 1 January 2005 and 31 December 2005

The main adjustments to the individual balance sheet figures as of 1 January 2005 and 31 December 2005 are discussed below.

BALANCE SHEET - ASSETS

1) PROPERTY, PLANT AND EQUIPMENT

euros 9.7 million at 1 January 2005 and euros 15.4 million at 31 December 2005

These adjustments relate to the reinstatement of the carrying amount of land relating to electrical stations at their historic cost, through the reversal of the related accumulated depreciation. These adjustments are based on the assumption that land has an indefinite useful life and, accordingly, is not subject to depreciation. In 2005, the adjustment is also due to the fair value adjustment of TSO business activity properties acquired from GRTN, for a total of euros 5.2 million.

2) DEFERRED TAX ASSETS

euros 36.8 million at 1 January 2005 and euros 39.6 million at 31 December 2005

These amounts reflect the balancing entry in balance sheet assets of the tax effect on adjustments mainly in relation to post employment benefits (euros 26.5 million at 1 January 2005 and euros 30.1 million at 31 December 2005), cash flow hedges (euros 6.2 million at 1 January 2005 and euros 5.8 million at 31 December 2005) and trading derivatives (euros 4.1 million at 1 January 2005 and euros 3.7 million at 31 December 2005).

3) FINANCIAL ASSETS AND OTHER ASSETS

euros 42.0 million at 1 January 2005 and euros 108.9 million at 31 December 2005

These relate to the recognition of derivatives in portfolio for fair value hedges on the Terna bonds in the balance sheet at fair value.

4) TRADE RECEIVABLES

euros 0.5 million at 1 January 2005 and euros 0.6 million at 31 December 2005

These reflect the restatement of the net receivable for contract work in progress for third parties, in the periods considered, under contract with Terna.
These amounts have balancing entries in trade payables.

BALANCE SHEET - LIABILITIES

5) LOANS

euros 41.8 million at 1 January 2005 and euros 105.0 million at 31 December 2005

This adjustment reflects the fair value adjustment of the hedged portion of Terna bonds. The net balance of the adjustment also includes the reclassification of the current portion of loans to current liabilities (euros -18.2 million at 1 January 2005 and euros -29.5 million at 31 December 2005).

6) TERMINATION BENEFITS AND OTHER EMPLOYEE-RELATED PROVISIONS
euros 77.2 million at 1 January 2005 and euros 90.7 million at 31 December 2005

These adjustments are summarized as follows:

In millions of euros	01.01.2005	31.12.2005
Termination benefits	-2,920,427	-1,215,825
Provision for the electricity discount	53,213,000	63,004,381
Other provisions	26,877,579	28,909,138
TOTAL	**77,170,152**	**90,697,694**

These mainly relate to the application of actuarial calculations to termination benefits and the recognition of the actuarially-based present value of obligations for post-employment defined-benefit plans.

7) DEFERRED TAX LIABILITIES
euros 4.6 million at 1 January 2005 and euros 7.2 million at 31 December 2005

These reflect the balancing entry in liabilities of the tax effect on adjustments made mainly for termination benefits and the reversal of accumulated depreciation of land.

8) NON-CURRENT FINANCIAL LIABILITIES
euros 31.5 million at 1 January 2005 and euros 29.0 million at 31 December 2005

These relate to the recognition of financial derivatives in portfolio at their fair value in the balance sheet at 1 January 2005 (CFH on EIB loans: euros 18.9 million; trading derivatives: euros 12.6 million) and 31 December 2005 (CFH on EIB loans: euros 17.8 million; trading derivatives: euros 11.2 million).

9) CURRENT PORTION OF LONG-TERM LOANS
euros 18.2 million at 1 January 2005 and euros 29.5 million at 31 December 2005

These reflect the reclassification of the current portion of long-term loans.

10) TRADE PAYABLES
euros 0.5 million at 1 January 2005 and euros 0.6 million at 31 December 2005

These reflect the restatement of the net payable for contract work in progress for third parties. These amounts have balancing entries in trade payables.

2005 INCOME STATEMENT ADJUSTMENTS

11) OTHER REVENUES - euros 0.1 million

This adjustment is due to the transfer of the TSO business activity from GRTN to Terna, and the excess fair value of the assets and liabilities acquired by the company with respect to the acquisition price paid for the business activity.

12) PERSONNEL EXPENSES - euros 5.4 million

This relates to the adjustment of provisions to the present value (actuarial) of obligations for post employment defined benefit plans. The adjustment of the period is due to higher costs recognized.

13) AMORTIZATION, DEPRECIATION AND IMPAIRMENT LOSSES - euros -0.4 million

This adjustment is mainly due to the reversal of the depreciation of the period in relation to land.

14) OTHER OPERATING EXPENSES - euros -2.3 million

This mainly relates to the reversal of costs of the electricity discount granted to retired former employees, recalculated using actuarial techniques and recognized under personnel expenses.

15) NET FINANCIAL EXPENSES - euros 0.8 million

The adjustment mainly includes:

- the financial component of the discounting of employee benefits (euros 5.9 million);
- the net effect on profits or losses of financial expenses (euros 62.0 million) and income (euros 67.1 million) on derivative financial instruments (hedging and trading) in portfolio at 31 December 2005.

16) INCOME TAXES - euros -1.0 million

This amount reflects the tax effects of adjustments on income statement captions, as detailed below:

TAX EFFECT OF IFRS ADJUSTMENTS

In millions of euros	2005
Termination benefits and other employee related provisions	-2,817,960
Separation of land from buildings	144,327
Derivatives	1,661,589
TOTAL TAX EFFECT	**-1,012,044**

17) RECONCILIATION OF EQUITY

The following reconciliation of equity at 1 January 2005 and 31 December 2005 and the profits for 2005, along with notes to the adjustments made to balances determined under Italian GAAP is provided to integrate the above reconciliation schedules of the balance sheets and income statement.

In millions of euros	Note	Equity at 01.01.2005	Equity at 31.12.2005	2005 income statement
ITALIAN GAAP		**1,837,961,568**	**1,866,006,002**	**268,044,434**
property, plant and equipment and related depreciation	a	9,741,655	15,367,500	528,388
employee benefits	b	-77,170,152	-90,697,694	-8,841,861
stock option plans	c	-	-	-162,510
derivative financial instruments	d	-31,315,981	-25,193,019	5,035,118
tax effect of IFRS adjustments	e	32,159,968	32,401,247	1,012,044
Total		**-66,584,510**	**-68,121,966**	**-2,428,821**
IFRS		**1,771,377,058**	**1,797,884,036**	**265,615,613**

a) Property, plant and equipment and related depreciation

IFRS provide that the caption “Land” be classified separately from other assets and not depreciated. Land relating to buildings, which was previously depreciated together with the asset built upon it, has been separated from those assets and the related depreciation has been eliminated, with a positive effect on equity at 1 January 2005 and 31 December 2005, totalling approximately euro 9.7 million and euro 15.4 million, respectively.

b) Employee benefits

IFRS identify post-employment benefits as a type of employee benefits. These are the benefits due to employees after termination of employment. In defined benefit plans, actuarial risk (the risk that benefits will be less than expected) and investment risk (the risk that the invested assets will be insufficient to meet expected benefits) fall on the company instead of the employee. Accordingly, the present value of the expected liability and related costs and income, including financial expenses and actuarial gains and losses is recognized. Terna’s defined benefit plans, which include termination benefits, additional month’s pay, indemnity for lack of notice, loyalty bonus and the electricity discount, have been remeasured and recognized as follows:

- electricity discount liability;
- loyalty bonus liability.

In compliance with the measurement methods for:

- termination benefits;
- provision for the additional month’s pay and indemnity for lack of notice.

The above adjustments have had a negative effect on equity at 1 January 2005 and 31 December 2005 of approximately euros 77.2 million and euros 90.7 million, respectively. They have also had a negative impact of euros 8.8 million on the 2005 income statement.

c) Stock option plans

Unlike Italian GAAP, IFRS require that the company recognize share-based payments to employees over the vesting period, on the basis of the fair value at the grant date. Recognition of fair value should be a balancing entry to a specific equity reserve. Accordingly, the total effect on equity is nil. The effect on profits and losses (personnel expenses) for 2005 amounts to euros 0.2 million for plans set up by the company.

d) Derivative financial instruments

The company agrees derivative contracts to hedge the risk of fluctuations in interest and exchange rates, for both specific transactions and overall exposure. IFRS provide for specific rules for the recognition of these derivatives, which vary from those set forth by Italian GAAP.

In particular, the main impact of derivatives that hedge fluctuations in projected future cash flows related to an asset, liability or future transaction (cash flow hedges, "CFH"), is the following:

- the recognition of the fair value of the derivative asset/liability in the balance sheet;
- the recognition of the effective portion of the hedge in the reserve for cash flows hedges;
- the recognition of the ineffective portion of the hedge in profits or losses.

The main impact of derivatives that hedge fluctuations in the fair value of the hedged item, consisting of an asset or liability recognized in the balance sheet (fair value hedge on interest rates), is the following:

- the recognition of the derivative asset/liability in the balance sheet at its fair value;
- the recognition of the difference in the fair value of the hedged risk as an adjustment to the hedged item.

Lastly, derivatives that do not qualify for hedge accounting under IFRS are measured at fair value and the related effects are taken directly to profits or losses.

This accounting treatment has had a negative effect on equity at 1 January 2005 and 31 December 2005 of euros 31.3 million and euros 25.2 million, respectively.

e) Tax effect of IFRS adjustments

This is due to the tax effects of adjustments to income statement balance sheet captions, with a positive impact on equity at 1 January 2005 and 31 December 2005 of euros 32.2 million and euros 32.4 million, respectively.

Effects on the 2005 cash flow statement

The reconciliation of the cash flow statement is not provided, since the effects of IFRS adoption have not had a significant impact.

The following table reconciles net financial indebtedness at 31 December 2005 under Italian GAAP with that under IFRS.

In millions of euros	31.12.2005
NET FINANCIAL INDEBTEDNESS - ITALIAN GAAP	**1,840,281,740**
Application of amortized cost to Terna bonds	6,638,331
Difference in the fair value of bonds hedged by fair value hedges	-10,492,833
Difference in the fair value of cash flow hedge derivatives	17,820,855
Difference in the fair value of trading derivatives	11,226,666
NET FINANCIAL INDEBTEDNESS - IFRS	**1,865,474,759**

The net difference reflects a euros 25.2 million increase in financial indebtedness, mainly due to the effect of hedges on variable rate loans and derivatives not eligible for hedge accounting under IFRS. The net decrease of euros 10.5 million in bonds relates to the fair value adjustment of such loans (euros 98.4 million) and the recognition of the related fair value hedges (euros -108.9 million). The application of amortized cost includes discounts and transaction costs that are directly attributable to bonds issued by the parent, which are no longer recognized separately, as was provided for under Italian GAAP.

REPORTS

REPORT OF THE BOARD OF STATUTORY AUDITORS TO THE SHAREHOLDERS' MEETING 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 S.p.A ("TERNA", "Company"),

Shareholders,

pursuant to Article 153 of Legislative Decree 58/98, we inform you on our activity, specifying that during the year that ended on December 31, 2006, we performed the supervisory activity required by the law, according to 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 about the activities carried out and about the most significant economic, financial and equity transactions of the Company, and we were satisfied that the resolutions were not only implemented but were also in compliance with law provisions and the Bylaws and were not manifestly imprudent, risky, representing a potential conflict of interest or in contrast with the resolutions passed by the Shareholders' Meeting;
- we gathered information and monitored, as far as our authority allowed, the organizational structure, noting the adequacy of such structure also in view of the modifications that were made following the integration process of the activities acquired (transmission and dispatching) with the TSO business segment (Transmission System Operator);
- we monitored the administrative and accounting system, assessing the reliability of the latter in providing a true and fair view of operations and we also monitored compliance with sound management practices. These activities were carried out both through direct observations and through information collected from the management;
- pursuant to Article 150 of Legislative Decree 58/98, we held meetings with the Independent Auditors

for the purpose of mutually exchanging data and information. During the various meetings, no facts worthy to be mentioned in this Report emerged;

- we assessed and monitored the existing internal control activity through information received from the management. No facts worthy to be mentioned in this Report emerged thus proving the adequacy of the existing control system;
- we monitored the updating and implementation of the law on administrative responsibility of legal persons pursuant to Legislative Decree 231/01;
- we monitored the adequacy of provisions issued by the holding company for its subsidiaries with regard to the communication obligations in compliance with the law;
- we verified, through direct inspections and through information obtained from the Independent Auditors, compliance with the provisions of law regarding the drawing up of the financial statement, with a particular focus on the formats adopted, contents and accounting principles applied. We verified the completeness of the Director's Report prepared according to Article 2428 of the Civil Code and its adequacy in providing information regarding transactions with related parties and atypical and/or unusual transactions carried out in 2006.

The only other aspects regarding the financial statement that the Board of Statutory Auditors deems relevant are the following:

- the increased value of the equity investment in the subsidiary RTL S.p.A., consequent to the contribution of capital, aiming at the acquisition of AEM Transmissione S.p.A. and Edison Rete S.p.A.;
- the increased revenue regarding the remuneration of the electricity grid both owing to the increased new tariffs and to the greater quantity of electricity transported;
- the capital gain obtained with the transfer, through an IPO, of 17,4% of shares owned in Terna Participações.

With regard to the Report of the Independent Auditors concerning the 2006 Financial Statement, no significant facts have emerged.

During the monitoring activities described above, and on the basis of information obtained from the

Independent Auditors and from TERNA executives, no omissions, reproachable facts, or irregularities were found that required reporting to the control bodies or that were worthy to be mentioned in this Report.

Furthermore, we inform you that:

- the Board of Directors held 14 meetings and the Board of Statutory Auditors always attended these meetings. During 2006, the Board of Statutory Auditors held 9 meetings;
- during 2006 the Board of Auditors issued two opinions pursuant to Article 2389, paragraph three of the Civil Code and Article 2386 of the Civil Code. Viceversa, the Independent Auditors issued only one opinion for the distribution of interim dividends, pursuant to Article 2433-*bis* of the Civil Code;
- no reports were received pursuant to Article 2408 of the Civil Code, nor were any complaints filed by third parties;
- the Company adopted the new Code of Self-Governance ("New Code") issued by Borsa Italiana S.p.A.

  In particular, Terna adapted its Corporate Governance, through the following:

  - defining general criteria on the basis of which the Board of Directors expressed its opinion regarding the maximum number of the positions to be held;
  - defining the new guidelines of the Internal Control System in compliance with the New Code;
  - adopting, on the part of the administrative body, criteria and procedures for evaluating the independence of its members;
  - issuing appropriate regulations for managing and handling company information and for regulating internal management and external communication as far as documents and information regarding the Company are concerned;
  - preparing, adopting and implementing appropriate procedures for regulating transactions with related parties, namely, transactions in which a Director bears an interest.

Furthermore, we would also like to point out, as emerged from the Report on Corporate Governance that is enclosed in the Financial Statement, that the Company has fulfilled its obligations as indicated in the New Code regarding the formation and the activity of the Board of Directors, of the relative internal Committees and of the Board of Statutory Auditors.

Lastly, with reference to the guidelines set forth in the Self-Disciplinary Code, that fall under the competence of this Board of Statutory Auditors, the following is pointed out:

- we verified the correct application of criteria and evaluation procedures for independence adopted by the Board of Directors, with no exception;
- we identified our independence criteria in those envisaged for the Directors, in compliance with the New Code;
- we adopted the transparency regulations and the information obligations set forth for Directors having an interest in a specific transaction;
- we participated in the activity of the Internal Control Committee;
- we monitored the independence of the Independent Auditors KPMG S.p.A.

To comply with the recommendations set forth in Consob notice dated April 6, 2001, and subsequent amendments and integrations, we report the following:

1. during 2006, no atypical or unusual transactions were carried out with related companies or with third parties;
2. with reference to routine transactions with related parties (subsidiaries and associated companies), they essentially concern providing institutional assistance and consulting services (management fee contracts), services for routine operations and maintenance of high voltage lines, financial transactions connected with treasury services, income from renting laboratories and other similar structures for specific uses as well as receiving technical consulting services, study and research services and rental payable for using portions of the National Transmission Grid. Sample checks carried out by the Board of Statutory Auditors and information received indicate that these transactions are in line with the Company's interest.
   As far as the economic outcome of the above-mentioned transactions is concerned, they have generated revenues equal to 42,3 million euros and costs equal to 13,3 million euros.

As specifically indicated, in addition to the auditing assignment, KPMG performed also the following services:

- assignment to audit IFRS reconciliation tables for TERNA, for the sum of 15.000 euros;
- assignment to issue an opinion pursuant to Article 2433-*bis* of the Civil Code for the sum of 32.000 euros;
- assignment to issue a comfort letter on the document for the Euro Medium Term Note Program (EMTNP), for the sum of 55.000 euros;
- assignment to audit the half-year financial statement as of June 30, 2006, following the enforcement of the IFRS and of the acquisition of the TSO business segment, for the sum of 21.000 euros;
- assignment for the translation from Italian into English of the 2006 half year report, for the sum of 9.500 euros.

In addition to the activities listed, information obtained has not revealed that further assignments have been entrusted to subjects associated with the Independent Auditors.

In view of the foregoing, the Board of Statutory Auditors, based on its authority, finds no impediment to the approval of the 2006 Financial Statement as prepared by the Board of Directors.

Rome, May 7, 2007

THE BOARD OF STATUTORY AUDITORS

Avv. Giovanni Ferreri

Dott. Giancarlo Russo Corvace

Prof. Roberto Tasca

KPMG S.p.A.
Revisione e organizzazione contabile
Via Ettore Petrolini, 2
00197 ROMA RM

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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 separate financial statements of TERNA S.p.A. as at and for the year ended 31 December 2006, comprising the income statement, balance sheet, statement of changes in equity, statement of recognised income and expense, cash flow statement and notes thereto. These financial statements are the responsibility of the company's directors. Our responsibility is to express an opinion on these financial statements based on our audit. These are the first set of separate financial statements prepared in accordance with the International Financial Reporting Standards 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 separate 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 directors. We believe that our audit provides a reasonable basis for our opinion.

The separate financial statements present the prior year corresponding figures for comparative purposes prepared using consistent accounting policies. Furthermore, note M to the separate financial statements discloses the effects of the adoption of the International Financial Reporting Standards 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 2006 and issued our report thereon on 5 September 2006.

3 In our opinion, the separate financial statements of TERNA S.p.A. as at and for the year ended 31 December 2006 comply with the International Financial Reporting Standards endorsed by the European Union and the Italian regulations implementing article 9 of

Legislative decree no. 38 of 28 February 2005. Therefore, they are clearly stated and give a true and fair view of the financial position of TERNA S.p.A. as at 31 December 2006, the results of its operations, changes in its equity and its cash flows for the year then ended.

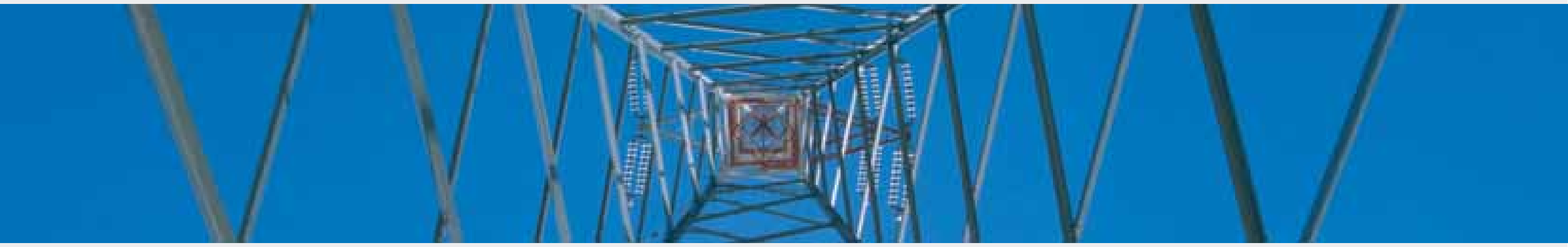
Rome, 7 May 2007

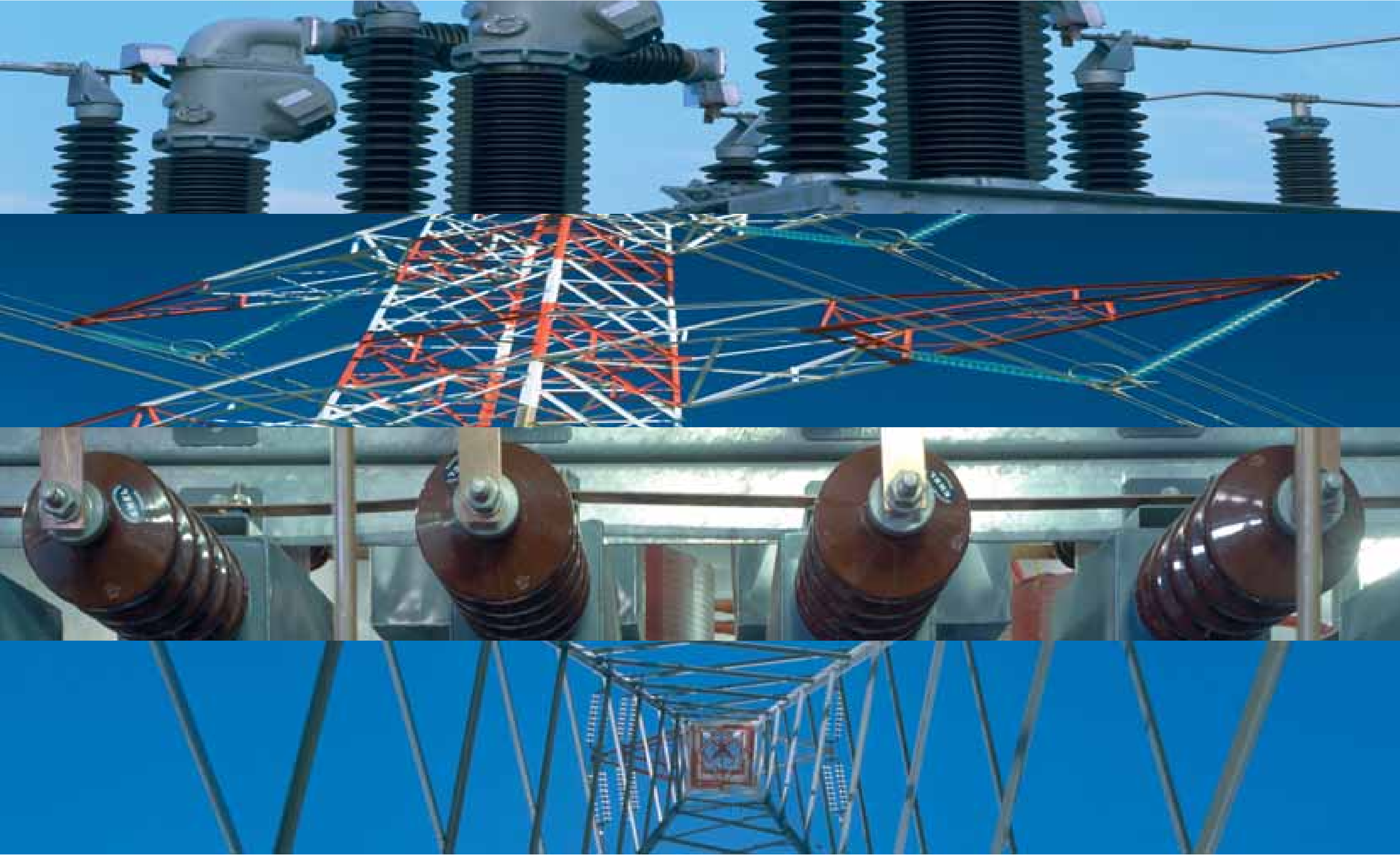
KPMG S.p.A.

(Signed on the original)

Bruno Mastrangelo
Director of Audit

HAVING FIRM BASIS MEANS GREATER MOVEMENT





TERNA GROUP ANNUAL REPORT 2006

Terna
Rete Elettrica Nazionale

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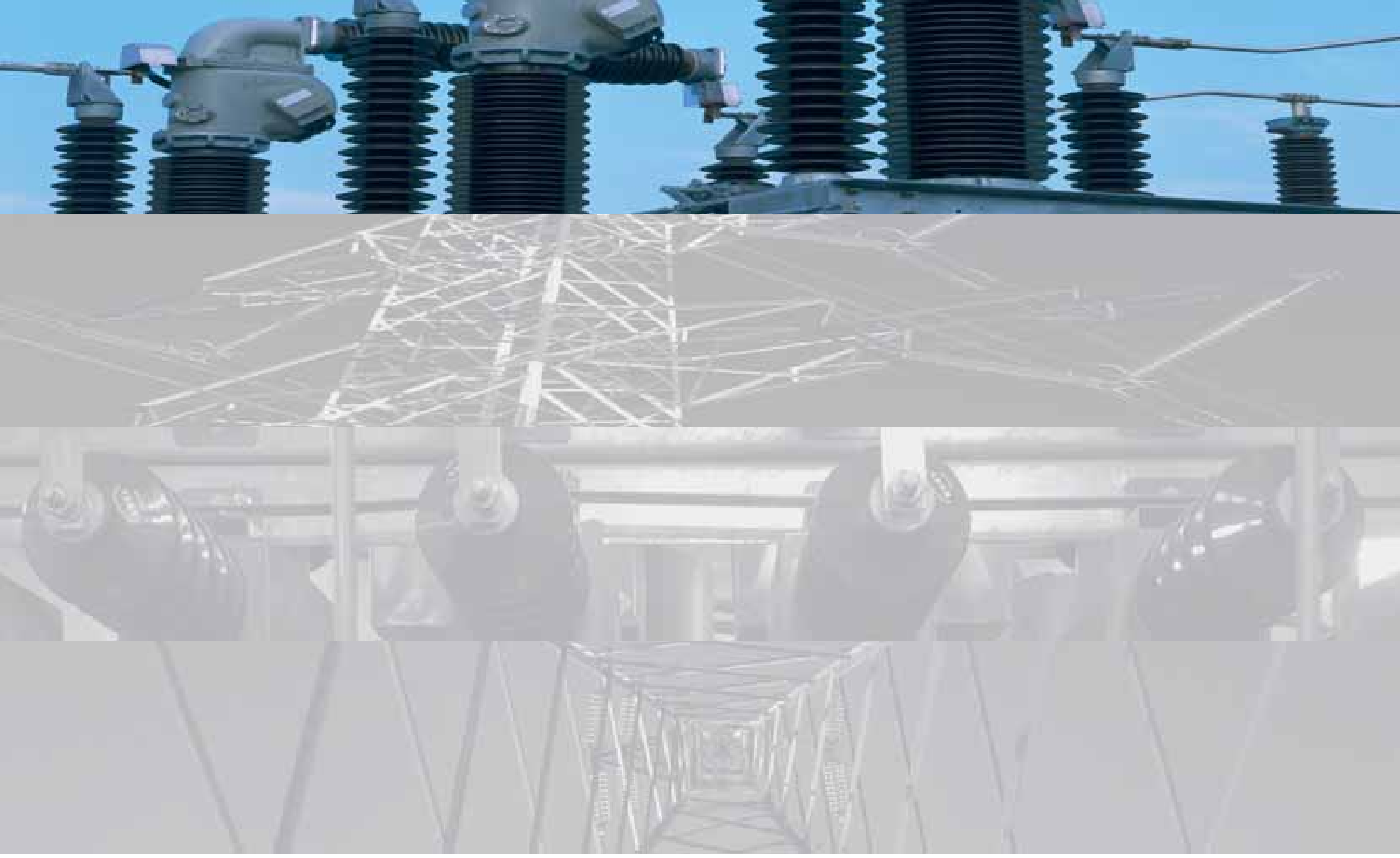


TERNA GROUP DIRECTORS’ REPORT

INTRODUCTION

Pursuant to Article 82 of Consob Resolution no. 11971/1999, the company is not required to publish a 2006 fourth quarter report.

Reference should be made to the Directors' Report on the separate financial statements of Terna SpA for details on the significant events of the year, relevant regulations, energy highlights, Corporate Governance and information.

CONSOLIDATION SCOPE

The consolidation scope includes the subsidiaries Terna Participações SA, TSN SA, Novatrans SA, RTL SpA, RTM1 SpA and RTM2 SpA.
The consolidated income statement includes the results of RTM1 and RTM2 for December 2006, as they were acquired at the end of November 2006. RTL’s figures for 2005 relate to the fourth quarter of that year.
Cesi SpA, which is 24.36% owned, is measured using the equity method.

SUBSIDIARIES

Brazil

Terna Participações

Terna Participações SA (“Terna Part”) was set up in São Paulo, Brazil, on 23 January 2006 under the name of Donnery Holdings SA, to participate as shareholder in other Brazilian or foreign companies active in the transmission of electrical energy.

During an extraordinary meeting on 3 April 2006, the shareholders approved the change of name from Donnery Holdings SA to Terna Participações SA.

On 13 March 2006, all shares in the company were sold to Terna - Rete Elettrica Nazionale SpA (Terna SpA), except for those held by members of the Board of Directors (each of the three Directors owns one share).

On 6 June 2006, Terna SpA contributed control of TSN - Transmissora Sudeste Nordeste SA (“TSN”) and Novatrans Energia SA (“Novatrans”) to Terna Part, with the authorization of the Agência Nacional de Energia Elétrica - ANEEL and lending banks.

On 6 September 2006, Terna Part was registered as “open” to the trading of ordinary shares on the Saõ Paulo stock exchange (BOVESPA).

The global offer of Terna Participações SA certificates (*certificados de deposito de ações*, representing one ordinary share and two preference shares each), launched in view of the subsidiary’s listing on the Nivel 2 segment of Brazil’s Saõ Paulo stock exchange (Bolsa de Valores de Sao Paulo - BOVESPA), related to a total of 29,841,453 certificates at a price of real 21 each (approximately euros 7.8), for a total of roughly real 627 million (approximately euros 232 million).

As part of the offer, 2,210,470 certificates were allocated to retail investors, approximately 7% of the global offer. At the same time, 27,630,975 certificates were allocated to institutional investors, covering roughly 93% of the global offer.

41% of certificates were allocated to US investors, with another 41% going to Brazilian investors and the remaining 18% to Europeans. The OTC offer in the transaction generated gross proceeds of around real 255 million (approximately euros 95 million for Terna SpA), while the primary offer generated proceeds of around real 372 million (approximately euros 137 million) for Terna Participações, which it will use to finance its growth in Brazil and throughout South America. Following the transaction, Terna owns 66% of Terna Participações share capital and 85.3% of its ordinary shares.

Acquisition and merger of Munirah

On 31 March 2006, TSN finalized the acquisition of 100% of Munirah Transmissora de Energia SA ("Munirah") from Control Y Montajes Industriales CYMI SA and Fluxo Engenharia Ltda.

The acquisition, which was governed by a sale and purchase agreement signed on 15 December 2005, was finalized once ANEEL and the financing bank BNDES had given their approval.

Munirah holds concessions on 107 km of transmission lines and two bays in two substations (owned by TSN and Chesf) in Bahia, and makes up the extension of the 500-kV lines owned by TSN that close the North-Northeast circuit.

This transaction will enable Terna to consolidate its presence in Brazil by giving it control over a strategic line in terms of geographical position and proximity to TSN's assets.

The total cost to acquire the entirety of shares amounted to real 48 million (approximately euros 18 million). At 31 March 2006, Munirah had total assets of real 104 million (approximately euros 39 million) and financial indebtedness of real 61 million (approximately euros 23 million). Munirah has the right to an annual fee of real 18 million (approximately euros 7 million) for operating the line on which it holds a concession. On 6 June 2006, based on the price adjustment mechanism included in the sales agreement, the final instalment of the price of real 6.8 million (approximately euros 2.6 million), based on accounting balances confirmed by independent auditors, was paid.

At the same time of the acquisition, Munirah was merged into TSN, to streamline the investment structure and optimize administrative expenses. The difference of roughly euros 3 million between the price paid to acquire Munirah (real 48 million, or approximately euros 18 million) and the fair value of the assets acquired and liabilities assumed and incurred (approximately euros 15 million) was allocated to goodwill.

Brazilian headquarters

In late May 2006, TSN/Novatrans moved its registered offices from rua São Bento 8 - 11 andar Centro - 20090-010 - Rio de Janeiro to Praça XV de Novembro, 20 - 20010-010 - Rio de Janeiro.

UNIBANCO - TSN loan

On 13 April 2006, TSN signed a new loan agreement with UNIBANCO for real 50.0 million, equal to euros 19.4 million, maturing on 13 April 2008. This loan provides for the payment of interest at the short-term interbank rate (CDI) plus a 0.85% spread, and the repayment of principal in 24 instalments at the end of each month.

The year end balance amounts to approximately real 35.0 million.

Projects to consolidate and develop the grid

On 7 June 2006, ANEEL sent TSN a request for a construction and investment plan for the three consolidation projects that will be assigned to it as part of the National Grid Development Plan: a new set of mobile reactors in Bom Jesus da Lapa, upgrade of a set of line reactors in Serra da Mesa I and the sectioning of the substation line in Serra da Mesa II with the installation of a new set of line reactors.

On 14 June 2006, the Master Settlement Agreement was signed by TSN/Novatrans and the consortium formed by Enelpower SpA and Enelpower do Brasil SA, effectively terminating EPC turnkey supply contracts on the construction of the line. In accordance with these contracts, the consortium issued guarantees totalling real 2.0 million.

Fee adjustment

On 27 June 2006, ANEEL issued standardization Resolution no. 355 establishing the new concession fees (RAP) from 1 July 2006 to 30 June 2007. The concession fee for TSN is real 244,183,558.97 and that for Novatrans amounts to real 268,468,585.33. These amounts have been adjusted for inflation (IGPM rate) from June 2005 to May 2006, of -0.32%. ANEEL has also set two lump-sum adjustment payments (*Parcela de Ajuste* or “PA”) to be paid in 12 monthly instalments from July 2006:

(I) a positive PA, as remuneration to the company for the portion of the fee of the previous regulatory period it did not receive because of the allocation of the *Deficit de Arrecadação* to all transmission companies (*transcos*);

(II) a negative PA (i.e., a deduction) in relation to the repayment of the PIS (social integration scheme) and COFINS (social insurance loan) received in the previous period.

The Brazilian tax authorities recently issued a clarification (SRF regulatory Recommendation no. 658 of 4 July 2006) with reference to the RAP, establishing that, for the concession holders that signed concession contracts before 31 October 2003 (such as TSN and Novatrans, but not Munirah), the former PIS/COFINS rates (i.e., PIS of 0.65% and COFINS of 3%) apply retroactively. The amount of the two components results in a net negative PA of real 10,661,195.10 for TSN and real 11,286,451.20 for Novatrans.

This resolution also clarifies that the fee for Munirah (which, despite no longer existing as a special-purpose entity, is still handled separately from TSN from a regulatory standpoint, since it holds a specific concession) in effect from 1 July 2006 to 30 June 2007 is a RAP of real 18,814,303.05 plus a positive PA of real 311,765.33.

Environmental issues

Brazil's environmental policy requires that activities believed to pollute or potentially pollute the environment or that have an adverse impact thereon obtain environmental permits before they can be carried out.

TSN and Novatrans have obtained all the necessary environmental permits for their installation, operation and maintenance activities on transmission lines and sub-stations.

To obtain and keep these permits, the companies are required to invest in protected areas, so as to offset the environmental impact caused by their activities. To this end, IBAMA sets the amounts, timing, methods and allocation of these investments, which should amount to at least 0.5% of the total amount invested.

Exchange rates during the year

In 2006, the Brazilian real appreciated against the US dollar and remained substantially stable with respect to the euro.

In addition, foreign investors' risk perception further improved. The spread on Brazilian securities with respect to US treasury bonds, as calculated by JP Morgan, dropped from 415 points at year-end 2005 to 194 points.

Exchange rates at the end of each quarter*

	dec. 05	mar. 06	jul. 06	sept. 06	dec. 06
BRL/USD	2.32	2.18	2.17	2.17	2.14
BRL/EUR	2.74	2.64	2.76	2.74	2.81
EUR/USD	1.18	1.21	1.27	1.27	1.32

* Source: Italian Exchange Bureau

Payments to Terna

During the year, TSN and NVT paid the parent Terna euros 14.0 million and euros 14.5 million, respectively, in interest on equity of 2005 and euros 18.1 million and euros 9.9 million, respectively, in dividends of 2005. In addition, on 19 October 2006, Terna Participações SA paid Terna the 2006 interim dividend of euros 9.9 million.

Operating activities

NOVATRANS ENERGIA (NVT)

Operating activities

In 2006, the 500-kV North-South II transmission line, which runs for approximately 1,278 km, from Samambaia (Federal district) to Imperatriz (Maranhão), covering the intermediate sub-stations in Serra da Mesa, Gurupí, Miracema and Colinas, became fully operational.

Construction activities

Construction on the new ancillary services for all stations with independent power supplies from Furnas and Eletronorte continued in 2006. All power units began operating and the MV/LV converters are near completion. The installation of the DC power supply systems of the ancillary services, essential for the transient voltage stability controllers (TCSC), was completed.

Service quality

The availability and failure rate indicators are provided below for 2006 and 2005.

Amounts are calculated using the ONS *Procedimentos de Rede* (grid procedures).

NOVATRANS - SERVICE QUALITY

	AVAILABILITY *		FAILURE RATE *	
	12/2006	**12/2005**	**12/2006**	**12/2005**
Line	99.99%	99.82%	0.23	0.24
FSC	99.93%	99.87%	0.17	0.67
TCSC	99.28%	98.12%	2.01	28.03

* excluding unavailability for external reasons or *force majeure*.

TRANSMISSORA SUDESTE NORDESTE (TSN)

Operating activities

During the year, the 500-kV Sudeste - Nordeste transmission line, with an “As Built” length of 1,062 km[(1)],

[(1)] (compared to the 1050 km indicated in the concession agreement), in addition to the 15 km on the 203-kV dual-triad sections (taking them as two separate circuits) for a total of 1,077 km.

from Serra da Mesa (Goias) to Sapeaçu (Bahia), and covering the intermediate sub-stations in Rio das Eguas, Bom Jesus da Lapa and Ibicoara, became fully operational. The Camaçari-Sapeaçu connection also began operating on 1 April 2006 for TSN.

Construction activities

During the year, two additional back-up reactors were put into use.

The basic project to expand the Serra da Mesa and Bom Jesus da Lapa stations, commissioned by ONS/ANEEL, continued.

The installation of the DC power supply system for the ancillary services, essential for the static voltage compensator, was practically completed, pending the provision of certain pieces of equipment.

Service quality

The availability and failure rate indicators are provided below for 2006 and 2005.

The figures show a progressive improvement in service quality from when the plants began operating.

Amounts are calculated using the ONS *Procedimentos de Rede* (grid procedures).

TSN - SERVICE QUALITY

	AVAILABILITY *		FAILURE RATE *	
	12/2006	**12/2005**	**12/2006**	**12/2005**
Line	99.98%	99.65%	0.00	0.00
Reactors	100.00%	99.98%	0.00	0.00
ATR	100.00%	99.07%	1.00	0.25
SVC	99.84%	99.88%	1.00	4.01

* excluding unavailability for external reasons, *force majeure* or reinforcement requested by ONS.

Italy

The financial statements of the subsidiaries RTL, RTM1 and RTM2 have been prepared in accordance with the current regulations under Article 2423 and subsequent articles of the Italian Civil Code, as modified by Legislative Decree no. 6/2003. The notes to the results of each company include disclosure of the effects of adjustment to International Financial Reporting Standards (IFRS), which the parent has adopted.

The business activity of all Group companies consists of operating and maintaining transmission grids, on a substantially regular basis.

The group achieved the reliability standards set by Terna in terms of failure types, the maintenance backlog and scheduled and unscheduled maintenance work.

RTL - Rete di Trasmissione Locale

The financial statements of this company show profits for the year of euros 1.7 million, net of depreciation of roughly euros 1.8 million, net financial and extraordinary income of euros 0.2 million and income taxes of euros 1.3 million.

Investments in property, plant and equipment amounted to euros 0.1 million.

Revenues totalled roughly euros 6.5 million, mainly in relation to the consideration received for use of a portion of the National Transmission Grid.

Operating expenses amounted to approximately euros 2.0 million, including services of euros 1.7 million.

Following the consolidation entries and adjustments to adjust the company's accounting policies to the IFRS adopted by the parent, RTL's contribution to the consolidated profits for the year attributable to the shareholders' of the parent amounted to around euros 3.0 million.

On 1 October 2005, RTL signed a specific agreement with the parent in line with market conditions, transferring to Terna the operating and ordinary maintenance activities on the transmission lines owned by RTL.

Furthermore, another two agreements (general service agreement and treasury agreement) with the parent. These are also in line with current market conditions or with cost-based appraisals considering the quantity of product/service used.

RTM1 - Rete Trasmissione Milano 1

The financial statements of this company show a profits for the year of euros 10.9 million, net of amortization and depreciation of roughly euros 10.5 million, net financial and extraordinary expenses of euros 1.6 million and income taxes of euros 7.2 million.

Investments in property, plant and equipment amounted to euros 2.1 million.

Revenues totalled roughly euros 49.4 million, mainly in relation to the consideration received for use of a portion of the National Transmission Grid.

Operating expenses amounted to approximately euros 19.2 million, including services of euros 9.9 million.

Following the consolidation entries and adjustments to adjust the company's accounting policies to the IFRS adopted by the parent, RTM1's contribution to the consolidated profits for the year attributable to the shareholders' of the parent (which relates only to December 2006, as mentioned above) amounted to around euros 0.3 million.

RTM2 - Rete Trasmissione Milano 2

The financial statements of this company show profits for the year of euros 5.3 million, net of amortization and depreciation of roughly euros 4.0 million, net financial and extraordinary income of euros 0.1 million and income taxes of euros 3.3 million.

Investments of the year amounted to euros 2.0 million.

Revenues totalled roughly euros 16.1 million, mainly in relation to the consideration received for use of a portion of the National Transmission Grid.

Operating expenses amounted to approximately euros 3.4 million, including services of euros 1.7 million.

Following the consolidation entries and adjustments to adjust the company's accounting policies to the IFRS adopted by the parent, RTM2's contribution to the consolidated profits for the year attributable to the shareholders' of the parent (which relates only to December 2005, as mentioned above) amounted to around euros 0.3 million.

New contracts with subsidiaries

Under specific agreements, on 1 February 2007, Terna SpA was entrusted with operating and carrying out ordinary maintenance on the lines owned by its subsidiaries RTM1 SpA and RTM2 SpA. These activities consist of the following:

1) inspections and testing;
2) emergency assistance;
3) preparing and implementing conventional work plans without shutting off voltage;
4) managing interference;
5) managing unavailability and operating events;
6) ordinary maintenance;
7) damage to the National Transmission Grid.

In addition, also on 1 February 2007, a management fee agreement was signed by Terna SpA and RTM1, making the parent responsible for outlining strategies and handling business coordination, as well as providing direct and indirect services to the subsidiary. These include:

1) the coordination of managers, through suitable training programmes;
2) the administrative and financial coordination of the subsidiary, including the set-up and management of its financial activities;
3) the provision of other services in specific business areas.

A similar management fee agreement will be signed by Terna SpA and its subsidiary RTM2 SpA.

TERNA GROUP RESULTS

The consolidated financial statements as of and for the year ended 31 December 2006 show profits for the year of euros 369.8 million, after amortization and depreciation of approximately euros 212.4 million, net financial expenses of euros 68.6 million and income taxes of euros 249.1 million.

Revenues amounted to approximately euros 1,307.8 million, including euros 1,191.5 million in relation to the consideration received for use of the grid. In particular, considerations for use of the parent's grid have been approved for approximately euros 994.3 million, up roughly euros 172.7 million (+21.0%) on 2005. The contribution of subsidiaries totalled euros 197.2 million (including euros 95.2 million from Novatrans, euros 91.3 million from TSN and euros 10.7 million from the Italian subsidiaries).
Operating expenses amounted to approximately euros 407.9 million, including personnel expenses of euros 242.0 million and services of euros 145.3 million.

Income taxes of the year, which totalled euros 249.1 million, include euros 211.1 million due from the parent, euros 18.7 million from Novatrans, euros 17.6 million from TSN and euros 1.7 million from the Italian subsidiaries. The balance sheet includes net non-current assets of euros 5,470.9 million, net invested capital of euros 4,441.7 million, of which euros 2,158.9 million is covered by equity (including euros 150 million attributable to minority interests) and net financial indebtedness of euros 2,282.8 million.

The 2006 and 2005 consolidated income statements of Terna Group for management purposes are summarized below. Figures have been reclassified.

Reclassified Income Statement

(a)

In millions of euros	2006	2005	Change	%
Revenues:				
Grid transmission consideration (1)	1191.5	992.7	198.8	20.0%
Other energy items (1)	41.9	6.9	35.0	507.2%
Other revenues from goods and services (1)	46.1	59.1	-13.0	-22.0%
Other revenues and income	28.3	23.1	5.2	22.5%
Total revenues	**1307.8**	**1081.8**	**226.0**	**20.9%**
Operating expenses:				
Personnel expenses	242.0	201.7	40.3	20.0%
Services and use of third party assets	145.3	118.8	26.5	22.3%
Materials	18.7	25.4	-6.7	-26.4%
Other expenses (2)	38.7	45.8	-7.1	-15.5%
Capitalized expenses	-36.8	-26.5	-10.3	38.9%
Total operating expenses	**407.9**	**365.2**	**42.7**	**11.7%**
GROSS OPERATING PROFITS	**899.9**	**716.6**	**183.3**	**25.6%**
Amortization and depreciation (3)	**212.4**	**175.1**	**37.3**	**21.3%**
OPERATING PROFITS	**687.5**	**541.5**	**146.0**	**27.0%**
Net financial income (expenses) (4)	-68.6	-80.2	11.6	-14.5%
PROFITS BEFORE TAXES	**618.9**	**461.3**	**157.6**	**34.2%**
Income taxes	249.1	163.4	85.7	52.4%
PROFITS FOR THE YEAR	**369.8**	**297.9**	**71.9**	**24.1%**
PROFITS FOR THE YEAR ATTRIBUTABLE TO MINORITY INTERESTS	3.5	0	3.5	100.0%
PROFITS FOR THE YEAR ATTRIBUTABLE TO THE SHAREHOLDERS OF THE PARENT	366.3	297.9	68.4	23.0%

(a) In accordance with Communication no. DME/6064291 of 28 July 2006, the reclassified income statement is unaudited.

Revenues for 2006, amounting to euros 1,307.8 million (parent: euros 1,108.1 million; Italian subsidiaries: euros 12.2 million; Brazilian subsidiaries: euros187.5 million), rose by euros 226.0 million (+20.9% on the euros 1,081.8 million of 2005).

The net increase in revenues is mainly due to the growth in the consideration for use of the grid, amounting to roughly euros 199 million, including:

- the parent's contribution of euros 172.7 million, mainly due to:
  - an increase in revenues of approximately euros 54.1 million, primarily as a result of the new tariff process;
  - an increase in revenues of approximately euros 58.9 million following the activities carried out for all of 2006 in relation to the acquisition of the TSO business activity in November 2005;
  - the effects of Resolution no. 162/06 and adjustments to previous years of euros 59.6 million;

In the consolidated financial statements:

(1) the balance is included in "Revenues from goods and services"

(2) this corresponds to the captions "Other costs" and "Amortization, depreciation and impairment losses" for the amount of the accrual to the provision for bad debts (euros 12.1 million);

(3) the balance corresponds to the caption "Amortization, depreciation and impairment losses", net of the accrual to the provision for bad debts;

(4) this corresponds to the balance of the captions described in points 1, 2 and 3 of "Financial income and expenses".

- the Brazilian companies' contribution of around euros 16.8 million, mainly due to the effect of the appreciation of the Brazilian real over the euro in 2006 compared to 2005;
- the Italian subsidiaries' contribution of roughly euros 9.4 million, including RTL revenues of euros 5.2 million (consolidated in the fourth quarter of 2005) and RTM1 and RTM2 revenues of euros 4.2 million, which were only included in the income statement in December 2006.

The increase of approximately euros 35.0 million in other energy items relates to the parent and is due to the dispatching and metering activities acquired with the GSE (formerly GRTN) business activity, which was only consolidated in the last two months of 2005.

Operating expenses: amounted to euros 407.9 million (parent: euros 369.1 million; Italian subsidiaries: euros 3.5 million; foreign subsidiaries: euros 35.3 million), up 11.7% (euros 42.7 million) on 2005 (euros 365.2 million).

The increase may be analyzed as follows:

- the parent's increase of approximately euros 46.3 million, mainly due to costs incurred throughout 2006 as a result of the acquisition of the TSO business activity, while in 2005 these costs only affected the last two months of the year;
- the Brazilian subsidiaries recorded a decrease in operating expenses of around euros 6.8 million, following the reduction in the PIS and COFINS tax rates, which also led to the recovery of taxes paid in 2005 (for a total decrease of roughly euros 16 million), partially offset by an increase in service costs of around euros 8 million, mainly due to costs incurred for the stock market listing of Terna Part;
- the increase recorded by RTM1 and RTM2 of approximately euros 3 million.

Moreover, capitalized expenses, entirely in relation to the parent, rose roughly by euros 10.3 million.

EBITDA (gross operating profits) rose by euros 183.3 million (+25.6%) from euros 716.6 million in 2005 to euros 899.9 million. The Brazilian subsidiaries contributed with euros 152.2 million, compared to euros 128.2 million in 2005.

EBIT (operating profits) grew euros 146.0 million (+27%) from euros 541.5 million in 2005 to euros 687.5 million. The benefits of this growth were offset by the substantial increase in amortization and depreciation (up euros 37.3 million), including euros 33.1 million attributable to the parent (amortization of euros 13.2 million and depreciation of euros 19.9 million, mainly due to the acquisition of the business activities from TSO and GSE).

Net financial expenses of euros 68.6 million decreased by 14.5% (- euros 11.6 million), as follows:

In millions of euros	2006	2005	Change
Financial income			
Interest income on former intercompany current account with Enel SpA	-	3.3	-3.3
Gain on Terna Part IPO	31.4	-	31.4
Other financial income	13.5	11.6	1.9
Value changes of the hedged bond	-	3.7	-3.7
Income on trading derivatives	8.8	-	8.8
Exchange rate gains	7.0	16.8	-9.8
Measurement of equity-accounted investees	-	1.8	-1.8
Total income	**60.7**	**37.2**	**23.5**
Financial expenses			
Interest expenses on medium/long-term loans	118.4	109.5	8.9
Value changes of the hedged bond	2.6	-	2.6
Expenses on trading derivatives	-	2.0	-2.0
Discounting of termination benefits and other employee-related provisions	6.6	5.9	0.7
Exchange rate losses	1.7	-	1.7
Total expenses	**129.3**	**117.4**	**11.9**
TOTAL	**68.6**	**80.2**	**-11.6**

The gains on the Terna Part IPO of euros 31.4 million includes the following:

- Terna SpA's collection of euros 82.7 million, corresponding with the listing price of Terna Part shares sold on the OTC market for euros 93.9 million, net of local taxes and fees incurred for the transaction (euros 11.2 million);
- the increase in the nominal value of shares held by Terna SpA (euros 32.7 million) following Terna Part's share capital increase subscribed by other investors on the primary market;
- transfer of profits and reserves of the Brazilian subsidiaries (- euros 44.6 million), accrued up to the listing by effect of the dilution of Terna's SpA percentage of ownership to 66%;
- the reversal of goodwill originally recognized, to the extent of the investment transferred through the listing (- euros 39.2 million).

The **profits for the year** rose by 24.1% from euros 297.9 million in 2005 to euros 369.8 million, net of income taxes of euros 249.1 million (Brazilian companies: euros 36.3 million and a net deferred tax charge of euros 19.3 million). The impact of income taxes on the profits before taxes is 40.2%.

Financial position

The Terna Group consolidated balance sheets for management purposes as of 31 December 2005 and 2006 are summarized below. Figures have been reclassified.

(a)

In millions of euros	31.12.2006	31.12.2005	Change
Non-current assets, net			
Intangible assets [1]	299.1	306.2	-7.1
Property, plant and equipment	5,159.0	4,646.3	512.7
Other [2]	12.8	13.4	-0.6
Total	**5,470.9**	**4,965.9**	**505.0**
Net working capital			
Trade receivables	1,182.1	1,026.2	155.9
Inventories	25.6	21.2	4.4
Other assets [3]	26.4	20.9	5.5
Trade payables	1,280.6	975.0	305.6
Tax liabilities, net [4]	115.5	16.9	98.6
Other liabilities [5]	249.6	255.4	-5.8
Total	**-411.6**	**-179.0**	**-232.6**
Gross invested capital	**5,059.3**	**4,786.9**	**272.4**
Other provisions [6]	617.6	616.0	1.6
Net invested capital	**4,441.7**	**4,170.9**	**270.8**
Equity	2,008.9	1,902.2	106.7
Equity attributable to minority interests	150.0	0.0	150.0
Net financial indebtedness [7]	2,282.8	2,268.7	14.1
TOTAL	**4,441.7**	**4,170.9**	**270.8**

(a) In accordance with Communication no. DME/6064291 of 28 July 2006, the reclassified balance sheet is unaudited.

In the consolidated interim financial statements the captions correspond to:
(1) "Goodwill" and "Intangible assets";
(2) "Equity-accounted investees" and "Other non-current assets"
(3) "Other current assets", net of tax assets (euros 8.2 million) and "Current financial assets" for the amount of accrued financial income (euros 0.6 million);
(4) "Other current assets" for the amount of tax assets (euros 8.2 million), "Tax liabilities" and "Other current liabilities" for the amount of tax liabilities other than payables for taxes of the year (euros 48.4 million);
(5) "Current financial assets" for the amount of accrued income on derivative contracts on bonds (euros 1.6 million), "Other non-current liabilities", "Current financial liabilities" and "Other current liabilities", net of tax liabilities other than payables for taxes of the year (euros 48.4 million);
(6) "Termination benefits and other employee-related provisions", the "Provision for contingencies and charges", "Tax liabilities, including deferred" and "Deferred tax assets".
(7) "Long-term loans", "Current portion of long-term loans", "Short-term loans", "Cash and cash equivalents", "Non-current financial assets" and "Non-current financial liabilities".

Net financial indebtedness is detailed as follows:

In millions of euros	2006	2005	Change
Bonds	1,406.60	1,498.40	-91.8
EIB loans	570.4	400	170.4
BNDES/IDS loans	462	468.9	-6.9
Short-term loans	50	55	-5
Bank account balances and cash	-200.4	-76.6	-123.8
Derivative financial instruments	-5.8	-77	71.2
TOTAL FINANCIAL INDEBTEDNESS	**2,282.80**	**2,268.70**	**14.1**

The euros 7.1 million decrease in intangible assets was the result of the combined effect of the following changes:

- an increase of euros 7.7 million in the parent's other intangible assets following ordinary changes of the year in relation to investments for the internal development of software or its purchase as part of system development programmes (euros 26.5 million) and amortization and depreciation (euros 18.8 million), including euros 5.6 million on the concession for transmission and dispatching activities;
- a decrease of roughly euros 14.8 million in goodwill, mainly due to:
  - an increase of approximately euros 38 million due to the Italian subsidiaries (RTM2: euros 26 million; RTM1: euros 12 million, reflecting the portion of the purchase price that could not be allocated under IFRS 3);
  - a net decrease of around euros 52 million in relation to the Brazilian subsidiaries, mainly following the loss of the 34% investment in Terna Part as a result of the stock market listing and exchange rate adjustments.

The euros 512.7 million increase in property, plant and equipment was mainly due to the following:

- euros 378.1 million on the inclusion in the consolidation scope at 31 December 2006 of RTM1 (euros 290.4 million) and RTM2 (87.7 million). These amounts include the effect of the purchase price allocation based on the estimated fair value of plant and machinery held by RTM1 and RTM2, included in the purchase price. These amounts, which were calculated on the basis of an appraisal conducted by independent experts, totalled euros 100.2 for RTM1 million and euros 10.2 million for RTM2;
- euros 128.6 million in relation to the parent, following the net effect of investments (euros 318.5 million) and amortization, depreciation and disposals (euros 189.9 million).

Net working capital amounted to a negative euros 411.6 million, up on the negative euros 232.6 million of 2005. This improvement was mainly due to the parent (euros 227.3 million) and includes the management of dispatching items, which are in transit, but which give rise to significant financial volumes (euros 139 million). The change in net tax liabilities (euros 98.6 million) was also significant, both in terms of VAT payables (euros 36.6 million), and the rise in income taxes, which was due to the following:

- a sharp increase in the profits for the year and the introduction of new tax regulations in 2006 concerning the deductibility of depreciation (land and motor vehicles);
- the tax gain on the contribution of investments in TSN and Novatrans to the Brazilian subsidiary Terna Participações, in addition to the gain realized on the listing of Terna Participações on the São Paulo stock exchange.

Other provisions amounted to euros 617.6 million, substantially in line with the previous year.

Accordingly, at year end, net invested capital amounted to euros 4,441.7 million, compared to euros 4,170.9 million at the end of the previous year. Equity coverage amounted to euros 2,158.9 million (48.6%) and net financial indebtedness covered the remaining euros 2,282.8 million (51.4%).

Reconciliation of the consolidated profits for the year and equity with the parent’s profits for the year and equity

In millions of euros	Profits 31.12.2006	Equity at 31.12.2006	Profits 31.12.2005	Equity at 31.12.2005
FINANCIAL STATEMENTS OF THE PARENT	**355.8**	**1,901.7**	**265.6**	**1,797.9**
Profits and equity of consolidated companies	57.7	66.2	69.7	64.1
Effect of the translation of financial statements of foreign companies	-	46.4	-	67.3
Reversal of dividends and interests on equity distributed by the subsidiaries	-40.0	-	-39.2	-28.9
Adjustment to the gain on the Terna Participações listing	-7.0	-7.0	-	-
Measurement of Cesi using the equity method	-	1.8	1.8	1.8
Other adjustments	-0.2	-0.2	-	-
IFRS-COMPLIANT CONSOLIDATED FINANCIAL STATEMENTS	**366.3**	**2,008.9**	**297.9**	**1,902.2**

Cash flows

Cash flow analysis

In millions of euros	2006	2005	Change
OPENING INTERCOMPANY CURRENT ACCOUNT AND CASH	**76.6**	**231.8**	**-155.2**
Profit for the year	369.8	297.9	71.9
Amortization and depreciation	212.5	175.2	37.3
Net change in provisions	2.2	20.2	-18
Self-financing	**584.5**	**493.3**	**91.2**
Change in net working capital	232.6	-21.5	254.1
Cash flows generated by/(used in) operating activities	**817.1**	**471.8**	**345.3**
Investments			
Property, plant and equipment	-326.0	-268.7	-57.3
Intangible assets	-26.5	-4.1	-22.4
Net investments in financial assets	-386.5	-341.3	-45.2
Total cash flows generated by/(used in) investing activities	**-739.0**	**-614.1**	**-124.9**
Change in loans	137.9	220.9	-83
Other changes in equity attributable to the shareholders of the parent	27.3	6.2	21.1
Dividends	-266.0	-240.0	-26
Terna Participações listing	148.7	0.0	148.7
Other changes in equity attributable to minority interests	-2.2	0.0	-2.2
Total cash flows generated by/(used in) financial activities	**45.7**	**-12.9**	**58.6**
Total cash flows of the year	**123.8**	**-155.2**	**279.0**
CLOSING INTERCOMPANY CURRENT ACCOUNT AND CASH	**200.4**	**76.6**	**123.8**

Change in consolidated net financial position

In millions of euros	2006	2005
OPENING NET FINANCIAL INDEBTEDNESS	**-2,268.7**	**-1,892.5**
Self-financing	584.5	493.3
Change in net working capital	232.6	-21.5
Cash flows generated by/(used in) operating activities	**817.1**	**471.8**
Investments in property, plant and equipment	-326.0	-268.7
Investments in intangible assets	-26.5	-4.1
Net investments in financial assets	-386.5	-341.3
Cash flows generated by/(used in) investing activities	**-739.0**	**-614.1**
Dividends distributed/collected	-266.0	-240.0
Other changes in equity attributable to the shareholders of the parent	27.3	6.2
Terna Participações listing	148.7	0.0
Other changes in equity attributable to minority interests	-2.2	0.0
Self-financing flows	**-92.2**	**-233.8**
Change in financial indebtedness	-14.1	-376.2
CLOSING NET FINANCIAL INDEBTEDNESS	**-2,282.8**	**-2,268.7**

The cash flows generated by operating activities during the year amounted to approximately euros 817.1 million and are due to self-financing (profits for the year, amortization and depreciation and accruals totalling euros 584.5 million) and the contribution of cash flows (euros 232.6 million) generated by the management of working capital.

Investing activities used net cash flows of approximately euros 739.0 million in relation to investments in property, plant and equipment and intangible assets (euros 352.5 million) and, more significantly, to the acquisition of investments in RTM1 and RTM2 (euros 416.8 million).

Cash outflows for self-financing were mainly due to the parent’s distribution of dividends to shareholders during the year (euros 266 million), which was partially offset by the cash flows generated by the Terna Participações IPO (euros 146.5 million).

Accordingly, the cash flows used in investing activities and self-financing totalled euros 831.2 million, which was almost entirely covered (euros 817.1 million) by the cash flows generated by operating activities.

Indebtedness

The following table details consolidated net financial indebtedness (euros 2,282.8 million) at year end with an analysis of timing:

In millions of euros	2006	2005	Change
A) Medium and long-term indebtedness			
Bonds	1,406.6	1,498.4	-91.8
EIB loans	540.9	370.5	170.4
Brazil loans	420.4	440.2	-19.8
Derivate financial instruments	-5.8	-77.0	71.2
Total A	**2,362.1**	**2,232.1**	**130.0**
B) Short-term indebtedness (funds)			
Bond (current portion)	0.0	0.0	0.0
EIB loans (current portion)	29.5	29.5	0.0
Brazil loans (current portion)	41.6	28.7	12.9
Short-term loans	50.0	55.0	-5.0
Cash and cash equivalents in Italy	-15.3	-15.8	0.5
Cash and cash equivalents in Brazil	-185.1	-60.8	-124.3
Total B	**-79.3**	**36.6**	**-115.9**
TOTAL A + B	**2,282.8**	**2,268.7**	**14.1**

Investments in property, plant and equipment

Investments at 31 December 2006 may be broken down by type of plant and compared with the previous year as follows:

In millions of euros	2006	2005
Transmission lines	120.4	121.3
Transformation stations	148.9	121.7
Other	49.7	18.9
Brazil	7.0	9.4
TOTAL INVESTMENTS	**326.0**	**271.3**

Development investments

The main projects of the year included the completion of the Laino-Feroleto-Rizziconi line, the Turbigo-Rho long distance line, the construction of the Sardinia-Corsica line and the start-up of SAPEI activities.

In addition, collaboration and preliminary design activities began in advance on the Sorgente-Rizziconi line (slated for 2007), while work progressed on the Matera - S.Sofia line (expected to become operational in the first half of 2007) and on the Casellina - S.Barbara line.

Maintenance and other investments

Renovation is being completed on the Villavalle, Calenzano and Verderio (already up and running) stations where civil projects are being finished up. Work continued on the Pianezza station.

Other investments include IT projects (rationalization of processes: basic software, LAN network upgrade, etc.), the purchase of company cars and the building in Via della Marcigliana.

Plants

The group's plants in Italy are detailed in the following table:

	TERNA		RTL		RTM1		RTM2		TOTAL	
	N°	Km	N°	Km	N°	Km	N°	Km	N°	Km
Stations	315	-	-	-	30	-	12	-	357	-
Transformers	576	-	-	-	18	-	1	-	595	-
Bays	4,046	-	8	-	207	-	56	-	4,317	-
Lines	-	35,316	-	538	-	2,482	-	720	-	39,056
Triads	1,968	39,222	26	703	105	2,756	23	1,095	2,122	43,776

The main changes seen in 2006, other than RTM1 and RTM2, which were not a part of the group at 31 December 2005, entirely relate to the parent, and are as follows:

Stations

The number of stations increased by a total of 13 compared to 31 December 2005. This increase was due to the following:

- seven new stations becoming operational: Carpi Fossoli, Ferrara Nord, Rho, Pogliano and Sparanise (380 kV); Edison Terni (150 kV); Bardi (132 kV);
- disposal of one plant: Rosen (380 kV);

- purchase of nine plants from Enel Distribuzione: Certosa (220 kV); Pettino (150 kV); Montestrutto, San Rocco, AGIP Petroli, Sondel Porcari, Centro Energia Ferrara, Degussa and Lonza (132 kV);
- sale of two stations to Enel Distribuzione: Sorio (220 kV); Bando (132 kV).

Transformers

The number of transformers increased by four, as follows:

- activation of two 220/132 kV autotransformers, which were previously available, for a total of 410 MVA in the Scorzè and Vicenza Monteviale stations;
- installation of two new 380/220 kV and 380/132 kV autotransformers for a total of 650 MVA in the S. Barbara station;
- installation of two new 380/220 kV autotransformers for a total of 800 MVA each in the S. Maria Capua Vetere and Rumianca stations;
- installation of a new 380 kV/132 kV autotransformer with 250 MVA in the S. Damaso station;
- acquisition of two machines (one 150/132 kV autotransformer and one 132/60 kV transformer) for a total of 75 MVA in relation to the acquisition of the S. Rocco and Pettino stations from Enel Distribuzione;
- replacement of two 380/132 kV, 160 MVA autotransformers with two 250 MVA autotransformers in the Avenza and Bussolengo S. Salvar stations;
- transfer of five 132 kV/MT transformers for a total of 160 MVA in relation to the transfer of the Sorio station and medium voltage section of the Tavarnuzze plant to Enel Distribuzione.

Total transformation capacity increased by 2,365 MVA during the year.

Long distance power lines

In terms of long distance lines, the total length of triads increased approximately 246 km compared to 31 December 2005. This increase is mainly due to the following:

- construction of the 380 kV Ospiate - Turbigo link (approximately 38 km, including 16.6 km underground);
- construction of the 150 kV underground/underwater line from S. Teresa di Gallura to Bonifacio (Corsica) called Sar.Co (approximately 14 km);
- construction of the 150 kV underground Molentargius - Selargius line (approximately 10 km);
- link between the Larderello plant to the 132 kV Certaldo - Poggibonsi line (approximately 34 Km);
- in-and-out link from the 380 kV Garigliano - S. Maria Capua Vetere line to the new Sparanise station (approximately 7 km);
- in-and-out link from the 220 kV Aversa - Capriati and Fratta - Presenzano lines to the new 220 kV section

of the S. Maria Capua Vetere station (approximately 12 km);

- acquisition of the 132 kV Bulciago - Nibionno, Nibionno - Carugo, Novedrate - Salice, Carugo - Salice and Strettoia - Isola Santa lines (for a total of approximately 35 km) from Enel Distribuzione;
- acquisition of the 150 kV Benevento II - Benevento Nord 1, Viagrande - S. Venerina, Reggio Condera - Reggio Industriale, Reggio Condera - Scilla, Reggio Industriale - Scilla, Gallico - Villa S.Giovanni, Gallico - Reggio Condera, Scilla - Villa S.Giovanni, Quartucciu - Molentargius, Quartu S. Elena - Molentargius, Selargius - Quartucciu, Selargius - Quartu S. Elena lines and Isili shunt (for a total of approximately 135 km) from Enel Distribuzione;
- demolition of the 220 kV Sondrio - Robbia pole 1 line (approximately 25 km);
- sale of the 150 kV S. Agata - Capo d’Orlando line (approximately 17 km) to Enel Distribuzione;

The group’s plants in Brazil are detailed in the following table:

	TSN		NOVATRANS		TOTAL	
	N°	Km	N°	Km	N°	Km
Stations	7	-	-	-	7	-
Transformers	14	-	-	-	14	-
Bays	31	-	10	-	41	-
Lines	-	1,183	-	1,278	-	2,461
Triads	12	1,183	5	1,278	17	2,461

In comparison with the previous year, there was an increase in the number of stations by two and in the length of lines by 107 km, following the acquisition of the Camaçari - Sapeaçu plants.

Results by geographical area and business segment

Reference should be made to the specific paragraph of the notes for a breakdown of Group highlights for its Italian and Brazilian activities and an analysis by business segment.

RESEARCH AND DEVELOPMENT

Reference should be made to the Directors' Report on the separate financial statements of Terna SpA for information on research and development.

HUMAN RESOURCES

New organizational structure

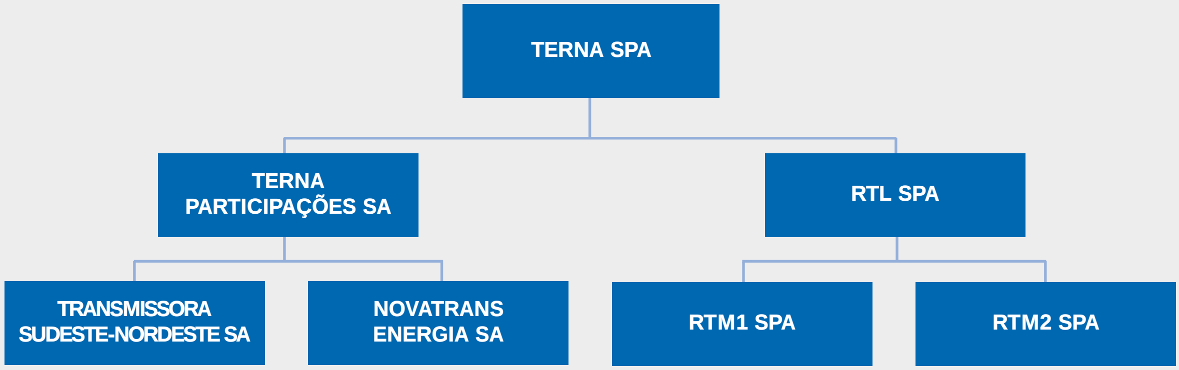
In January 2006, Terna's new organizational structure became operational. As part of this structure and with the goal of ensuring control over the business development process, the Business Development and International Management Area was created.

With effect from 1 October 2006, in view of the stock market listing of Terna Participações (carried out on 27 October 2006), the organization of Terna's Business Development and International Management Area was reviewed, resulting in the elimination of the Subsidiaries Coordination Department. At the same time, the entire organizational structure of Terna Participações was also reviewed.

Terna Participações General Management now reports directly to the CEO of Terna SpA. The various departments of Terna Participações now directly report to the General Manager and, functionally, to the corresponding departments of Terna SpA.

On 24 November 2006, through Rete Trasmissione Locale SpA ("RTL SpA"), wholly owned by Terna SpA, the Terna Group concluded the acquisition of 100% of Edison Rete SpA and 99.99% of AEM Trasmissione SpA with Edison SpA and AEM SpA, respectively. On the same day, the shareholders of Edison Rete SpA and AEM Trasmissione SpA met and appointed the new company officers, moved their registered offices and changed their company names. Edison Rete became Rete Trasmissione Milano 1 Società per azioni ("RTM1 SpA") and AEM Trasmissione became Rete Trasmissione Milano 2 Società per azioni ("RTM 2 SpA"). The organizational structure of both companies is unchanged.

Accordingly, the group's structure at year end is as follows:



2007 will see the implementation of the integration plan for RTM1 and RTM2 employees into Terna SpA.

Changes in the number of employees

Changes in the number of Terna Group employees are shown below.

Change in workforce	ITALY		BRAZIL		TOTAL		
	31.12.2006	31.12.2005	31.12.2006	31.12.2005	31.12.2006	31.12.2005	Changes
Senior management	75	75			75	75	--
Middle management	439	403			439	403	36
Office staff	1,857	1,813	80	53	1,937	1,866	71
Workers	1,104	1,098			1,104	1,098	6
TOTAL	**3,475**	**3,389**	**80**	**53**	**3,555**	**3,442**	**113**

The number of employees at year end is net of resignations with effect up to year end (44 resignations at 31 December 2006, 59 at 31 December 2005).

The increase in the total number of Group employees at year end was due to the 24 November 2006 acquisition of Edison Rete (RTM1) and AEM Trasmissione (RTM2) and the consolidation of the organizational structure of the Brazilian companies to support the stock market listing and development plan.

RTM1 had 81 employees at the closing date and 80 employees at 31 December 2006 (two senior managers, six middle managers, 33 office staff members and 39 workers), RTM2 had 27 employees both at the closing date and year end (1 senior manager, 2 middle managers, 8 office staff members and 16 workers).

Training and Development

The group completed the main initiatives of its training and development plan put in place to support the post-Terna/GRTN business activity integration phase.

It confirmed its significant commitment to consolidating and developing specialized expertise and operating skills to sustain excellence in performance and focus intensely on service continuity and security.

Specific focus was put on defining and implementing the training and development systems, in line with Group logic and policies and by integrating certain specific local aspects with regard to Terna Participações.

Managerial incentive systems

The 2006 MBO plan was established, with the assignment of annual targets for senior and middle management. The 2006 Terna SpA stock option plan was approved (Resolution of 21 December 2005) and will entail the allotment of options to senior managers of the company who fill key roles in the achievement of the group's strategic targets. Another long-term cash-based incentive plan was approved for senior managers who are not beneficiaries of the stock option plan.

On 14 December 2006, following the approval of the shareholders during the extraordinary meeting held on 5 October 2006, the Board of Directors of Terna Participações SA resolved to implement its first stock option plan for three Terna Participações SA managers. The plan offers a total of 163,472 units that can be exercised by 31 December 2011, provided that specific business performance targets have been reached. More in general, with respect to the compensation system, during the year a project was completed whereby all organizational positions were weighted to support the definition of human resource compensation policies, also given the new organizational structure.

RELATED PARTY TRANSACTIONS

Related party transactions carried out by the Terna Group during the year included those with the associate Cesi SpA and the employee pension funds FONDENEL and FOPEN.
The group's corporate governance rules, which are detailed in the specific section of the Directors' Report on the separate financial statements of Terna SpA, to which reference should be made, establish the necessary conditions to ensure that related party transactions are carried out correctly, in terms of procedure and substance.
Related party transactions are indicated in the notes to the individual financial statements captions.
Reference should be made to the summary included in "Related party transactions".

Moreover, transactions carried out with members of the parent's Board of Directors and Board of Statutory Auditors, specifically with respect to fees, bonuses and other incentives, are detailed in the notes to the caption "Services".

Shares held by Directors, Statutory Auditors, General Managers and Key Managers

As required by the provision of Article 79 of Consob Resolution no. 11971/99, the following table lists the shares of Terna SpA and the companies under its control held by Directors, Statutory Auditors, General Managers and Key Managers, in addition to their spouses (unless legally separated) and minor children, either directly or indirectly through subsidiaries, trustees or nominees, as per the shareholders' book, communications received or other information obtained from the members of the Boards of Directors and Statutory Auditors, General Managers and Key Managers. These include all those persons who, in 2006, filled the office of Director, Statutory Auditor, General Manager and Key Managers.

DISCLOSURE ON THE SHARES HELD BY DIRECTORS AND THE STATUTORY AUDITORS

Name and Surname	Company in which investiment is held	Number of shares held at the end of the previous year (2005)	Number of shares acquired (in 2006)	Number of shares sold (in 2006)	Number of shares held at the end of the current year (2006)	Type of ownership (1)
Luigi Roth	Terna SpA	0	0	0	0	-
	Terna Participações	-	1	0	1	ownership
Flavio Cattaneo	Terna SpA	0	0	0	0	-
	Terna Participações	-	1	0	1	ownership
Luigi De Paoli	Terna SpA	7,805 (2)	1,536	0	9,341(3)	ownership
Mario Garraffo	Terna SpA	0	0	0	0	-
Claudio Machetti (4)	Terna SpA	0	0	0	0	-
Salvatore Machì	Terna SpA	0	0	0	0	-
Carmine Macrì	Terna SpA	0	0	0	0	-
Piero Giuseppe Maranesi	Terna SpA	0	0	0	0	-
Vittorio Rispoli (5)	Terna SpA	0	0	0	0	-
Franco Smurro	Terna SpA	0	0	0	0	-
Massimo Ponzellini (6)	Terna SpA	2,000	0	0	2,000	ownership
Massimo Romano (7)	Terna SpA	13,200	0	0	13,200	ownership
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	ownership
Vito Di Battista	Terna SpA	0	0	0	0	-
Bruno Franceschetti	Terna SpA	0	0	0	0	-

(1) This column - which is in addition to the format provided by appendix 3C) of Article 79 of CONSOB Resolution no. 11971/99 to indicate the information required - is shown if the investment is held as a result of ownership, a pledge, beneficial ownership, on deposit, as collateral, etc.
(2) including: 5,204 personally and 2,601 held by his spouse.
(3) including: 6,740 personally and 2,601 held by his spouse.
(4) In office since 21 March 2007.
(5) In office since 13 July 2006.
(6) In office up to 3 July 2006.
(7) In office up to 16 March 2007.

OUTLOOK

The group will continue to pursue compliance with the provisions of the Prime Minister's Decree of 11 May 2004 in 2007, with specific focus on the unification of the National Transmission Grid through the acquisition of additional portions of the grid owned by others.

Furthermore, to optimize company operations, the group will merge RTM1 and RTM2 into RTL.

The parent will continue to seek investment opportunities abroad, with particular focus on profitability and low risk profiles.

In terms of regulations applicable to Terna, in 2007, the Electricity and Gas Regulator is expected to adopt certain measures that could have a direct impact on the parent.

Firstly, as anticipated in Resolution no. 208/06 launching the procedure for the creation of tariff measures, in 2007, the Regulator will establish new tariff regulations with effect for the third regulatory period from 2008 to 2011. These will apply to Terna, among others.

Secondly, as the Regulator announced in the 32/06 consultation document issued in late 2006, 2007 could see the start-up of experimental incentives for Terna in the procurement of dispatching resources and their use.

These measures, which the company plans to take full advantage of, will ensure and increase the creation of value for shareholders.

Brazil

Terna will continue to evaluate expanding its future growth potential in Brazil, while reducing its direct exposure to risk. In addition, it will merge Novatrans into TSN.

Human Resources

A plan is currently being prepared to integrate RTM1 and RTM2 employees into Terna SpA's local organizational structures. The integration will take place in the first half of 2007 and will be supported by a specific training plan for the resources of the organizational units involved.

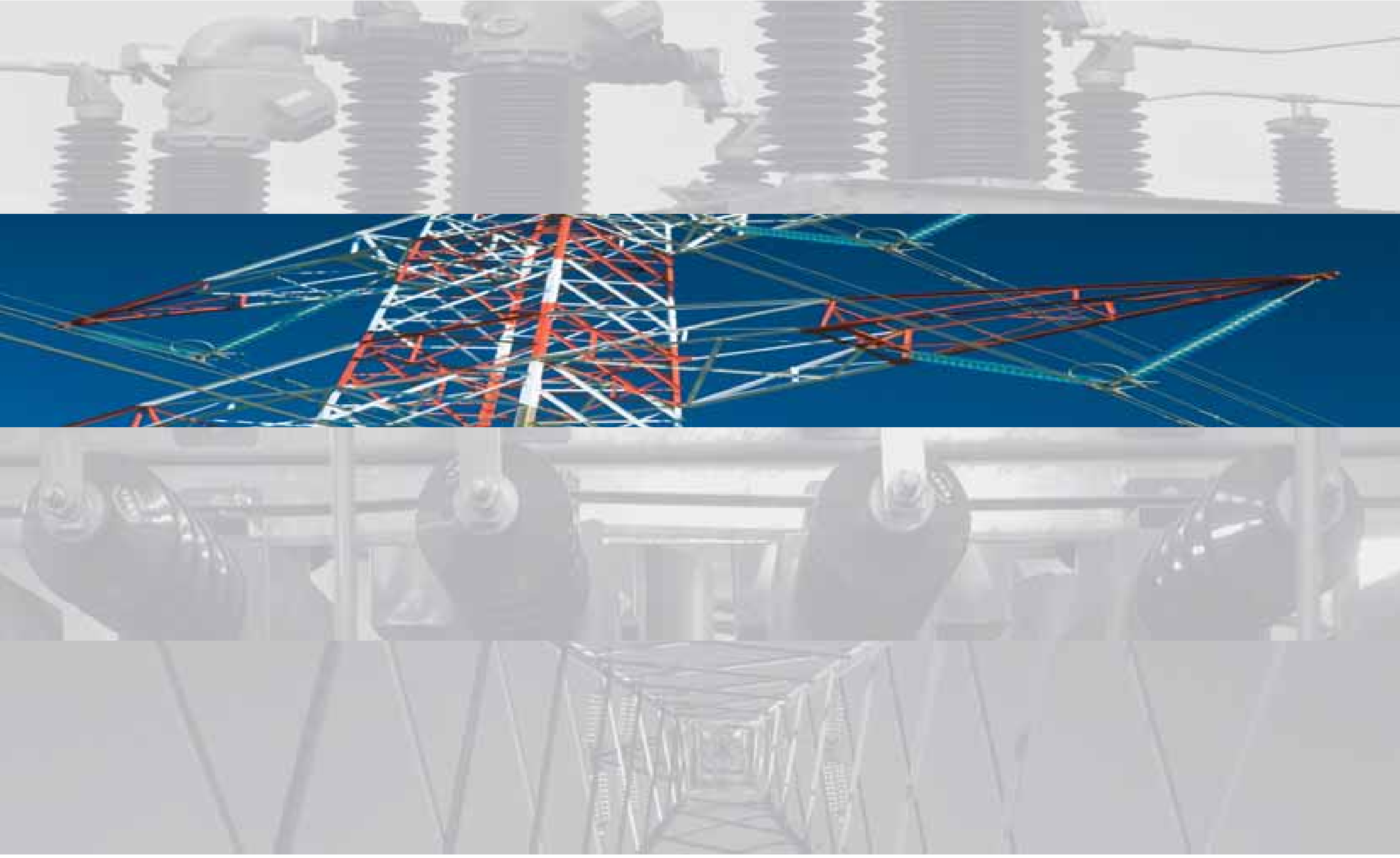
OTHER INFORMATION

Personal data protection code (Legislative Decree no. 196 of 30 June 2003)

Terna SpA prepared the personal data protection document in 2003 and updated it in 2006, in accordance with Presidential Decree no. 318/1999.
It will next be updated at 31 March 2007, within the term provided for by Legislative Decree no. 196 of 30 June 2003.

Treasury shares

The company does not hold any treasury shares or shares of its parent, nor has it acquired or sold any during the year, either directly or indirectly.



CONSOLIDATED FINANCIAL STATEMENTS 2006

INCOME STATEMENT

TERNA GROUP CONSOLIDATED - INCOME STATEMENT

In millions of euros	Note	2006	2005	Changes
A) REVENUES				
Revenues from goods and services	1	1,279.5	1,058.7	220.8
Other revenues	2	28.3	23.1	5.2
of which from related parties		0.1	0.2	-0.1
Total revenues		**1,307.8**	**1,081.8**	**226.0**
B) OPERATING EXPENSES				
Raw materials and consumables	3	18.7	25.4	-6.7
Services	4	145.3	118.8	26.5
of which to related parties		0.9	1.8	-0.9
Personnel expenses	5	242.0	201.7	40.3
of which to related parties		1.7	1.3	0.4
Amortization, depreciation and impairment losses	6	224.6	175.2	49.4
Other operating expenses	7	26.5	45.7	-19.2
Capitalized internal work	8	-36.8	-26.5	-10.3
Total expenses		**620.3**	**540.3**	**80.0**
A-B OPERATING PROFITS		**687.5**	**541.5**	**146.0**
C) FINANCIAL INCOME/EXPENSES				
Financial income	9	60.7	35.4	25.3
of which non-recurring		31.4	0.0	31.4
Financial expenses	9	-129.3	-117.4	-11.9
Share of profits/(losses) of equity-accounted investees	10	0.0	1.8	-1.8
D) PROFITS BEFORE TAXES		**618.9**	**461.3**	**157.6**
E) INCOME TAXES	**11**	**249.1**	**163.4**	**85.7**
F) PROFITS FOR THE YEAR		**369.8**	**297.9**	**71.9**
Profits for the year attributable to minority interests		**3.5**	**0.0**	**3.5**
Profits for the year attributable to the shareholders of the parent		**366.3**	**297.9**	**68.4**
Basic earnings per share	12	0.185	0.149	0.036
Diluted earnings per share	12	0.184	0.148	0.036

BALANCE SHEET ASSETS

TERNA GROUP CONSOLIDATED - BALANCE SHEET ASSETS

In millions of euros	Note	31.12.2006	31.12.2005	Changes
A) NON-CURRENT ASSETS				
Property, plant and equipment	13	5,159.0	4,646.3	512.7
Goodwill	14	139.9	154.7	-14.8
Intangible assets	15	159.2	151.5	7.7
Deferred tax assets	16	62.1	57.3	4.8
Equity-accounted investees	17	6.4	6.4	0.0
Non-current financial assets	18	12.0	106.1	-94.1
Other non-current assets	21	6.4	7.0	-0.6
Total non-current assets		**5,545.0**	**5,129.3**	**415.7**
B) CURRENT ASSETS				
Inventories	19	25.6	21.2	4.4
Trade receivables	20	1,182.1	1,026.2	155.9
of which from related parties		0.0	0.1	-0.1
Current financial assets	18	2.2	4.4	-2.2
Cash and cash equivalents	22	200.4	76.6	123.8
Other current assets	21	34.0	32.9	1.1
Total current assets		**1,444.3**	**1,161.3**	**283.0**
TOTAL ASSETS		**6,989.3**	**6,290.6**	**698.7**

BALANCE SHEET LIABILITIES

TERNA GROUP CONSOLIDATED - BALANCE SHEET LIABILITIES

In millions of euros	Note	31.12.2006	31.12.2005	Changes
C) EQUITY ATTRIBUTABLE TO THE SHAREHOLDERS OF THE PARENT				
Share capital		440.0	440.0	0.0
Other reserves		832.9	811.1	21.8
Retained earnings		475.7	453.2	22.5
Interim dividend		-106.0	-100.0	-6.0
Profits for the year		366.3	297.9	68.4
Total equity attributable to the shareholders of the parent	23	**2,008.9**	**1,902.2**	**106.7**
D) MINORITY INTERESTS		150.0	0.0	150.0
Total equity		**2,158.9**	**1,902.2**	**256.7**
E) NON-CURRENT LIABILITIES				
Long-term loans	24	2,367.9	2,309.1	58.8
Termination benefits and other employee-related provisions	25	166.1	168.2	-2.1
Provisions for contingencies and charges	26	59.1	37.4	21.7
Deferred tax liabilities	27	454.5	467.7	-13.2
Non-current financial liabilities	24	6.2	29.0	-22.8
Other non-current liabilities	28	170.8	176.2	-5.4
Total non-current liabilities		**3,224.6**	**3,187.6**	**37.0**
F) CURRENT LIABILITIES				
Short-term loans	24	50.0	55.0	-5.0
Current portion of long-term loans	24	71.1	58.3	12.8
Trade payables	29	1,280.6	951.4	329.2
of which to related parties		4.5	2.7	1.8
Tax liabilities	29	75.3	14.4	60.9
Current financial liabilities	24	16.0	16.8	-0.8
Other current liabilities	29	112.8	104.9	7.9
of which to related parties		0.7	0.7	0.0
Total current liabilities		**1,605.8**	**1,200.8**	**405.0**
TOTAL EQUITY AND LIABILITIES		**6,989.3**	**6,290.6**	**698.7**

STATEMENT OF CHANGES IN CONSOLIDATED EQUITY

In millions of euros	Share capital	Legal reserve	Translation reserve GOODWILL	Translation reserve OTHER	Retained earnings	Other reserves	Interim dividend	Profit for the year	**Equity attributable to the shareholders of the parent**	Share capital and reserves attributable to minority interests	Profit for the year attributable to minority interests	**Equity attributable to minority interests**	**Total equity**
	CONSOLIDATED SHARE CAPITAL AND RESERVES												
AT 31 DEC. 2004	**440.0**	**84.5**	**1.5**	**-13.2**	**-34.5**	**1.139.7**	**-90.0**	**231.1**	**1,759.1**	**0.0**	**0.0**	**0.0**	**1759.1**
ALLOCATION OF 2004 PROFITS									-				-
Legal reserve		3.5			-2.4			-1.1	-				-
2004 interim dividend						90.0	-90.0	-				-	
2004 final dividend								-140.0	**-140.0**				**-140.0**
Translation of financial statements of foreign companies			37.2	41.8					**79.0**				**79.0**
Reduction in share capital								-				-	
Other changes					422.8	-416.6			**6.2**				**6.2**
Profits for the year								297.9	**297.9**				**297.9**
2005 interim dividend							-100.0		**-100.0**				**-100.0**
AT 31 DEC. 2005	**440.0**	**88.0**	**38.7**	**28.6**	**385.9**	**723.1**	**-100.0**	**297.9**	**1,902.2**	**0.0**	**0.0**	**0.0**	**1,902.2**

In millions of euros	Share capital	Legal reserve	Translation reserve GOODWILL	Translation reserve OTHER	Retained earnings	Other reserves	Interim dividend	Profits for the year	**Equity attributable to the shareholders of the parent**	Share capital and reserves attributable to minority interests	Profits for the year attributable to minority interests	**Equity attributable to minority interests**	**Total equity**
	CONSOLIDATED SHARE CAPITAL AND RESERVES												
AT 31 DEC. 2005	**440.0**	**88.0**	**38.7**	**28.6**	**385.9**	**723.1**	**-100.0**	**297.9**	**1.902.2**	**0.0**	**0.0**	**0.0**	**1902.2**
ALLOCATION OF 2005 PROFITS									-			-	**0.0**
Retained earnings					37.9			-37.9	-			-	**0.0**
2005 interim dividend							100.0	-100.0	-			-	**0.0**
2005 final dividend								-160.0	**-160.0**			-	**-160.0**
Translation of financial statements of foreign companies			-2.5	-5.2					**-7.7**	-3.6		**-3.6**	**-11.3**
Terna Part listing			-13.2						**-13.2**	138.8	9.9	**148.7**	**135.5**
Other changes					5.5	21.8			**27.3**	1.4		**1.4**	**28.7**
Profits for the year								366.3	**366.3**		3.5	**3.5**	**369.8**
2006 interim dividend							-106.0		**-106.0**			-	**-106.0**
AT 31 DEC. 2006	**440.0**	**88.0**	**23.0**	**23.4**	**429.3**	**744.9**	**-106.0**	**366.3**	**2.008.9**	**136.6**	**13.4**	**150.0**	**2.158.9**

CONSOLIDATED STATEMENT OF RECOGNIZED INCOME AND EXPENSES

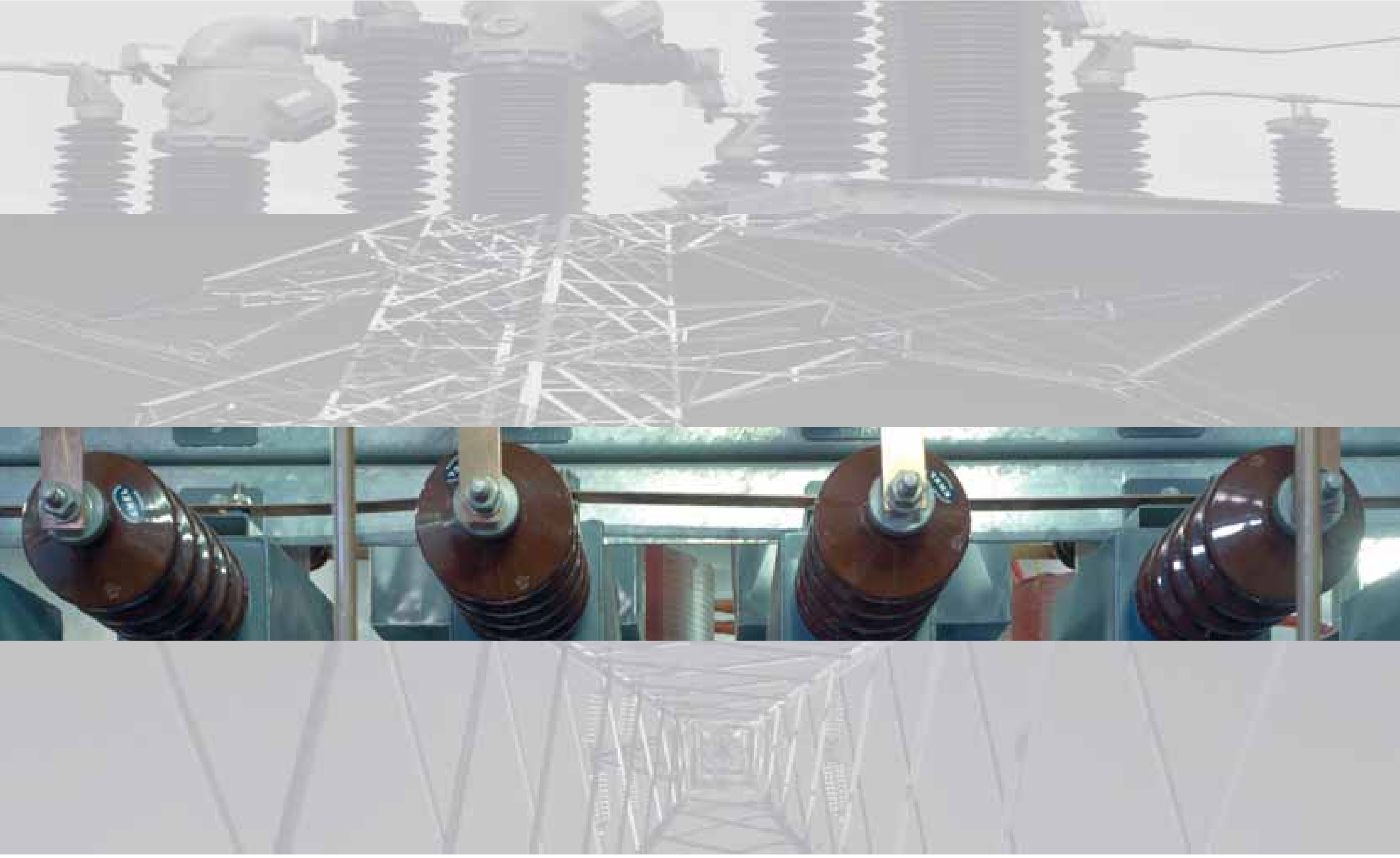
In millions of euros	2006	2005
Exchange rate differences	-11.3	79.0
Reduction in the translation reserve following the listing of Terna Participações SA	-13.2	-
Brazilian tax incentive	14.6	5.4
Effective portion of changes in the fair value of cash flow hedges	7.8	0.7
Actuarial gains on defined benefit plans	5.5	-
Exercise of stock options	0.8	0.2
Income and expenses recognized directly in equity	**4.2**	**85.3**
Profits for the year	369.8	297.9
Recognized income and expenses	374.0	383.2
Attributable to:		
Shareholders of the parent	372.7	383.2
Minority interests	1.3	-

CONSOLIDATED CASH FLOW STATEMENT*

TERNA GROUP CONSOLIDATED CASH FLOW STATEMENT

In millions of euros	2006	2005
Profits for the year attributable to the shareholders of the parent	**366.3**	**297.9**
ADJUSTMENTS FOR		
Amortization, depreciation, impairment losses/(reversals of impairment losses) on property, plant and equipment, investment property and intangible assets, net of grants related to plant taken to profits or losses for the year	200.4	164.9
Exchange rate gains/losses (including cash and cash equivalents)	2.0	-7.6
Accruals to provisions (including employee-related provisions) and impairment losses	48.0	32.8
(Gains)/losses on disposals of property, plant and equipment	0.6	2.6
Financial (income)/expenses	73.9	98.8
Income taxes	249.1	169.0
Cash flows generated by/(used in) operating activities, before changes in net working capital	**940.3**	**758.4**
Decrease in provisions (including employee-related and tax provisions)	-24.3	-25.1
(Increase)/decrease in inventories	-4.4	-1.6
(Increase)/decrease in trade receivables and other current assets	-163.0	-767.5
Increase/(decrease) in other non-current liabilities	-4.5	14.5
(Increase)/decrease in other non-current assets	-108.0	-55.0
Increase/(decrease) in trade payables and other liabilities	477.0	664.8
Interest income and other financial income received	115.2	61.5
Interest expenses and other financial expenses paid	-216.3	-146.9
Income taxes paid	-243.0	-173.8
Cash flows generated by/(used in) operating activities [a]	**769.0**	**329.3**
Investments in property, plant and equipment, net of recognized grants	-312.7	-271.3
Acquisition of Munirah, RTM1 and RTM2 assets	-416.7	
Revenues from sale of property, plant and equipment	4.5	1.8
Investments in intangible assets	-26.2	-1.6
Goodwill on acquisition of Munirah, RTM1 and RTM2	-40.4	
Group proceeds from the Brazil IPO (OTC market and increase in the nominal value of Terna Part shares)	115.4	
Acquisition of TSO and RTL business activities		-104.8
Cash flows generated by/(used in) investing activities [b]	**-676.1**	**-375.9**
Recognition of equity, net of minority interests and the portion sold by the group in the Brazil IPO	105.3	
Changes in reserves	19.5	7.3
Changes in medium/long-term financial payables (including short-term portions), net of fair value hedges	155.3	45.7
Acquisition of Munirah loan	23.1	
Changes in short-term financial payables and term credit lines	-5.0	66.3
Dividends paid	-266.0	-240.0
Cash flows generated by/(used in) financing activities [c]	**32.2**	**-120.7**
Effect of change in exchange rates on cash and cash equivalents [d]	**-1.3**	**12.1**
INCREASE/(DECREASE) IN CASH AND CASH EQUIVALENTS [A+B+C+D]	**123.8**	**-155.2**
Opening cash and cash equivalents	**76.6**	**231.8**
Closing cash and cash equivalents	**200.4**	**76.6**

* Reference should be made to the specific paragraph in the notes "NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT" for comments.



NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

A) ACCOUNTING POLICIES AND MEASUREMENT CRITERIA

Introduction

Terna SpA has registered offices in Via Arno, 64 Rome, Italy. Its consolidated financial statements as of and for the year ended 31 December 2006 include its separate financial statements and those of its subsidiaries (the "Group"), as well as the group's investment in associates. The subsidiaries included in the consolidation scope are listed below.

These consolidated financial statements were approved for publication by the Directors on 21 March 2007. The Board of Directors also authorized the Chairman and CEO to make any formal changes to the consolidated financial statements and any integrations and adjustments to the sections relating to subsequent events that should be necessary up to the date of approval by the shareholders (23 and 24 May 2007).

International Financial Reporting Standards

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) and the Standing Interpretations Committee (SIC), endorsed by the European Commission ("IFRS") at that date.
These consolidated financial statements have been prepared also considering the provisions of Legislative Decree no. 38 of 28 February 2005, the provisions of the Italian Civil Code and Consob Resolutions no. 15519 and no. 15520 of 27 July 2006, as well as Consob Communication no. DEM/6064293 of 28 July 2006.

Presentation criteria

The consolidated financial statements are comprised of the balance sheet, income statement, cash flow statement, statement of changes in consolidated equity, statement of recognized income and expenses and the notes thereto.
In the balance sheet, assets and liabilities are classified on a current/non-current basis, with specific mention of assets and liabilities held for sale. Current assets, which include cash and cash equivalents, are those held for realization, sale or consumption in the group's normal operating cycle. Current liabilities are those

expected to be settled in the group's normal operating cycle or within one year from the balance sheet date. The consolidated income statement is classified on the basis of the nature of costs, while the cash flow statement has been prepared using the indirect method.

These consolidated financial statements are presented in euros, and all figures are shown in millions of euros, unless otherwise indicated.

The consolidated financial statements have been prepared using the historic cost method, with the exception of captions that are recognized at fair value in accordance with IFRS, as indicated in the accounting policies for each caption.

Use of estimates

The preparation of the consolidated financial statements in accordance with IFRS requires the use of estimates and assumptions that affect the carrying amounts of assets and liabilities and related disclosures, in addition to contingent assets and liabilities at the reporting date. The estimates and associated assumptions are based on previous experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying amounts of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates. The estimates and underlying assumptions are reviewed on an ongoing basis.

Revisions of accounting estimates are recognized in the year in which the estimate is revised if the revision affects only that year, or in the year of the revision and future years if the revision affects both current and future years.

The critical areas for key estimates and assumptions used by management in applying IFRS endorsed by the European Commission that could have significant effects on the consolidated financial statements or that could give rise to risks that would entail significant adjustments to the carrying amounts of assets and liabilities in subsequent years are summarized below.

Employee benefits

The liability for employee benefits paid upon or following termination of employment in relation to defined benefit plans or other long-term benefits is recognized net of any plan assets and is measured on the basis of actuarial assumptions, estimating the amount of future benefits that employees have vested at the reporting date.

Provisions for contingencies and charges

Accruals to the provisions for contingencies and charges are recognized when, at the reporting date, there is a legal or constructive obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the effect is material, accruals are measured by discounting estimated future cash flows at a discount rate that reflects current market assessments of the time value of money and the risks specific to the liability.

Provision for bad debts

Trade receivables are initially recognized net of any impairment losses relating to sums considered non recoverable, which are taken to the specific provision for bad debts. Impairment losses are measured on the basis of the present value of estimated future cash flows, discounted at the original effective interest rate.

Recoverable amount of non-current assets

Property, plant and equipment and intangible assets are analyzed at least once a year to check for indications of impairment. If there is an indication that an asset may be impaired, its recoverable amount is estimated. Recoverable amount is the higher of an asset’s fair value, net of costs to sell and its value in use, measured by discounting estimated future cash flows considering available information at the time of estimate and on the basis of subjective assessments of the performance of future variables, such as prices, costs, demand growth rates, production profiles - and discounted at a rate that reflects current market assessments of the time value of money with respect to the investment period and the risks specific to the asset.

Subsidiaries and the consolidation scope

The consolidation scope includes the parent Terna SpA and the companies over which the parent has the power to directly or indirectly govern financial and operating policies as to obtain benefits from their activities. In assessing whether or not the parent has control, potential voting rights that are presently exercisable or convertible are also considered.

The financial statements of subsidiaries are included in the consolidated financial statements on a line-by line basis from the date when the parent gains control until the date when such control ceases.

Below is a list of the companies included in the consolidation scope:

Company	Registered offices	Business activity	Share capital	Currency	% of ownership	Consolidation method
Companies controlled directly by Terna SpA						
Terna Participações SA	Rio de Janeiro (Brazil)	Holding of investments in other companies that operate in the electrical energy transmission sector	1,309,403,148	real	66%	Line-by-line
RTL Rete Trasmissione Locale	Rome	Construction and maintenance of electrical energy transmission grids	20,600,000	euro	100%	Line-by-line
Companies controlled indirectly through RTL SpA						
Rete Trasmissione Milano 1	Rome	Construction and maintenance of electrical energy transmission grids	106,778,200	euro	100%	Line-by-line
Rete Trasmissione Milano 2	Rome	Construction and maintenance of electrical energy transmission grids	76,596,900	euro	99.99%	Line-by-line
Companies controlled indirectly through Terna Participações SA						
TSN Transmissora Sudeste Nordeste SA (Brazil)	Rio de Janeiro (Brazil)	Construction and maintenance of electrical energy transmission grids	250,000,000	real	66%	Line-by-line
Novatrans Energia SA	Rio de Janeiro (Brazil)	Construction and maintenance of electrical energy transmission grids	373,135,465	real	66%	Line-by-line

The change in the consolidation scope was due to the acquisition of investments in Rete Trasmissione Milano 1 SpA (“RTM1”) and Rete Trasmissione Milano 2 SpA (“RTM2”) by the subsidiary RTL on 24 November 2006. Furthermore, the percentage of ownership in the Brazilian companies decreased (from 100% at 31 December 2005 to 66%) following the listing of the Brazilian subsidiary Terna Participações on the São Paulo stock exchange in the second half of 2006.

Associates

Investments in associates are those over which the Terna Group has significant influence but which are neither subsidiaries nor joint interests. In assessing whether or not the parent has significant influence, potential voting rights that are presently exercisable or convertible are also considered.
These investments are initially recognized at acquisition cost and subsequently measured using the equity method. Profits and losses attributable to the shareholders of the parent are recognized from the date when it begins to exercise significant influence until that influence ceases.
In the event that an investee's losses attributable to the shareholders of the parent exceed that investments' carrying amount, the latter is written off and any excess is recognized in a specific provision, where the parent is required to meet the legal or construction obligations of the investee or, in any case, to cover its losses.

Consolidation policies

All financial statements of investees used to prepare the consolidated financial statements are as of and for the year ended 31 December 2006. They have been adjusted, where necessary, to align them with the parent's accounting policies.
In the preparation of the consolidated financial statements, intercompany balances, transactions, revenues and costs are fully eliminated, net of the related tax effect, where material ("consolidation on a line-by-line basis"). Unrealized gains and losses with associates are eliminated in proportion to the group's share therein. In both cases, unrealized losses are eliminated, unless they represent impairment.

Translation of foreign currency captions

The financial statements of each consolidated company are prepared using the functional currency with reference to the economic context in which each company operates.
In these financial statements, all transactions in currencies other than the functional currency are recognized at the exchange rate ruling on the date of the transaction. Monetary assets and liabilities in currencies other than the functional currency are subsequently adjusted at the exchange rate ruling at year end. Any exchange rate differences are taken to profits or losses.
Non-monetary assets and liabilities in foreign currency stated at historic cost are converted at the exchange

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

Translation of financial statements in foreign currency

For the purposes of the consolidated financial statements, profits and losses, assets and liabilities are expressed in euros, which is the parent Terna SpA's functional currency.
For the purposes of preparing the consolidated financial statements, the financial statements of investees with a functional currency other than the euro, including goodwill and consolidation adjustments, are converted into euros at the exchange rate ruling at the balance sheet date. Income statement figures included in these financial statements are converted at the average exchange rate of the year. Any resulting exchange rate differences are taken directly to equity, and are classified separately in a specific equity reserve. This reserve is then released to profits or losses when the investment is sold.

Business combinations

All business combinations, including acquisitions of minority interests in entities over which control is already held, are recognized using the purchase method, where purchase cost is equal to the fair value, at the date of exchange, of assets given and liabilities incurred or assumed, plus any costs directly attributable to the combination. This cost is allocated by recognizing the identifiable assets, liabilities and contingent liabilities of the acquired business at fair value. If the purchase cost exceeds the fair value of net assets acquired and attributable to the group, this excess amount is recognized as goodwill or, if negative, taken to profits or losses, after having verified once again that the current values of assets and liabilities acquired and the purchase price have been measured correctly.
Decreases in minority interests, following sale or dilution, in subsidiaries, without losing control, are accounted for accordingly. As a result, the portion of losses or gains realized on the disposal in excess of goodwill subsequently realized is taken to profits or losses.

Property, plant and equipment

Property, plant and equipment are recognized at historic cost, including directly costs attributable to putting the asset in the condition necessary for it to be capable of operating in the manner for which it was acquired. In the event of legal or constructive obligations, cost also includes the present value of the estimated cost of disposal or removal of the asset. The corresponding liability is recognized in the provisions for contingencies and charges. Borrowing costs related to loans taken out to acquire assets are taken to profits or losses in the year to which they refer. Expenses incurred after purchase are recognized as an increase in the carrying amount of the asset to which they relate if it is probable that the future benefits of that cost will flow to the group and if the cost can be reliably measured. All other costs are recognized in profits or losses when incurred.

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

Certain assets that were revalued at 1 January 2004 (transition date) or previously are recognized at the revalued amount, which is considered deemed cost at the date of the revaluation.

Property, plant and equipment are shown net of accumulated depreciation and any impairment losses, which are measured as described below. Depreciation is calculated on a straight-line basis over the estimated useful life of the asset, which is reviewed annually, with revisions applied on a prospective basis. The depreciation of assets under construction begins when the assets become available for use.

Liabilities associated with items of property, plant and equipment are taken to a specific provision as a balancing entry to the related asset. The amount is taken to profits or losses through the depreciation of the asset.

The main depreciation rates calculated on the basis of the related asset's useful life are as follows:

DEPRECIATION RATE

Civil and industrial buildings	2.50% - 4.00%
Power lines	2.50% - 4.50%
Transformation stations:	
- Electrical machinery	2.00% - 3.00%
- Electrical devices and equipment	2.80 - 4.50%
- Automated and control systems	5.00 - 6.70%
Central systems for remote conduction and control:	
- Devices, electrical equipment and ancillary plants	5.00%
- Electronic calculators	10.00%

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

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

Leases in which the lessor maintains substantially all the risks and rewards of ownership are classified as operating leases. Costs related to operating leases are taken in full to profits or losses over the term of the lease.

Terna

The concession granted to the parent, with effect from 1 November 2005, on a free basis by the Minister of Production Activities, to carry out electrical energy transmission and dispatching activities in Italy, runs for twenty-five years and is renewable for another twenty-five years. Under the provisions of Articles 18 and 19 of the Decree issued by the Ministry of Production Activities on 20 April 2005, in the event of termination and revocation, or expiry of the concession, the Ministry has the right to purchase assets used directly for the transmission and dispatching activities included in the concession owned by the concession-holder, with the exclusion of plants (lines and stations) that make up the National Transmission Grid. If the Ministry decides to purchase the concession-holder's assets, it will pay the latter an amount, agreed upon by the parties, calculated on the basis of adequate parameters, averaging out the value of the assets with their profitability.

Brazil

Similarly to that described above with respect to Terna's concession, the Brazilian companies hold free concessions to use the portion of the electrical energy transmission grid they own. The term of the concession is thirty years from the grant date (2003) and the Brazilian companies have no obligation to return the plants (lines and stations) that make up the portion of the transmission grid they own upon expiry of the concession. Upon expiry, the plants, rights and privileges of the concession will be transferred to the Federal Government, upon payment of an indemnity commensurate with the undepreciated portions of investments in the related assets made to ensure guaranteed service continuity.

Accordingly, the assets directly related to the transmission and dispatching activities, including plants (lines and stations) that make up the portion of the electrical energy transmission grid owned by the group are classified as property, plant and equipment and are depreciated over their useful lives.
As specified further down, in November 2006, the International Financial Reporting Interpretation Committee ("IFRIC") issued IFRIC Interpretation 12 *Service Concession Arrangements*. The parent is currently evaluating the applicability and any effects that would arise from the adoption of this accounting policy.

Intangible assets

Intangible assets, which all have finite useful lives, are recognized at cost and shown net of accumulated amortization and any impairment losses, measured as described below.
Amortization is calculated on a straight-line basis over the estimated useful life of the related asset, which is reviewed annually. Any revisions are applied on a prospective basis.
Amortization begins when the asset becomes available for use.
Intangible assets are substantially comprised of the exclusive concession to carry out electrical energy transmission and dispatching activities and other intangible assets. In particular, the parent acquired the concession for electrical energy transmission and dispatching activities in Italy on 1 November 2005 when it acquired the TSO business activity. As established in the Decree issued by the Ministry of Production Activities on 20 April 2005, this concession runs for twenty-five years from the date of effective transfer of the activities, functions, assets and legal arrangements of the concession from GSE (formerly GRTN) to Terna SpA.

This intangible asset was initially recognized at cost, which reflected fair value.

Other intangible assets mainly relate to the following:

the development and innovation of application software to manage the energy invoicing process;

the development and innovation of application software to protect the electrical energy system;

software applications related to the development of the power exchange, particularly relating to the registration of operators, consumption units and the development of foreign procedures.

These are amortized over their estimated residual useful lives, which are normally three years, given their rapid obsolescence.

Goodwill

Goodwill arising from the acquisition of subsidiaries is allocated to each of the identified cash-generating units ("CGU"). The identified CGUS are the companies that hold concessions for electrical energy transmission and dispatching activities. Goodwill is not amortized after initial recognition. Rather, it is adjusted to reflect impairment losses, measured as described below. Goodwill relating to investments in associates is included in the carrying amount of those companies. Where negative goodwill arises, it is taken to profits or losses at the time of the acquisition.

In the adoption of IFRS endorsed by the European Commission, the group decided to restate only those business combinations that occurred after the transition date (1 January 2004). Goodwill arising on acquisitions before that date corresponds to the amount recognized using the previous accounting policies.

Impairment losses

Property, plant and equipment and intangible assets with finite useful lives are tested at least once a year to check for indications of impairment. If there is an indication that an asset may be impaired, its recoverable amount is estimated.

The recoverable amount of goodwill and intangible assets with indefinite useful lives, where present, as well as intangible assets not yet available for use, is estimated annually.

Recoverable amount is equal to the greater of fair value less costs to sell and value in use.

Value in use is measured considering the estimated future cash flows discounted at a pre-tax rate that reflects the time value of money for the investment period and risks specific to the asset. If the intangible asset does not generate cash inflows that are largely independent, the asset's recoverable amount is calculated as part of the cash-generating (CGU) unit to which it belongs.

An impairment loss is recognized in the income statement when the asset's carrying amount or the net invested capital of the CGU to which it belongs, is greater than its recoverable amount.

Impairment losses of CGUs are first taken as a reduction in the carrying amount of any allocated goodwill and then as a reduction in other assets of the CGU on a *pro rata* basis. Except for goodwill, impairment losses may be reversed if there is an indication that the impairment loss no longer exists or when there is a change in the methods used to measure recoverable amount.

Inventories

Inventories are stated at the lower of purchase cost and net realizable value. Cost is calculated as the weighted average cost, including related charges.

Contract work in progress

When the profits or losses of a contract can be reliably estimated, the related contract costs and revenues are recognized separately in profits or losses on a percentage of completion basis. Progress is measured based on the work carried out. Differences between the value of completed contracts and payments on account received are recognized under balance sheet assets or liabilities, considering any impairment losses on the work carried out so as to take into account the risks of customers' refusal to recognize the work performed.

Expected contract losses are immediately taken to profits or losses under contract costs.

Contract costs include all those costs that relate directly to the specific contract, as well as fixed and variable costs incurred as part of normal operations.

Financial instruments

Financial assets

Any financial assets that the company has the positive intention and ability to hold to maturity are recognized at cost at the “settlement date”, which is the fair value of the initial consideration given in exchange, including transaction costs. They are subsequently measured at amortized cost, using the effective interest method, net of any impairment losses, which are determined as the lower of the asset’s carrying amount and the present value of estimated future cash flows, discounted using the original interest rate. Financial assets are derecognized when, following their transfer or settlement, the company is no longer involved in their management and no longer holds the risks and rewards of the transferred or settled instruments.

Trade receivables

Trade receivables are initially recognized at fair value and subsequently measured at amortized cost, using the effective interest method, and net of any impairment losses due to sums considered non-recoverable, which are taken to the specific provision for bad debts. Impairment losses are calculated on the basis of the present value of estimated future cash flows, discounted using the initial effective interest rate.

Receivables with due dates that fall under normal commercial terms are not discounted.

Cash and cash equivalents

Cash and cash equivalents are stated at nominal value. They include cash on hand, i.e., amounts that are available on demand or with a very short maturity, subject to an insignificant risk and without redemption expenses.

Trade payables

Trade payables are stated at amortized cost. If their due date falls under normal commercial terms, they are not discounted.

Financial liabilities

Financial liabilities are initially recognized at the settlement date and measured at fair value, net of directly related transaction costs.

Subsequently, financial liabilities are measured at amortized cost, using the original effective interest method. If the liabilities are subject to fair value hedges, they are adjusted to reflect changes in fair value with respect to the hedged risk.

Derivative financial instruments

Derivatives are recognized at fair value at the trade date and classified as hedges if the relationship between the derivative and the hedged item is formally documented and the hedge is highly effective and ranging from 80% to 125%, as initially verified and periodically checked. When derivatives cover the risk of fluctuations in the cash flows of the hedged instruments (cash flow hedges), changes in the fair value are initially taken to equity and subsequently to profits or losses, in line with the effects of the hedged transaction.

Changes in the fair value of derivatives that do not meet hedge accounting requirements are recognized in profits or losses.

When hedging derivatives cover the risk of fluctuations in the fair value of hedged instruments (fair value hedges), they are recognized at fair value through profits or losses. Accordingly, the hedged items are adjusted to reflect changes in the fair value associated with the hedged risk.

Fair value is measured with reference to official quotations for instruments traded in regulated markets. The fair value of instruments not traded in regulated markets is measured by discounting projected cash flows along a yield curve of interest rates at the reporting date, and by converting amounts in currency other than the euro at the year-end exchange rate.

Employee benefits

The liability related to employee benefits payable upon or after termination of employment relates to defined benefit plans (termination benefits, additional month's pay[9], indemnity for lack of notice[10], energy discount, ASEM health benefits and other benefits) or other long-term employee benefits (loyalty bonus) is recognized net of any plan assets. It is measured separately for each plan on the basis of actuarial calculations that estimate the amount of future benefits employees have accrued at the reporting date. The liability is recognized on an accruals basis over the vesting period. It is measured by independent actuaries. Actuarial gains and losses at 1 January 2005 (date of transition to IFRS) were recognized in equity. If, after that date, unrecognized actuarial gains and losses arise in excess of 10% of the greater of the present value of the defined benefit plan obligation and the fair value of plan assets, that portion is taken to profits or losses for the average expected term of service of employees participating in the plan. Otherwise, actuarial gains and losses are not recognized.

At the reporting date, the effects of new regulations concerning termination benefits were not considered, as uncertainty remains as to whether the parent has an obligation to employees who will opt to have their termination benefits managed by INPS. These employees could make up the entire workforce, if there is no participation in the management plans.

Share-based payments

The cost of employee service remunerated through stock option plans is measured at the fair value of the options granted to employees at the grant date. The fair value of options granted is recognized under personnel expenses over the vesting period, with a corresponding increase in equity, considering the best possible estimate of the number of options that employees will be able to exercise.

The measurement method used for fair value considers all the characteristics of the options (duration, price and conditions, etc.), as well as the value of the Terna share at the grant date, the volatility of the share and the interest rate curve at the grant date, in line with the duration of the plan. The amount recognized as cost is adjusted to reflect the actual number of vesting options, unless the failure to meet the conditions to obtain the right is based solely on the market.

[9] Additional month's pay
[10] Indemnity for lack of notice

Provisions for contingencies and charges

Accruals to the provisions for contingencies and charges are recognized when, at the reporting date, the group has a legal or constructive obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the effect of the time value of money is material, accruals are measured by discounting estimated future cash flows using a pre-tax discount rate that reflects current market assessments of the time value of money and those risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as an interest expenses. If the liability relates to property, plant and equipment, the provision is recognized as a balancing entry to the asset to which it relates. The expenses is recognized in the income statement through depreciation of the item of property, plant and equipment to which it relates.

Grants

Grants from public and private entities are recognized at fair value when it is reasonably certain that they will be received and that the conditions provided for obtaining the grants will be satisfied.

Grants received for specific expenditure are recognized under other liabilities and taken to the income statement on a systematic basis over the period in which the related costs accrue.

Grants received in relation to specific assets whose value is recognized under non-current assets are, for plants operating before 31 December 2002, recognized under other liabilities and taken to the income statement over the depreciation period of the related assets. From 2003, grants for new plants going into use are taken as a direct reduction in the value of the related asset.

Grants for operating expenses are expensed in full when the conditions for recognition are satisfied.

Revenues

Depending on the type of transaction, revenues is recognized on the basis of the following specific criteria:

- revenues from the sale of goods is recognized when the significant risks and rewards of ownership of the goods have been transferred to the buyer;
- revenues from the rendering of services is recognized with reference to the stage of completion of the transaction. If revenues cannot be reliably measured, it is recognized to the extent of recoverable costs.

In particular, revenues from fees to use the National Transmission Grid are measured based on the tariffs established by the Electricity and Gas Regulator.

Considerations collected on behalf of third parties, such as the consideration paid to other non-Group grid owners, as well as revenues recognized for managing activities related to the balancing of the national electrical energy system, which do not increase equity, are shown net of the related costs. This presentation method, which reflects the substance of transactions by offsetting revenues with the related costs arising from the "same transaction" is described in all its parts in a specific paragraph of the notes.

Financial income and expenses

Financial income and expenses are recognized on an accruals basis in line with the interest accrued on the net amount of related financial assets and liabilities, using the effective interest method.

Dividends

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

Basic earnings per share

Basic earnings per share are calculated by dividing the profits for the year attributable to holders of ordinary shares by the weighted average of outstanding ordinary shares during the year.
Diluted earnings per share are calculated by dividing the profits for the year attributable to holders of ordinary shares by the weighted average of outstanding shares, adjusted to consider the effects of all potential ordinary shares, which have a diluting effect.

Income taxes

Current income taxes are recognized as tax liabilities, net of advances paid, or tax assets where the net balance of the captions is positive. They are based on the estimated taxable income and in accordance with current legislation.
Deferred tax assets and liabilities are calculated on the temporary differences between the carrying amounts of assets and liabilities recognized in the consolidated financial statements and the corresponding amounts recognized for tax purposes, in application of current tax rates, or rates expected to be in effect when the temporary differences reverse, based on current rates or those that are substantially approved at the reporting date.
Deferred tax assets are recognized when their recovery is considered probable, i.e., when future taxable profits will be available against which the asset can be used. The recoverability of deferred tax assets is reviewed at each year end.
Deferred tax liabilities are recognized in any case if they exist.

New reporting standards

In 2006, no new standards or interpretations were approved and no amendments were made to the standards and interpretations in effect as from 1 January 2006, with a significant impact on the consolidated financial statements.
Regulations nos. 108/2006, 708/2006 and 1329/2006 issued by the European Commission modified certain standards and interpretations already in place, exclusively with respect to disclosure requirements.
The following standards and interpretations were approved, and could become applicable to the group's consolidated financial statements in the future.

IFRS 7 - Financial instruments: additional disclosures

IFRS 7 requires additional disclosures on the relevance of financial instruments with respect to the company's performance and financial position. These disclosures incorporate certain requirements that were previously included in IAS 32 - Financial Instruments: Disclosure and Presentation. The new standard also requires information on the level of risk exposure arising from the use of financial instruments and a description of the objectives, policies and procedures implemented by management to manage such risks. IFRS 7 takes effect from years beginning on 1 January 2007 or subsequently.

IFRS 8 - Operating Segments

IFRS 8 establishes how a company should report on operating segments in the annual financial statements and, as an amendment to IAS 14 - Segment Reporting, requires the same information also in interim reports. In addition, it defines disclosure requirements with respect to products and services, the geographical areas in which the company operates and its key customers. The new standard is the result of the comparison of IAS 14 and SFAS 131 - Disclosures about Segments of an Enterprise and Related Information, as part of the IFRS and US GAAP convergence project, to reduce the discrepancies between the two.
IFRS 8 supersedes IAS 14 and is applicable to financial statements for years beginning on 1 January 2009. However, early application is allowed.

IFRIC 8 - Scope of IFRS 2

This interpretation clarifies when IFRS 2 must be applied to transactions in which the company cannot specifically identify a portion or all of the goods or services received. IFRIC 8 takes effect from years beginning on 1 May 2006 or subsequently.

IFRIC 9 - Revaluation of embedded derivatives

This interpretation requires a specific assessment so that embedded derivatives are separated from the host contract and recognized as derivatives when they become part of the contract. IFRIC 9 takes effect from years beginning on 1 June 2006 or subsequently.
Moreover, in 2006, the relevant international bodies issued the following amendments to existing standards and new interpretations, which have not yet been endorsed by the European Commission.

IFRIC 10- Interim financial reporting and impairment

This interpretation clarifies that in the preparation of annual financial statements, companies are not permitted to reverse any impairment losses recognized in previous interim financial statements in relation to the impairment of goodwill, financial investments carried at cost or investments or financial assets carried at cost.
This interpretation is applicable to financial statements for years beginning on 1 November 2006. However, early application is allowed.

IFRIC 11 - IFRS 2 Group and treasury share transactions

This interpretation clarifies the recognition methods for share-based payments (e.g., stock option plans to employees) between Group companies.
This interpretation is applicable to financial statements for years beginning on 1 March 2007. However, early application is allowed.

IFRIC 12 - Service Concession Arrangements

IFRIC 12 substantially confirms the recognition methods provided for by the previous three draft interpretations (D12, D13 and D14) concerning assets (freely transferable assets), liabilities (reclamation provisions), revenues and costs in connection with service concession arrangements between a public body and a private company. It excludes concessions between private companies.
This interpretation is applicable to financial statements for years beginning on 1 January 2008. However, early application is allowed.
The group is evaluating the impact that all of the amendments and new standards and interpretations could have on the financial statements, considering the date they take effect.

As described below, certain balances of the consolidated financial statements at 31 December 2005 have been reclassified, for the purpose of a more correct presentation. However, equity figures as of 31 December 2005 and income statement figures for 2005 have not been modified.

Risk Management

Interest rate risk

In carrying out its operations, Terna is exposed to the risk of fluctuations in interest rates. Its main source of interest rate risk relates to items of net financial indebtedness that generate interest expenses. Terna's strategy for financial indebtedness is to focus on long-term loans, which reflect the useful life of Group assets. It pursues an interest rate risk hedging policy that aims to combine this choice with the regulatory context, which every four years establishes the cost of debt as part of the formula to set RAB remuneration. Accordingly, the hedging instruments used, at various maturity dates, include both derivatives that transform fixed rates into variable rates (fair value hedges) and derivatives that transform variable rates into fixed rates (cash flow hedges and trading).

With the aim of reducing the amount of financial indebtedness exposed to the risks of fluctuations in interest rates and reducing the cost of funding, two types of plain vanilla derivatives have been used, i.e. interest rate swaps and interest rate collars. At year end, considering the transactions in derivatives, 66.1% of Terna SpA's gross indebtedness bears interest at fixed rates, while net indebtedness bearing interest at fixed rates amounts to 67.2%.

All derivative contracts have a notional amount and maturity date less than or equal to that of the underlying financial liability, so that any change in the fair value and/or estimated cash flows of the contracts is offset by a corresponding change in the fair value and/or estimated cash flows of the underlying position.

The main source of interest rate risk with regard to the investments in Brazil is the subsidised indexed interest rate on the loan granted by Banca BNDES. This indebtedness has not be hedged since the subsidised rate granted by BNDES (TJLP) is not volatile and is considered advantageous with respect to short-term Italian interest rates (CDI) and similar rates on similar maturity loans.

The Brazilian companies have taken out loans in US dollars, and the related exchange rate risk has not been hedged, considering both the burden of long-term hedges and the natural hedging that occurs, as the companies' revenues is indexed to the US dollar, given that it closely follows trends in the US dollar/Brazilian real exchange rate.

In terms of liquidity risk, considering that there is normally a negative difference between interest received on loans granted and interest paid on loans received, financial optimization activities are geared towards minimizing liquidity positions in line with the group's needs.

Sensitivity to interest rate risk

If the Eurozone interest rate curve were to rise or drop 50 bps at 31 December 2006, the average cost of Terna SpA debt would fluctuate by approximately 35 bps, for a total of roughly euros 7 million.

In Brazil, a similar change in interest rates would not have material effects, given the nature of Brazilian debt, which is indexed to an interest rate (TJLP) that is subsidised by the Brazilian Government. Accordingly, it is not vulnerable to market volatility.

Credit risk

The Terna Group provides its services exclusively to counterparties considered solvent by the market, i.e., they have high credit ratings. Moreover, the group does not have concentrations of credit risk.

Credit risk arising from open positions in derivative financial instruments is considered marginal, since the counterparties are leading Italian and international banks with high ratings and the management of these transactions is fractioned off, in compliance with specific concentration limits.

Exchange rate risk

The group carries out transactions with counterparties residing in non-EU countries. It has marginal exposure to the risk of fluctuations in the US$/R$ exchange rate. The group evaluates the individual transactions and sets up hedges where necessary and in compliance with financial risk management policies.

B) SEGMENT REPORTING

The segments were identified and Terna Group's primary and secondary segments were determined considering the organizational structure and internal reporting system. In particular, since the risks and rewards of the group's investments are exclusively affected by differences in the services provided, the primary reporting segment is based on the activities performed (transmission/dispatching/metering), while the transmission activities are reported geographically, since they are performed in Italy and Brazil. Specific allocation parameters have been established for income and expenses and assets and liabilities not specifically attributable to individual sectors (in particular, financial assets and liabilities, tax assets and liabilities and deferred tax assets and liabilities). They are indicated separately.

In addition, intersegment transfers sectors are measured at current market conditions.

Reporting by business segment and geographical area is provided below for 2005 and 2006:

2005

In millions of euros	Regulated activities: Transmission – Italy	Regulated activities: Transmission – Brazil	Regulated activities: Dispatching Italy	Metering Italy	Unregulated activities	Total
Revenues	837.5	170.4	17.7	1.5	60.3	1,087.4
Segment revenues	**465.1**	**116.0**	**-2.3**	**1.5**	**26.6**	**606.9**
Unallocated expenses						59.8
Operating profits						**547.1**
Financial income/(expenses)						-82.0
Share of profits/(losses) of equity accounted investees	1.8					1.8
Income taxes						169.0
Profits for the year						**297.9**
OTHER INFORMATION						
Segment assets	4,024.0	884.2	1,090.4	2.2	289.7	6,290.6
Segment liabilities	2,797.6	499.7	837.9	-	253.2	4,388.4
Investments	260.3	9.4	3.2	-	-	272.9
Amortization, depreciation and impairment losses	151.3	17.7	6.2	-	-	175.2
Other non-monetary expenses	1.1	-	-	-	-	1.1

2006

In millions of euros	Regulated activities: Transmission – Italy	Regulated activities: Transmission – Brazil	Regulated activities: Dispatching Italy	Metering Italy	Unregulated activities	Total
Revenues	954.6	187.6	105.0	9.3	51.3	1,307.8
Segment profits	**636.3**	**133.3**	**1.4**	**8.0**	**18.8**	**797.8**
Unallocated expenses						110.3
Operating profits						**687.5**
Financial income/(expenses)						-68.6
Share of profits/(losses) of equity-accounted investees	0.0					0.0
Income taxes						249.1
Profits for the year						**369.8**
OTHER INFORMATION						
Segment assets	4,456.8	937.6	1,345.0	10.4	239.5	6,989.3
Segment liabilities	2,763.8	473.2	1,309.4	2.0	282.0	4,830.4
Investments	324.7	7.0	20.7	0.1	-	352.5
Amortization, depreciation and impairment losses	171.2	18.9	34.1	0.4	-	224.6
Other non-monetary expenses	0.8		-	-	-	0.8

C) NOTES TO THE CONSOLIDATED INCOME STATEMENT

Revenues

1) REVENUES FROM GOODS AND SERVICES - euros 1,279.5 million

The table below details revenues of the year:

In millions of euros	2006	2005	Change
Grid transmission consideration	1,143.9	957.8	186.1
Adjustments for prior year grid transmission consideration	47.6	34.8	12.8
Other energy revenues	41.9	6.9	35.0
Other revenues from goods and services	46.1	59.1	-13.0
TOTAL	**1,279.5**	**1,058.6**	**220.9**

Grid transmission consideration

Most of this caption (euros 876.0 million) relates to the consideration received by the parent for use of the National Transmission Grid. It also includes grid transmission considerations (AEEG Resolution no. 15/2005) paid to Terna with the acquisition of the TSO business activity (euros 71 million); while revenues earned by the Brazilian companies, of euros 186.5 million, relates to the fixed fee established by the concession for transmission lines issued by the local energy authority (ANEEL); this caption also includes revenues of the subsidiaries of RTL Group (euros 10.5 million) relating to the related portion of the National Transmission Grid. The net increase (euros 186.1 million) is due to the following factors in particular:

- increased revenues relating to the remuneration of the national electricity grid (up euros 101.3 million), in Italy, especially following the new tariffs, which took effect in 2006, as well as to the higher volumes of transmitted energy (up 2.2%); during 2005 the AEEG adjusted tariffs (as detailed in the paragraph below), therefore also affecting 2006 tariffs;
- the grid transmission consideration arising from the merger of the TSO business activity (euros 58.9 million);
- the euros 16.7 million increase in the revenues of the Brazilian subsidiaries which is entirely related to the appreciation of the local currency (approximately euros 18.5 million);
- the contribution of revenues of the subsidiaries of the RTL Group in relation to its portion of the National Transmission Grid (euros 9.2 million).

Adjustments for prior year grid transmission consideration

AEEG's Resolution no. 162/06 of 27 July 2006 established that the transmission service tariff proceeds for 2005, based on the tariffs in place in that period, did not adequately remunerate the transmission operators.

The tariff deficit recorded amounted to a total of euros 51.7 million, which GSE SpA will pay rightful transmission operators, by using a portion of the transmission capacity considerations realized in 2004 and 2005. In particular, the greater revenues relating to Group companies includes approximately euros 47.3 million for the parent and euros 0.3 million for its subsidiary RTL SpA.

This caption also includes adjustments from GSE SpA for the grid transmission consideration of previous years (euros 19.8 million) and revenues from the release of the provision for contingencies which had been accrued for doubtful grid transmission considerations (Cip 6 - autoproducers litigation - euros 15.0 million). At 31 December 2005, these amounts totalled euros 34.8 million and were stated under “Other revenues and income”.

Other energy revenues

This caption relates to the consideration due to the parent by operators for metering activities (MIS component - euros 9.3 million) and to the consideration for the acquisition of resources necessary for dispatching requirements (DIS component - euros 32.3 million). In 2005, these items related to only the last two months of the year, that is from the acquisition date of the business activity from GSE (1 November 2005).

The caption also includes the consideration as per AEEG Resolution no. 34/05 (euros 0.3 million) to cover the administrative and management costs incurred to withdraw energy from renewable sources producers with a power not exceeding 10 MVA and similar connected to the National Transmission Grid.

Other energy items - energy in transit revenues/costs

This caption includes the cost and revenues (energy in transit activities for the group; these have a nil balance) relating entirely to the parent and arising from daily purchases and sales with operators on the electricity market to carry out transmission and dispatching activities.

The components of these transactions are detailed below. Those related to 2005 refer only to the last two months of the year:

In millions of euros	2006	2005	Changes
REVENUES - POWER EXCHANGE			
procurement of resources on the ancillary services market	1,502.4	217.3	1,285.1
unbalancing and others	1,313.1	270.5	1,042.6
sale of energy on the day-ahead market. adjustment market, ancillary services market and others	885.1	106.2	778.9
foreign market - exports	2.9	0.3	2.6
other items - Power exchange	3.5	0.4	3.1
Total revenues - Power Exchange	**3,707.0**	**594.7**	**3,112.3**
REVENUES FROM OUTSIDE THE POWER EXCHANGE			
revenues under Laws no. 168/04 - 237/04 and others	820.0	117.5	702.5
revenues from grid transmission considerations of other owners and portion of GRTN CIP/6	113.0	16.9	96.1
other items (returns, CBT)	389.5	11.7	377.8
Total revenues from outside the Power Exchange	**1,322.5**	**146.1**	**1,176.4**
TOTAL REVENUES FROM ENERGY IN TRANSIT	**5,029.5**	**740.8**	**4,288.7**
COSTS - POWER EXCHANGE			
to provide the dispatching service	2,800.6	450.2	2,350.4
for unbalancing	478.5	39.0	439.5
on the day-ahead and adjustment markets	323.3	64.0	259.3
on the foreign market - imports	91.7	39.7	52.0
Electricity market operator fees	8.0	1.4	6.6
other items	4.9	0.4	4.5
Total costs - Power Exchange	**3,707.0**	**594.7**	**3,112.3**
COSTS FROM OUTSIDE THE POWER EXCHANGE			
costs under Laws no. 168/04 - 237/04 and others	820.0	117.5	702.5
fees to be paid to National Transmission Grid owners. GRTN and others	113.0	16.9	96.1
other items (returns, CBT)	389.5	11.7	377.8
Total costs from outside the Power Exchange	**1,322.5**	**146.1**	**1,176.4**
TOTAL EXPENSES FOR ENERGY IN TRANSIT	**5,029.5**	**740.8**	**4,288.7**

Other revenues from goods and services

Other revenues from goods and services amounted to euros 46.1 million (2005: euros 59.1 million) and mainly relates to revenues from a variety of specialized high and very high voltage services, which the parent provides to third party customers. In particular, the amount reflects revenues from:

- maintenance for high-voltage lines (euros 20.1 million), in particular the maintenance contract for the high voltage lines owned by Enel Distribuzione SpA (euros 16.1 million, down euros 4.4 million on 2005);
- the operating, maintenance and development of the optical fibre owned by Wind Group on Terna SpA plants (safety cables) (euros 7.1 million);
- a variety of specialized services in the high voltage field for several customers (euros 17.5 million);
- requests to connect to the National Transmission Grid as per AEEG Resolution no. 281/05 (euros 1.4 million).

2) OTHER REVENUES - euros 28.3 million

Other revenues and income

Other revenues mainly relates to the parent, and is detailed below:

In millions of euros	2006	2005	Changes
Third party contributions for high-voltage connections	12.1	10.2	1.9
Other revenues	6.2	6.7	-0.5
Rental income	6.8	1.7	5.1
Prior year income	3.2	4.6	-1.4
TOTAL	**28.3**	**23.2**	**5.1**

This caption generally reflects rental income (including invoices of the year, relating to second half of the year only, issued to the Wind Group in connection with the housing of optical fibre on the parent's grids - euros 4.7 million), insurance compensation for damage to plants, gains on the sale of plant parts to third parties and, in particular, portions of third party contributions for connections to the National Transmission Grid released during the year. The prior year income for adjustments from GSE SpA on the grid transmission consideration of previous years and the release of the provision for contingencies already accrued for grid transmission consideration (euros 34.8 million) recognized in 2005, were reclassified to “revenues from goods and services”.

Income for higher taxes recognized in 2005 under “prior year income” (euros 5.6 million) is reclassified under “income taxes” as a direct decrease of such caption.

Operating Expenses

3) RAW MATERIALS AND CONSUMABLES - euros 18.7 million

In millions of euros	2006	2005	Changes
Inventory procurement	10.7	10.7	0.0
Supply of materials and equipment	5.7	9.6	-3.9
Other supplies	2.3	5.1	-2.8
TOTAL	**18.7**	**25.4**	**-6.7**

This caption includes costs incurred to purchase materials and sundry equipment used in ordinary operations and plant maintenance, mainly by the parent. It also includes the change in inventories during the year.

4) SERVICES - euros 145.3 million

In millions of euros	2006	2005	Changes
Tenders on plants	24.7	25.6	-0.9
Sundry services	64.8	41.8	23.0
Insurance	5.1	5.4	-0.3
Remote transmission and telephone	19.0	22.0	-3.0
IT services	13.0	10.5	2.5
Use of third party assets	18.7	13.5	5.2
TOTAL	**145.3**	**118.8**	**26.5**

This caption increased by euros 26.5 million on 2005 mainly because the parent Terna was fully operative as TSO integrated operator for the entire year. Figures for 2005 only relate to costs for the last two months of the year. With respect to the parent, services total euros 123.7 million.
This caption mainly includes the costs of maintenance and repairs in relation to tenders and services for ordinary maintenance activities, as well as maintaining the efficiency of plants. It also relates to remote transmission and telephone services, IT services, leases, rentals and general services.

The following table shows the fees paid to the parent’s Directors and statutory auditors. The table shows their term of office and fees are calculated on an accruals basis.

Surname and Name	Position	Term of office	Expiry	Fees	Bonuses and other incentives **	Total
Roth Luigi	Chairman/Director	jan-06/dec-06	Approval of the 2007 financial statements	254,999.98		254,999.98
Cattaneo Flavio	CEO	jan-06/dec-06	Approval of the 2007 financial statements	233,333.34	16,666.67	250,000.01
De Paoli Luigi	Director	jan-06/dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Garaffo Mario	Director	jan-06/dec-06	Approval of the 2007 financial statements	95,000.00		95,000.00
Machì Salvatore	Director	jan-06/dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Macrì Carmine	Director	jan-06/dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Maranesi Piero Giuseppe	Director	jan-06/dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Rispoli Vittorio	Director	jul-06/dec-06	Approval of the 2007 financial statements	16,250.00		16,250.00
Smurro Franco	Director	jan-06/dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Romano * Massimo	Director	jan-06/dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Ponzellini Massimo	Director	jan-06/jul-06	Approval of the 2007 financial statements	32,500.00		32,500.00
Total fees - Directors				**962,083.32**	**16,666.67**	**978,749.99**
Ferreri Giovanni	Chairman of the Board of Statutory Auditors	jan-06/dec-06	Approval of the 2007 financial statements	55,000.00		55,000.00
Corvace Giancarlo	Standing Auditor	jan-06/dec-06	Approval of the 2007 financial statements	45,000.00		45,000.00
Tasca Roberto	Standing Auditor	jan-06/dec-06	Approval of the 2007 financial statements	45,000.00		45,000.00
Total fees - Statutory Auditors				**145,000.00**		**145,000.00**
TOTAL				**1,107,083.32**	**16,666.67**	**1,123,749.99**

* With respect to the positions held, fees totalling euros 55,000.00 were transferred to Enel SpA.
** This amount relates to the variable portion of the fee for 2005, approved and disbursed in 2006.

5) PERSONNEL EXPENSES - euros 242.0 million

In millions of euros	2006	2005	Changes
SHORT-TERM EMPLOYEE BENEFITS			
wages and salaries	157.2	128.4	28.8
social security contributions	51.0	33.3	17.7
other	3.8	2.9	0.9
Directors	1.2	1.1	0.1
POST-EMPLOYMENT BENEFITS			
Defined benefit plans			
electricity discount	2.6	8.8	-6.2
asem-acem	0.6	1.7	-1.1
Defined contribution plans			
fopen	1.3	1.1	0.2
fondenel	0.4	0.2	0.2
EMPLOYEES' TERMINATION BENEFITS			
leaving incentives	13.1	15.2	-2.1
Employees' stock option plans	0.8	0.2	0.6
Termination benefits	10.0	8.8	1.2
TOTAL	**242.0**	**201.7**	**40.3**

This caption includes the cost of wages and salaries, social security contributions and other costs incurred by the parent for leaving incentives, as well as benefits paid to employees who stay with the company and termination benefits provided for by the current national labour contract for the electrical energy sector.

Personnel expenses increased by euros 40.3 million, mainly due to the costs following the acquisition of the TSO business activity and the addition of its human resources (wages, salaries, social security contributions and termination benefits up euros 39 million on 2005). The main changes were as follows:

- additional social security contributions borne by the parent for CIG and CIGS (euros 9.8 million);
- lower termination benefits (down euros 7.7 million) mainly related to the electricity discount which decreased, *inter alia*, following the reorganization of the criteria for eligible parties;
- financial effects (euros 2.4 million) of the renewal of employees' labor contract which was signed in July 2006.

The following table shows the number of employees by category at year end and the average number for the year:

	Average number 2006	Number at 31.12.2006	Number at 31.12.2005
Managers	73	75	75
Junior managers	420	439	403
White collars	1,890	1,937	1,866
Blue collars	1,074	1,104	1,098
TOTAL	**3,457**	**3,555**	**3,442**

The net change with respect to 31 December 2005 is an increase of 113 employees. The increase is mainly due to the acquisition of RTM1 and RTM2.

6) AMORTIZATION, DEPRECIATION AND IMPAIRMENT LOSSES - euros 224.6 million

These relate to accruals during the year calculated on the basis of amortization and depreciation rates that reflect the useful lives of the plants of the group companies. This caption increased by euros 37.4 million on 2005, mainly due to the parent, following the acquisition of the TSO business activity (euros 13.3 million) and the new plants that began operating during the year (euros 6.0 million). The Brazilian subsidiaries also recorded an increase in amortization and depreciation (euros 1.2 million), entirely due to the effects of the different exchange rates ruling from one year to the next, while the amortization and depreciation of the subsidiaries of the RTL Group amounting to euros 3.4 million.
The caption also includes accruals to the provision for bad debts of euros 12.1 million, relating to receivables due to the parent for energy items which are reasonably unlikely to be collected.

7) OTHER OPERATING EXPENSES - euros 26.5 million

In millions of euros	2006	2005	Changes
Local taxes and duties	13.5	35.0	-21.5
Prior year expenses	2.9	4.3	-1.4
Losses on the sale/disposal of plants	3.1	3.4	-0.3
Other operating expenses	7.0	3.0	4.0
TOTAL	**26.5**	**45.7**	**-19.2**

This caption mainly includes indirect local taxes, as well as losses on the disposal of plants and other residual operating expenses. The decrease on 2005 is mainly due to:

- lower local taxes and duties, (down euros 15.6 million) reported by the Brazilian subsidiaries in the year;
- the registration tax for the acquisition of the TSO business activity paid in 2005 (down euros 2.8 million);
- taxes on interest on equity paid abroad in 2005 which are not deductible in Italy (down euros 3.7 million);
- contractual penalties for services and use of third party assets paid by the parent (up euros 2.1 million);
- grants and membership fees paid by the parent (up euros 0.8 million).

8) CAPITALIZED INTERNAL WORK - euros -36.8 million

Capitalized expenses relate to personnel expenses (euros 27.7 million) and the consumption of materials and equipment in inventories (euros 9.1 million) for plants under construction. They relate entirely to the parent. The euros 10.4 million increase is fully attributable to personnel expenses, which also offset the reduction in the capitalization of consumed materials.

Financial income expenses

9) NET FINANCIAL EXPENSES - euros 68.6 million

This caption is detailed as follows:

In millions of euros	2006	2005	Change
FINANCIAL INCOME			
Interest income on former intercompany current account with Enel SpA	-	3.3	-3.3
Other financial income	44.9	11.6	33.3
Value changes of the hedged bond	-	3.7	-3.7
Income on trading derivatives	8.8	-	8.8
Exchange rate gains	7.0	16.8	-9.8
Total income	**60.7**	**35.4**	**25.3**
FINANCIAL EXPENSES			
Interest expenses on medium/long-term loans	-118.4	-109.5	-8.9
Value changes of the hedged bond	-2.6	-	-2.6
Expenses on trading derivatives	-	-2.0	2.0
Discounting of termination benefits and other employee-related provisions	-6.6	-5.9	-0.7
Exchange rate losses	-1.7	-	-1.7
Total expenses	**-129.3**	**-117.4**	**-11.9**
TOTAL EXPENSES, NET	**-68.6**	**-82.0**	**13.4**

Net financial expenses of the year amounts to euros 68.6 million, down euros 13.4 million on 2005. The change is due to the combined effect of a variety of factors. In particular:

- an increase in financial expenses due to medium/long-term indebtedness (up euros 8.9 million) mainly following the rise in interest rates with repercussions on bonds and the related hedges (up euros 11.0 million) and the EIB loans bearing interest at variable rates and the related hedges (down euros 1.6 million). A decrease in financial expenses for the Brazilian subsidiaries, including the effects of the real/euros exchange rate (down euros 0.4 million);
- an increase in other financial income (euros 33.3 million) mainly related to the gain on sale of 17.4% of Terna Participações shares. The sale was carried out by launching an IPO on the São Paulo Stock Exchange in Brazil (euros 31.4 million);
- lower exchange rate gains recognized by the parent (down euros 11.5 million) and lower exchange rate losses due to the appreciation of the Brazilian real against the euro and the US dollar with respect to 2005.
- the net positive effects of the fair value adjustment of bonds and related hedges, as well as additional derivative instruments in the parent's portfolio (up euros 4.5 million);
- the financial effect of the discounting of employee benefits, which includes charges substantially in line with 2005 (up euros 0.7 million);
- lower financial income (down euros 3.3 million) of the parent in relation to the intercompany current account, which was still open in 2005 with Enel SpA and closed on 15 September 2005.

10) SHARE OF PROFITS/(LOSSES) OF EQUITY-ACCOUNTED INVESTEES - euros -0.0 million

In 2005, this caption included the fair value adjustment of the investment in the associate Cesi SpA, measured using the equity method. In 2006, no changes occurred in this respect.

11) INCOME TAXES - euros 249.1 million

Income taxes of the year amount to euros 249.1 million, with an impact on profits before taxes of 40.23% (net of tax adjustments relating to previous years). In 2005, income taxes amounted to euros 163.4 million, with an impact on profits before taxes of 35.41%.

Income taxes of the year are detailed as follows:

In millions of euros	2006	2005	Changes
INCOME TAXES			
Current taxes:			
- IRES	195.2	136.2	59.0
- IRAP	40.9	28.6	12.3
- Brazilian companies	32.2	11.4	20.8
Temporary differences:			
- deferred tax income	-15.7	-14.2	-1.5
- deferred tax expenses	9.9	32.3	-22.4
Reversal of temporary differences:			
- deferred tax income	8.2	11.9	-3.7
- deferred tax expenses	-21.7	-37.2	15.5
Adjustments to income taxes of previous years	0.1	-5.6	5.7
TOTAL	**249.1**	**163.4**	**85.7**

The euros 85.7 million increase with respect to the previous year is mainly due to higher current taxes in Italy (up euros 71.3 million) and in Brazil (up euros 20.8 million), following the strong results of the year.

Deferred tax income and expenses (-euros 19.3 million) decreased by a net euros 12.1 million, mainly as a result of the following events:

- deferred tax income, net (euros 7.5 million) recognized in connection with temporary differences which arose during the year for accruals for personnel incentives (leaving incentives and bonuses) and to the provision for bad debts in excess of the tax-deductible portion;
- the net utilization of deferred taxes (down euros 11.8 million) mainly related to the effects of the introduction of Italian Law no. 266 of 23 December 2005, which introduced limitations on the tax deductibility of depreciation.

The caption also includes income (down euros 5.7 million on 2005) in relation to the parent's higher current taxes of previous years (euros -3.2 million), offset by adjustments for greater taxes (euros 3.3 million) in relation to previous years recognized by Brazilian subsidiaries for the recalculation of contributions to the

PIS (Social integration scheme) and the Cofins (Social insurance loan) on the Brazilian grid concession fees (RAP) with the former fees, which were higher, as established by the Brazilian tax authorities, with retroactive effect, as per Legislative Instructions no. 658 issued by the SRF (Secretaria da Receita Federal) on 4 July 2006.

The table below shows the differences between the theoretical and actual tax rates:

In millions of euros	2006	2005
Theoretical tax charge 33%	**204.2**	**154.1**
IRAP	40.9	28.6
Brazil	2.4	-16.9
Permanent differences	1.5	3.2
Actual tax charge	**249.0**	**169.0**
ACTUAL RATE	**40.2%**	**36.2%**

At year end, the total deferred tax charge relating to items recognized directly in equity amounts to euros 2.0 million and relates to the deferred tax effect on the fair value adjustment of derivatives hedging cash flow hedges.

12) EARNINGS PER SHARE

Basic earnings per share amount to euros 0.185, in which the numerator and denominator amount to euros 369.8 million and euros 2,000 million, respectively.

Diluted earnings per share amount to euros 0.184, in which the numerator and denominator amount to euros 369.8 million and euros 2,010 million, respectively.

D) NOTES TO THE CONSOLIDATED BALANCE SHEET

Assets

13) PROPERTY, PLANT AND EQUIPMENT - euros 5,159.0 million

Property, plant and equipment amount to euros 5,159.0 million (euros 4,646.3 million at 31 December 2005). They may be broken down as follows:

In millions of euros	Land	Buildings	Plant and machinery	Industrial and commercial equipment	Other assets	Assets under construction and payments on account	Total
Cost at 01.01.2006	**20.7**	**614.5**	**7,392.4**	**42.0**	**31.3**	**376.9**	**8,477.8**
Investments	2.3	18.7	108.5	2.3	14.6	179.6	326.0
Reclassifications	1.9	20.9	153.2		2.5	-178.5	0.0
Acquisition of Munirah		0.1	36.9			0.3	37.3
RTM1		0.4	359.4	0.5	0.3	0.6	361.2
RTM2	0.3		112.3	0.1			112.7
Exchange rate differences		-0.4	-18.4		0.2	-1.0	-19.6
Disposals	0.1	-0.3	-26.0	-0.1	-0.1	-0.6	-27.0
Other changes		-0.9	-12.6				-13.5
Reclassifications		-34.7	36.4		-1.7		0.0
Cost at 31.12.2006	**25.3**	**618.3**	**8,142.1**	**44.8**	**47.1**	**377.3**	**9,254.9**
Accumulated depreciation and impairment losses at 01.01.2006		**-216.0**	**-3,565.9**	**-29.3**	**-20.3**		**-3,831.5**
Depreciation of the year		-14.1	-172.6	-2.3	-4.7		-193.7
Impairment losses							0.0
Acquisition of Munirah			-0.4				-0.4
RTM1		-0.1	-69.0	-0.1	-0.3		-69.5
RTM2			-24.6				-24.6
Exchange rate differences			1.7				1.7
Disposals		0.2	21.6	0.1			21.9
Other changes			0.2				0.2
Reclassifications		1.8	-2.2		0.4		0.0
Accumulated depreciation and impairment losses at 31.12.2006	**0.0**	**-228.2**	**-3,811.2**	**-31.6**	**-24.9**		**-4,095.9**
Carrying amount							
AT 31 DECEMBER 2006	**25.3**	**390.1**	**4,330.9**	**13.2**	**22.2**	**377.3**	**5,159.0**
AT 31 DECEMBER 2005	**20.7**	**398.5**	**3,826.5**	**12.7**	**11.0**	**376.9**	**4,646.3**

The caption “plant and machinery” includes the electrical energy transmission grid and the transformation stations in Italy and Brazil, the central systems for remote conduction and the national electrical energy control system.

The Brazilian plant includes 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 Goias, and ending at the Sapeaçu substation, in the state of Bahia; 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.

By acquiring Munirah (March 2006), TSN acquired an additional 107 Km of 500 kV transmission lines and the substation of Camaçari (II) (Bahia), therefore completing the North-Northeast transmission circuit.

A summary of changes in property, plant and equipment during the year is provided in the table below:

In millions of euros	
Investments:	
- Transmission lines	120.4
- Transformation stations	148.9
- Other	49.7
- Brazil	7
Total investments	**326.0**
Depreciation	-193.7
Disposals and other changes	-18.4
Changes in consolidation scope:	
- RTM1	291.7
- RTM2	88.1
- Munirah	36.9
Exchange rate differences	-17.9
TOTAL	**512.7**

In addition to ordinary changes of the year relating to investments (euros 326.0 million), contributions for plants which became operative during the year (euros 13.6 million), sales (euros 5.1 million) and depreciation (euros 193.7 million), the caption also includes the acquisition of non-current assets following the acquisition of RTM1 (euros 291.7 million) and RTM2 (euros 88.1 million) in Italy (for greater information, reference should be made to the section "business combinations") and Munirah (euros 36.9) in Brazil.

Investments of the year relating to the National Transmission Grid (euros 318.7 million) mainly include the completion of the Laino-Feroleto-Rizziconi (euros 3.8 million), Turbigo-Rho (euros 15.9 million) and Sardinia-Corsica (euros 2.9 million) long distance lines and the construction of the underwater long distance line SAPEI (euros 34.7 million).

Investments also include the development of the Matera-S.Sofia line (euros 8.2 million) and the Casellina-S.Barbara line (euros 5.9 million). Other investments include the purchase of company cars (euros 16.7 million) and the building in Rome, via della Marcigliana (euros 7.2 million).

Investments in Brazil (euros 7.0 million) mainly relate to the termination of the EPC contract (euros 1.3 million), the acquisition of ancillary services for all NVT stations (euros 1.2 million), the purchase of a back up reactor for the Serra de Mesa station (euros 0.6 million) and the restructuring of the new headquarters in Rio de Janeiro (euros 0.6 million).

In terms of assets under construction and payments on account, the main grid development and repowering projects, worth more than euros 5 million, are listed below:

In millions of euros	
Transmission lines	
KV 380 MATERA - S.SOFIA	80,133,093
SAPEI - DC underwater link	33,230,166
380 kV transformation stations	
FRATTA	8,133,254
CARPI FOSSOLI	6,627,750
CASELLINA	6,503,128
SORGENTE	6,370,000
B. PIGNICELLE	5,205,158
220 kV transformation stations	
MAGENTA	6,245,833

14) GOODWILL - euros 139.9 million

Goodwill amounts to euros 139.9 million (euros 154.7 million at 31 December 2005). The balance and the changes by cash-generating unit are shown in the table below:

In millions of euros	TSN	NVT	RTL	RTM1	RTM2	MUNIRAH	Total
BALANCE AT 31 DEC. 2005	**106.1**	**48.1**	**0.5**	**0.0**	**0.0**	**0.0**	**154.7**
Change in consolidation scope				11.9	25.9	2.6	40.4
Terna Participações Listing	-36.1	-16.3					-52.4
Exchange rate differences	-1.7	-0.8					-2.5
Other changes			-0.3				-0.3
BALANCE AT 31 DEC. 2006	**68.3**	**31.0**	**0.2**	**11.9**	**25.9**	**2.6**	**139.9**

At 31 December 2006, goodwill (euros 139.9 million) relates to the difference paid by the group with respect to equity of subsidiaries at the acquisition date which was adjusted, for foreign subsidiaries, to reflect the effects of the year-end exchange rate. The increase in the balance at 31 December 2006 on the previous year end relates to the following:

- the acquisition of the subsidiaries RTM1 (euros 11.9 million) and RTM2 (euros 25.9 million) on 24 November 2006; for greater information reference should be made to the section “business combinations”;
- the partial realization of goodwill of Brazilian subsidiaries arising from the 34% reduction in the parent’s investment in the subsidiary Terna Participações following the listing of the company on Brazil’s São Paulo stock exchange in the second half of 2006 (euros -52.4 million);
- the adjustment of remaining goodwill (66%) to the above-mentioned listing relating to foreign subsidiaries

to reflect the effects of the year-end exchange rate (euros -2.5 million);

- the acquisition of the Brazil-based Munirah (euros 2.6 million).

Impairment testing

The recoverable amount of goodwill on the three Brazilian cash-generating units (CGUs) (Trasmissora Sudeste-Nordeste/TSN, Novatrans/NVT and Terna Participações) was estimated based on the list price of Terna Participações shares at 31 December 2006 (real 24.1), less estimated selling costs comprising local commissions and taxes of 4.1%. Based on the above, the recoverable amount of goodwill exceeds the above-mentioned carrying amount of the CGUs.

15) INTANGIBLE ASSETS - euros 159.2 million

Changes during the year in intangible assets are detailed below:

In millions of euros	Concessions	Other assets	Assets under development and payments on account	Total
BALANCE AT 31 DEC. 2005	134.5	11.3	5.7	151.5
Investments	0.0	16.1	10.4	26.5
Increases on capitalized internal work	0.0	0.5	-0.5	0.0
Amortization	-5.6	-13.2	0.0	-18.8
BALANCE AT 31 DEC. 2006	**128.9**	**14.7**	**15.6**	**159.2**
BALANCE AT 31 DEC. 2005				
Cost	135.4	53.6	15.6	204.6
Accumulated amortization	-6.5	-38.9	0.0	-45.4
Accumulated impairment losses	-	-	-	-
BALANCE AT 31 DEC. 2006	**128.9**	**14.7**	**15.6**	**159.2**

Intangible assets amount to euros 159.2 million (euros 151.5 million at 31 December 2005); the increase of the year (euros 7.7 million) is due to changes of the year relating to investments (euros 26.5 million) and amortization (euros 18.8 million).

The caption mainly includes the concession for electrical energy transmission and dispatching activities in Italy which was initially recognized in 2005, at fair value (euros 135.4 million) and subsequently measured at cost.

Other intangible assets mainly relate to the following:

- the development and innovation of application software to manage the energy invoicing process;
- the development and innovation of application software to protect the electrical energy system;
- software applications related to the development of the power exchange, particularly relating to the registration of operators, consumption units and the development of external procedures.

These software applications are amortized over their estimated residual useful lives, which are normally three years, given their rapid obsolescence.

16) DEFERRED TAX ASSETS - euros 62.1 million

Deferred tax assets relate to the following captions:

In millions of euros	31.12.2005	Change in consolidation scope and other changes	IMPACT RECOGNIZED IN PROFITS OR LOSSES		31.12.2006
			Accruals	Utilization	
Provision for contingencies and charges	10.3	1.4	5.4	-0.8	16.3
Provision for bad debts			2.1		2.1
Termination benefits and other employee-related provisions	30.5		7.4	-7.2	30.7
CFH and trading derivatives	9.6			-3.9	5.7
Tax loss	5.0			-5.0	0.0
Other	1.9	4.2	1.7	-0.5	7.3
DEFERRED TAX ASSETS	**57.3**	**5.6**	**16.6**	**-17.4**	**62.1**

The net increase (euros 0.8 million) on 2005 is mainly due to the combined effect of the following:

- the recognition of receivables of euros 5.4 million relating to the non-deductible accruals to the provisions for contingencies and charges;
- the recognition of receivables of euros 2.1 million relating to the non-deductible portion of the accruals to the provision for bad debts;
- the utilization of receivables of euros 3.9 million for the year-end fair value adjustments of cash flow hedge financial instruments;
- the utilization of receivables following the full recovery of the tax losses incurred by Novatrans and RTL (euros -5.0 million);
- the increase in receivables following the acquisition of RTM1 and RTM2 (euros 6.9 million).

The change in this caption (euros 4.8 million) does not include the impact of the tax effects on profits or losses of some items, such as the adjustment of cash flow hedge derivatives (euros -3.8 million).

17) EQUITY-ACCOUNTED INVESTEES - euros 6.4 million

Investments in equity-accounted investees amount to euros 6.4 million and relate to Cesi SpA, in which the group holds 24.4%.

This company operates in the construction and management of laboratories and plants for tests, inspections, studies and experimental research relating to the general electro-technical field and its technical and scientific progress. The carrying amount of this investment is unchanged with respect to 2005.

As permitted by current legislation, Cesi opted not to apply IFRS to the preparation of its financial statements at 31 December 2006. Consequently, these financial statements were prepared in accordance with Italian GAAP.

The main figures of Cesi, restated in accordance with the presentation and measurement criteria applied by Terna Group are as follows:

	ASSETS		LIABILITIES				
In millions of euros	Current	Non-current	Current	Non-current	Equity	Revenues	Profits for the year
Cesi	71.3	56.9	36.1	65.3	26.8	69.3	0.7

18) FINANCIAL ASSETS

Financial assets recognized in the consolidated financial statements are detailed in the table below:

	CARRYING AMOUNT		
In millions of euros	31.12.2006	31.12.2005	Change
FVH derivatives	11.3	106.1	-94.8
Trading derivatives	0.7	0.0	0.7
Non-current financial assets	**12.0**	**106.1**	**-94.1**
Deferred assets on FVH derivative contracts	1.5	4.4	-2.9
Other non-current financial assets	0.7	0.0	0.7
Current financial assets	**2.2**	**4.4**	**-2.2**
TOTAL	**14.2**	**110.5**	**-96.3**

The carrying amount shown in the table is equal to the fair value of the financial assets recognized in the consolidated financial statements.

“Non-current financial assets” amount to euros 12.0 million. The euros 94.1 million decrease is due to the rise in interest rate curve which triggered a reduction in the carrying amount of FVH derivatives (euros 94.8

million) and an increase in trading derivatives (euros 11.9 million).

The following table shows the group financial assets subject to interest rate risk, broken down by due date:

In millions of euros	Maturity	31.12.2005	31.12.2006	Average interest rate
FVH derivatives	2014-2024	106.1	11.3	1.30%
Trading derivatives	2007-2008	0	0.7	0.36%
TOTAL		**106.1**	**12**	

Trading derivatives have an impact on the income statement, while fair value hedge derivatives offset the impact of the change in the fair value of bonds. Fair value was calculated using the same method applied in 2005, that is by discounting estimated future cash flows to the market interest rate curve at the balance sheet date. The increase in the interest rate curve generated an increase in the fair value (up euros 11.9 million) of trading derivatives (a euros 0.7 million increase in non-current financial assets and a euros 11.2 million decrease in non-current financial liabilities) and a decrease (euros 94.8 million) in fair value hedge derivatives.

"Current financial assets" amount to euros 2.2 million (euros 4.4 million at 31 December 2005) and mainly relate to the following:

- "Deferred assets on FVH derivative contracts", which are entirely related to interest accrued and not yet received at the balance sheet date in connection with the derivative contracts (swaps) agreed to hedge bonds issued, amount to euros 1.5 million;
- "Other financial assets - current", which are entirely related to interest accrued and not yet received at the balance sheet date in connection with the current account balances, amount to euros 0.7 million.

19) INVENTORIES - euros 25.6 million

Inventories under current assets include materials and devices used in the operating, maintenance and construction of plants of euros 25.6 million (euros 21.2 million at 31 December 2005). The euros 4.4 million increase is mainly due to the ordinary maintenance requirements of plants.

20) TRADE RECEIVABLES - euros 1,182.1 million

Trade receivables are composed as follows:

In millions of euros	31.12.2006	31.12.2005	Change
Non-energy related receivables	285.3	266.5	18.8
Energy-related receivables	896.8	759.7	137.1
TRADE RECEIVABLES	**1,182.1**	**1,026.2**	**155.9**

Trade receivables amount to euros 1,182.1 million, up euros 155.9 million on 2005. The increase is due to electrical energy transmission and dispatching activities carried out by Terna in 2006 (in 2005 these activities had an impact for only two months following the acquisition of the transmission and dispatching business activity from GSE (formerly GRTN) SpA in November 2005).

Energy-related receivables are measured net of impairment losses relating to items considered uncollectible and recorded as an adjustment in the provision for bad debts (euros 13.1 million).

Non-energy related receivables - euros 285.3 million.

These amount to euros 285.3 million and mainly relate to the grid transmission consideration (euros 218.7 million) and related fees paid to the company for use of the National Transmission Grid by distributors (under Article 17 of AEEG Resolution no. 5/04 and subsequent modifications) and producers (under Article 19 of AEEG Resolution no. 5/04 and subsequent modifications) of electrical energy. In particular, under Resolution no. 5/04, the receivable mainly relates to the fee pertaining to the last two months of 2006, which was collected in full at the end of February 2007 (euros 185.0 million). The residual portion (euros 33.7 million) relates to the residual amount of the additional remuneration of 2005 paid under AEEG Resolution no. 162/06. It will be invoiced and collected by 31 July 2007. This caption also includes the share of fees pertaining to the operation of the Brazilian lines, both invoiced and to be invoiced (euros 14.5 million).

Receivables of foreign subsidiaries decreased substantially on 31 December 2005 (down euros 18.7 million), mainly as a result of the effects of the adjustment of the concession fees (RAP) for the period from 1 July 2006 to 30 June 2007 (ANEEL standardization Resolution no. 385 of 27 June 2006) and the retroactive application (again with respect to the RAP) of the former PIS/CONFINS rates to concession agreements signed before 31 October 2003 (under SRF regulatory Recommendation no. 658 of 4 July 2006, issued by the Brazilian Ministry of Finance). The latter measure entailed an adjustment to receivables following the higher grid transmission consideration calculated for PIS/CONFINS (period from January 2004 to the first half of 2006) and the corresponding recognition of tax receivables.

Other trade receivables include receivables due from Italian customers (euros 41.3 million), Enel Group companies (euros 5.4 million) and receivables for contract work in progress (euros 1.8 million) relating to long-term work that the company is carrying out for third-party customers.

Energy-related receivables - euros 896.8 million

Energy items mainly include receivables in relation to energy in transit items arising on the dispatching of electrical energy and which do not create profits margins for the parent. This caption also includes receivables for considerations payable by market operators for dispatching activities (DIS consideration as per AEEG Resolution no. 237/04) and metering activities (MIS consideration as per AEEG Resolution no. 05/04).

This caption also includes deferred charges relating to the signing of ETSO-CBT (European Transmission System Operators - Cross Board Trade) agreements governing the offsetting of energy in transit costs on foreign electricity grids. Under Resolution no. 15/2005, the AEEG ensured the coverage of the above charges and established that repayment terms will be set out in a specific provision.

21) OTHER ASSETS

In millions of euros	31.12.2006	31.12.2005	Change
Receivables due from others:			
- loans and advances to employees	4.6	4.2	0.4
- assets on deposit with third parties	1.3	1.3	0.0
- tax advance on termination benefits	0.5	1.5	-1.0
Other non-current assets	**6.4**	**7.0**	**-0.6**
Tax assets	8.0	11.7	-3.7
Receivables due from others:			
- advances to employees	0.2	0.2	0.0
- other	25.8	21.0	4.8
Other current assets	**34.0**	**32.9**	**1.1**

Non-current assets, detailed above, have not undergone any changes with respect to the previous year. Other current assets amount to euros 34.0 million (euros 32.9 million at 31 December 2005) and mainly relate to the following:

- tax assets of euros 8.0 million, primarily in relation to the following items:
  - tax receivables of foreign subsidiaries (euros 5.6 million) due to the retroactive adjustment of the former PIS/COFINS rates (under SRF regulatory Recommendation no. 658 of 4 July 2006 issued by the Brazilian Ministry of Finance);
- receivables due from others of euros 26.0 million, mainly in relation to the following:
  - receivables from the Greek tax authorities for indirect taxes (VAT of euros 9.1 million) in relation to the activities carried out by Terna's branch in Greece;
  - deferred tax assets of euros 3.9 million relating, in particular, to charges on use of third-party assets contracts which the parent subsequently entered into following the sale of plants by Enel Distribuzione (euros 1.5 million) and insurance premium (euros 1.6 million);
  - sundry receivables of euros 6.6 million;
  - sundry advances to employees (euros 0.2 million) and third parties (euros 2.2 million).

22) CASH AND CASH EQUIVALENTS - euros 200.4 million

At 31 December 2006, the parent's cash and cash equivalents amounted to euros 15.3 million, including bank current account deposits of euros 15.2 million (bearing interest at an average rate of 3.58%) and euros 0.1 million in cash on hand for operating areas.
At 31 December 2006, the cash and cash equivalents of the Brazilian subsidiaries amounted to euros 185.1 million (real 179.7 million and US$ 5.4 million) and include current account deposits of euros 149.1 million and term deposits of euros 36.0 million to guarantee loans granted.
The significant increase in the cash and cash equivalents of the Brazilian subsidiaries is due to the listing (IPO) of Terna Participaçoes shares on the São Paulo Stock Exchange in October.

Liabilities

23) EQUITY ATTRIBUTABLE TO THE SHAREHOLDERS OF THE PARENT euros 2,008.9 million

Share capital - euros 440.0 million

The share capital of Terna SpA is comprized of 2,000,000,000 ordinary shares with a nominal value of euros 0.22 each.

Legal reserve - euros 88 million

The legal reserve is equal to 20% of the parent's share capital.

Other reserves - euros 744.9 million

Other reserves underwent a net increase of euros 21.8 million, mainly as a result of the following:
fair value adjustment of derivatives hedging EIB loans - cash flow hedge derivatives, (up euros 11.6 million), net of the related tax effect (euros -3.8 million);
the net accrual of the portion (euros 13.2 million) of the incentive received from the Brazilian Ministry of National Integration relating to 2006 to equity reserves by the subsidiaries TSN and Novatrans;
the recognition of the cost of stock options described below (up euros 0.8 million).

Retained earnings - euros 475.7 million

Retained earnings mainly relate to the reserve as per the Vietti Law (euros 421.3 million), which was set up at 31 December 2004. The increase of the year (euros 22.5 million) mainly relates to the following events:

- allocation of the excess (euros 37.9 million) consolidated profits for the year ended 31 December 2005, with respect to the distribution of the balance of the related dividend during the first half of 2006 (euros 160.0 million).
- decrease in translation reserve following:
    - the reduction in translation differences arising on the consolidation of the foreign subsidiaries, mainly as a result of the appreciation of the Brazilian real against the euro compared with 2005. In this respect, the adjustment of goodwill at the year-end exchange rate entailed a euros 2.5 million decrease in that caption;
    - the partial goodwill of Brazilian subsidiaries arising from the 34% reduction in the investment in the subsidiary Terna Participações following the listing of the company on the Nivel 2 segment of Brazil's São Paulo stock exchange (Bolsa de Valores de São Paulo - BOVESPA), in the second half of 2006 (euros -13.2 million);

2006 interim dividend

After receiving the report of the auditors as per Article 2433 *bis* of the Italian Civil Code, the parent's Board of Directors, on 6 September 2006, approved the distribution of an interim dividend of euros 106 million, equal to 0.053 per share which was paid beginning from 23 November 2006.

The following table shows individual equity captions at the balance sheet date, indicating their origin, availability and possibility of distribution:

In millions of euros	Amount	Possibility of use	Available portion
Share capital	440.0	-	-
Legal reserve	88.0	B	-
Other reserves:			
- equity-related	396.1	A, B, C	396.1
- income-related	395.2	A, B	329.4
Retained earnings	429.3	A, B, C	398.4
interim dividend	-106.0	-	-
Profits for 2006	366.3	-	-
Total	**2,008.9**		
		TOTAL	**1,123.9**
		Unavailable portion	710.4
		Residual available portion	413.5

Key: **A** - to increase share capital **B** - to cover losses **C** - to be distributed to shareholders

The unavailable portion is mainly related to income-related reserves and retained earnings not yet subject to taxation.

The Board of Directors proposed that the shareholders, in their meeting which will be called on 23 May 2007 (first call) and 24 May 2007 (second call), approve a total dividend for 2006 of euros 0.14 per share and to pay, gross of withholdings as provided for by the law, the remaining euros 0.087 per share with respect to the above mentioned interim dividend. Consequently, the proposed dividend for 2006 amounts to euros 280 million, up 20 million or 7.7% on 2005.

The dividend is subject to the approval of shareholders called in their annual meeting. Therefore, it was not included under balance sheet liabilities. The balance of the proposed 2006 dividend will be payable to all shareholders on 21 June 2007.

Equity attributable to minority interests - euros 150.0 million

Equity attributable to minority interests relates to the Brazilian subsidiaries. In particular, the following is attributable to minority interests:

the purchased (OTC market) and subscribed (primary market) share capital and the relevant portion of equity reserves and the share of profits/(losses) of the Brazilian subsidiaries until the listing date (euros 148.7 million);

the profits, translation reserve and the reserve relating to the incentive received from the Brazilian Ministry of National Integration to the extent of the portion accrued in the period subsequent to the listing (euros 1.3 million).

Terna SpA stock option plans

On 21 December 2005, based on the proposals put forth by the Remuneration committee, the Board of Directors also resolved to adopt a 2006 stock option plan for Terna Group managers who hold the most important roles in terms of achieving the group’s strategic targets.

These plans are aimed at giving the Terna Group - in line with international best practice and that of the leading publicly listed Italian companies - a management incentive and loyalty tool, capable of giving key resources a sense of corporate belonging, while ensuring they are constantly focused on creating value, so as to bring shareholders’ and management’s interests together.

2006 stock option plans may be analyzed as follows:

Regulation governing the 2006 stock option plan (Resolution dated 21 December 2005)

The plan provides for the distribution of a maximum of 10,000,000 options to approximately 20 managers of the Terna Group, who hold the most important roles in terms of achieving the group’s strategic targets, including the CEO, as a senior manager of the company.

Under the approved regulation governing the stock option plan:

1. the strike price of each share shall be determined as the arithmetic mean of the reference prices of Terna ordinary shares as identified by the computer system of Borsa Italiana SpA in the period ranging between the date of the offer and the same day on the previous calendar month;
2. the exercise of the options and consequently, the right to subscribe newly-issued Terna ordinary shares depends on two performance parameters. In particular:

a. Terna Group EBITDA for the grant year (2006), must be greater than that shown in the group budget approved by the Board of Directors;

b. the 2006 performance of each beneficiary must be positively assessed by the CEO, forecasting a 50% reduction in the options that the individual beneficiary can exercise, should this second condition not be met;

3. if the conditions underlying the exercise are met, individual beneficiaries can exercise their options by 31 March 2010 and up to the following maximum quantities:
   a. up to 30% of exercisable options, beginning from the date disclosed in the notice communicating the fact that the conditions underlying the exercise have been met;
   b. up to 60% of exercisable options, beginning from the first day of the first calendar year subsequent to the year in which the conditions underlying the exercise are met;
   c. up to 100% of exercisable options, beginning from the first day of the second calendar year subsequent to the year in which the notice communicating the fact that the conditions underlying the exercise have been met.

Options can be exercised only when the stock exchange is open during the last 10 days of each month.
The 2006 stock option plan entailed the granting, on 21 December 2005, of 9,992,000 options with a strike price of euros 2.072, to 17 managers of the company. The Board of Directors verified that the conditions for exercise had been met when it approved the draft financial statements at 31 December 2006.

The options granted under this plan at 31 December 2006 are all outstanding and none may be exercised at that date.

	2006 plan
Outstanding at 1 January	9,992,000
Granted during the year	-
Unopted during the year	9,992,000
Exercised during the year	-
Matured during the year	-
Outstanding at 31 December 2006	9,992,000
Exercisable at 31 December 2006	-

The table below shows the residual life of options at 31 December 2006 and their fair value:

	Options granted (at 21 december 2005)	End of vesting period	Fair value * at grant date (in euros)
2006 plan	2,997,600	2007	0.126
	2,997,600	2008	0.121
	3,996,800	2009	0.115
TOTAL	**9,992,000**		

* factor of probability (100%)

The Cox-Rubinstein pricing method is used, which considers the value of the Terna share at the grant date, the volatility of the share, the interest rate curve at the grant date and throughout the duration of the plan. The pricing parameters applied are the following:

- Closing price (underlying or spot price) of the share at the grant date (source: Bloomberg) of euros 2.058;
- Strike price of euros 2.072;
- Interest rate curve for the calculation of the discount factor at the grant date (source: Reuters);
- Historic volatility of the share recorded at the grant date (source: Bloomberg) of 14.860%.

Stock options - Terna Participações SA

On 14 December 2006, the Board of Directors of Terna Participações SA, following the approval of shareholders in their extraordinary meeting of 5 October 2006, decided to adopt the first stock option plan for the three managers of Terna Participações SA; in particular, the 2007 Brazil stock option plan may be analyzed as follows:

Regulation governing the stock option plan (Resolution dated 14 December 2006)

The plan provides for the distribution of a maximum of 163,472 options to three managers of Terna Participações, who hold the important roles in terms of achieving strategic targets, including the CEO. Under the approved regulation governing the stock option plan:

1. the strike price of each share certificate (unit) is real 21.00;

2. the exercise of the options and consequently, the right to subscribe certificates of the newly-issued Terna Participações shares depends on meeting two performance parameters. In particular:

a. Terna Participações EBITDA for 2006 and the first half of 2007, must be greater than that shown in the budget approved by the Board of Directors;

3. if the conditions underlying the exercise are met, individual beneficiaries can exercise their options by 31 December 2011 and up to the following maximum quantities:
   a. up to 30% of exercisable options, beginning from the date disclosed in the notice communicating the fact that the conditions underlying the exercise have been met;
   b. up to 60% of exercisable options, beginning from 31 December of the year in which the notice communicating the fact that the conditions underlying the exercise have been met is issued;
   c. up to 100% of exercisable options, beginning from 31 December of the first calendar year subsequent to the year in which the notice communicating the fact that the conditions underlying the exercise have been met.

The Board of Directors will verify that the conditions for exercise are met when it approves the interim financial statements at 30 June 2007.

The options granted under this plan at 31 December 2006 are all outstanding and none may be exercised at that date.

	2007 Plan
Outstanding at 1 January	-
Granted during the year	163,472
Unopted during the year	163,472
Exercised during the year	-
Matured during the year	-
Outstanding at 31 December 2006	163,472
Exercisable at 31 December 2006	-

The table below shows the residual life of options at 31 December 2006 and their fair value:

	Options granted (at 14 December 2006)	End of vesting period	Fair value * at grant date (in real)
2007 Plan	49,041	first half 2007	3.17
	49,041	second half 2007	3.17
	65,390	2008	3.17
TOTAL	**163,472**		

* factor of probability 80%

The binomial pricing method is used, which considers the value of the Terna Participações share at the grant date, the volatility of the share, the interest rate curve at the grant date and throughout the duration of the plan. The pricing parameters applied are the following:

- Closing price (underlying or spot price) of the share at the grant date (source: Bloomberg) of real 24.10;
- Strike price of real 21.00;
- Interest rate curve for the calculation of the discount factor at the grant date (source: Reuters);
- Historic volatility of the share recorded at the grant date of 13.62%.

24) LOANS

The following table details loans and financial liabilities recognized in the Terna Group's consolidated financial statements at 31 December 2006. In particular, for each category, the carrying amount and the fair value of all financial liabilities recognized in the Terna Group's consolidated financial statements are compared.

In millions of euros	Carrying amount 31.12.06	Carrying amount 31.12.05	Change	Fair Value 31.12.06	Fair Value 31.12.05	Change
Bonds	1,406.6	1,498.4	-91.8	1,406.6	1,498.4	-91.8
Bank loans:						
- Italy	540.9	370.5	170.4	540.9	370.5	170.4
- Brazil	420.4	440.2	-19.8	420.4	436.5	-16.1
Total bank loans	**961.3**	**810.7**	**150.6**	**961.3**	**810.7**	**150.6**
Long-term loans	**2,367.9**	**2,309.1**	**58.8**	**2,367.9**	**2,305.4**	**62.5**
CFH derivatives	6.2	17.8	-11.6	6.2	17.8	-11.6
Trading derivatives	0.0	11.2	-11.2	0.0	11.2	-11.2
Non-current financial liabilities	**6.2**	**29.0**	**-22.8**	**6.2**	**29.0**	**-22.8**
Short-term loans	50.0	55.0	-5.0	50.0	55.0	-5.0
Current portion of long-term loans	71.1	58.3	12.8	71.1	58.3	12.8
Short-term loans and current portion of medium/long-term loans	**121.1**	**113.3**	**7.8**	**121.1**	**113.3**	**7.8**
TOTAL	**2,495.2**	**2,451.4**	**43.8**	**2,495.2**	**2,447.7**	**47.5**

The carrying amount of the bonds has been measured by adjusting the amortized cost to reflect the change in the fair value of the risk hedged, between the date of inception of the hedge and the balance sheet date.

Official Luxembourg stock exchange quotations for Terna bonds are as follows:

- bond maturing in 2024; price at 31.12.2006 103.56 and at 31.12.2005 109.68;
- bond maturing in 2014; price at 31.12.2006 99.77 and at 31.12.2005 105.43.

(*) Source: Bloomberg

Long-term loans

The following table shows the carrying amount of medium/long-term indebtedness and the repayment plan at 31 December 2006, broken down by loan type, including amounts falling due within one year.

In millions of euros	Maturity	31.12.2005	31.12.2006	Due within one year	Due after one year	2008	2009	2010	2011	After
Bonds	2014-2024	1,498.4	1,406.6	0.0	1,406.6	0.0	0.0	0.0	0.0	1,406.6
IDB	2016	48.8	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total fixed rate		**1,547.2**	**1,406.6**	**0.0**	**1,406.6**	**0.0**	**0.0**	**0.0**	**0.0**	**1,406.6**
EIB no. 20271	2014	61.4	54.6	6.8	47.8	6.8	6.8	6.8	6.8	20.6
EIB no. 21159	2016	238.6	215.9	22.7	193.2	22.7	22.7	22.7	22.7	102.3
EIB no. 22947	2020	100.0	100.0	0.0	100.0	0.0	4.6	9.1	9.1	77.3
EIB no. 22947	2008	0.0	200.0	0.0	200.0	0.0	10.5	21.1	21.1	147.4
BNDES-UNIBANCO	2016-2018	420.2	461.9	41.5	420.4	38.4	37.8	40.9	44.4	258.9
Total variable rate		**820.2**	**1,032.4**	**71.1**	**961.3**	**67.9**	**82.4**	**100.6**	**104.0**	**606.4**
TOTAL		**2,367.4**	**2,439.0**	**71.1**	**2,367.9**	**67.9**	**82.4**	**100.6**	**104.0**	**2,013.0**

Bonds are recognized at their fair value at 31 December 2006, calculated as described above. The repayment of a nominal euros 1,400.00 million provides for the settlement of euros 600.00 million at 28 October 2014 and euros 800.00 million at 28 October 2024.

All other financial indebtedness items are stated at nominal value with the related repayment plan.

The Terna Group's total loans at 31 December 2006 amount to euros 2,439.0 million, including medium/longterm loans of euros 2,367.9 million. The changes during the year include the new payables acquired on 31 March 2006 following TSN's acquisition and merger of Brazil-based Munirah Transmissora de Energia SA, which had been recognized in Munirah's financial statements. They total euros 23.0 million, broken down as follows:

- euros 21.3 million granted by BNDES on 22 April 2005 to fund the Munirah line investment project, including principal of euros 3.7 million in Brazilian real, but updated daily for changes in the real against a basket of foreign currencies (88.08% US dollar, 11.50% Japanese yen, 0.24% euro and 0.18% other currencies). Interest on this debt in Brazilian real is calculated at the TJLP rate plus a spread of 3.0%. If the TJLP exceeds 6%, interest due for that excess amount is capitalized and repaid in accordance with the repayment plan for residual debt. Interest on debt indexed to the basket of foreign currencies accrues at a variable rate based on the average cost incurred by BNDES to acquire foreign currency, plus a 3%

spread. Interest is paid at the end of each month for both loans. The principal is repayable in 144 monthly instalments from 15 April 2006;

- euros 1.7 million granted by Banco Santander on 31 March 2006, but repaid on 2 May 2006.

On 15 December 2006, Novatrans took out a new loan granted by BNP Paribas, Banco Santander and Citibank denominated in local currency and indexed to the short-term interbank rate (CDI), plus a 0.90% spread. Interest is paid and the principal is repaid in instalments at the end of the each month. This payable was used to early repay the existing payable denominated in US dollars taken out with Interamerican Development Bank (IDB).

On 13 April 2006, TSN took out a new loan with the following characteristics:

- real 50.0 million, equal to euros 19.4 million (at the exchange rate of 2.58256 ruling on 13 April 2006) granted by UNIBANCO and maturing on 13 April 2008. Interest accrues at the short-term interbank rate (CDI), plus a 0.85% spread, while principal is repaid in 24 instalments at the end of each month.

Lastly, on 17 April 2006, BNDES disbursed TSN the last instalment of a loan, amounting to euros 0.5 million.

These loans are not hedged by derivatives. Accordingly, the entire amount is exposed to risks of fluctuations in interest rates.

Guarantees given amount to approximately euros 211 million and relate to the subsidiaries TSN and Novatrans shares held by Terna Group, which have been pledged to the lending banks (BNDES Itaú, ABN, Citibank, BNP e Santander) for investments in Brazil. However, Terna Participações retains the right to vote and receive dividends.

The following table illustrates medium/long-term indebtedness, broken down by currency and average interest rate, including amounts due within one year.

In millions of euros	Maturity	Original currency	31.12.2006	Due within one year	Due after one year	Average interest rate at 31.12.06
Bonds	2014-2024	euro	1,406.6	0.0	1,406.6	4.62%
Fixed rate			**1,406.6**	**0.0**	**1,406.6**	
EIB no. 20271	2014	euro	54.6	6.8	47.8	2.93%
EIB no. 21159	2016	euro	215.9	22.7	193.2	3.03%
EIB no. 22947	2020	euro	100.0	0.0	100.0	3.07%
EIB no. 22947	2018	euro	200.0	0.0	200.0	3.70%
BNDES-UNIBANCO	2016-2018	real	461.9	41.5	420.4	11.19%
Variable rate			**1,032.4**	**71.1**	**961.3**	
TOTAL			**2,439.0**	**71.1**	**2,367.9**	

Considering the implicit rate of hedges, the average interest rate on the bonds is 3.6%. With respect to the two EIB loans, which are hedged against interest rate risk, considering the effect of cash flow hedge derivatives whose cost has been classified as current liabilities, the EIB no. 20271 loan has an average rate of 4.7%, while the EIB no. 21159 loan has an average rate of 4.4%.

The hedges in place to protect the group against the risk of fluctuations in interest rates ensure that the volatility of the cost of financial indebtedness remains limited.

The following table shows changes in medium and long/term indebtedness during the year:

In millions of euros

Type of debt	Notional debt at 31.12.05	Carrying amount at 31.12.05	Repayments and capitalizations	New issues	Exchange rate differences	Difference in fair value from 31.12.05 to 31.12.06	Notional debt at 31.12.06	Carrying amount at 31.12.06
Listed fixed rate bonds	1,400.0	1,498.4	0.0	0.0	0.0	(91.8)	1,400.0	1,406.6
Total bonds	**1,400.0**	**1,498.4**	**0.0**	**0.0**	**0.0**	**(91.8)**	**1,400.0**	**1,406.6**
Bank loans of subsidiaries	469.0	469.0	(78.0)	82.9	(12.0)		461.9	461.9
Bank loans of the parent	400.0	400.0	(29.5)	200.0	0.0	0.0	570.5	570.5
Total bank loans	**869.0**	**869.0**	**(107.5)**	**282.9**	**(12.0)**	**0.0**	**1,032.4**	**1,032.4**
TOTAL FINANCIAL INDEBTEDNESS	**2,269.0**	**2,367.4**	**(107.5)**	**282.9**	**(12.0)**	**(91.8)**	**2,432.4**	**2,439.0**

Medium and long-term indebtedness shows a euros 71.6 million increase on 31 December 2005, due to the drop in the fair value of bonds (euros 91.8 million), the repayment of EIB loans (euros 170.5 million; euros 29.5 million as a decrease in the repayment subsidiaries' loans and euros 200.00 million as an increase for new issues), the repayment of subsidiaries' loans (euros 78.0 million), the decrease due to exchange rate differences (euros 12.0 million) and the increase following the issue of new debt or the consolidation of new debt (euros 82.9 million).

At 31 December 2006, the parent has available credit lines of euros 1,569 million, including hot money of euros 819 million and the five-year revolving credit line of euros 750 million.

The latter was renegotiated on 10 April 2006, and the amount, maturity and terms were redefined. The total amount of the credit line was increased from euros 500 million to euros 750 million through the extension of portions of the banking syndicate (Banca Intesa SpA, Banca Nazionale del Lavoro SpA, Banco Bilbao Vizcaya Argentaria SA, Capitalia Gruppo Bancario, Mediobanca - Banca di Credito Finanziario SpA, Monte dei Paschi di Siena SpA, Sanpaolo IMI SpA, Unicredit Banca Mobiliare SpA Mediobanca - Banca di Credito Finanziario SpA and Banco Bilbao Vizcaya Argentaria SA are lead arrangers of this transaction). The maturity was postponed from 2009 to 2011, and Terna may request a further extension to 2013. The terms were also revised and, in particular, the importance of the rating was eliminated. Moreover, the spread on both the availed and unavailed portions of the credit were reduced from 17.5 to 15 base points and from 5.25 base points (30% of the margin of use) to 4 base points, respectively.

Furthermore, on 12 July 2006 the "Euro Medium Term Note Programme" (EMTN) was signed, for a total of euros 2 billion. The programme will enable Terna to benefit from the potential financial opportunities of international capital markets through the issue of bonds with various maturities in main world currencies.

Net financial indebtedness is detailed below:

In millions of euros	Carrying amount 31.12.2006
A) Cash on hand - Italy	15.3
B) Cash on hand - Brazil	185.1
C) Securities held for trading	0.0
D) Cash and cash equivalents (A) + (B) + (C)	**200.4**
E) Current financial receivables	**0.0**
F) Current bank debt	50.0
G) Current portion of long-term debt	71.1
H) Other current financial payables	0.0
I) Current financial indebtedness (F) + (G) + (H)	**121.1**
J) Net current financial indebtedness (I) - (E) - (D)	**-79.3**
K) Non-current bank debt	961.3
L) Bonds	1,406.6
M) Derivative financial instruments in portfolio	-5.8
N) Non-current financial indebtedness (K) + (L) + (M)	**2,362.1**
O) Net financial indebtedness (J) + (N)	**2,282.8**

There are no financial payables or receivable due from/to related parties.

The contractual clauses of loans in place at 31 December 2006 include negative pledges and default events in line with market standards (and, accordingly immaterial), while there are no financial covenants on existing debt.

Non-current financial liabilities

The table below provides the maturity and average interest rate of non-current financial liabilities:

In millions of euros	Maturity	31.12.2006	31.12.2005	Average interest rate
CFH derivatives	2014-2016	6.2	17.8	1.85%
Trading derivatives	2007-2008	-	11.2	0.36%
TOTAL		**6.2**	**29.0**	

Non-current financial liabilities include the fair value of fair cash flow hedge derivatives at 31 December 2006. Fair value is measured by discounting estimated future cash flows on the basis of the market interest rate curve at the reporting date. The fair value of cash flow hedge derivatives is recognized in the balance sheet under financial liabilities, with a balancing entry in a specific equity reserve. Accordingly, changes in the fair value of cash flow hedge derivatives have no impact on profits or losses. The rise in the interest rate curve generated a euros 11.6 million increase for cash flow hedge derivatives and euros 11.9 million change in trading derivatives, i.e. those derivatives that do not satisfy the requirements to be recognized hedging instruments and have an impact on the income statement (increase in non-current financial assets of euros 0.7 million and decrease in non-current financial liabilities of euros 11.2 million).

Short-term loans

To meet cash requirements, in December, two short-term credit lines were used for a total of euros 50 million. These credit lines were recognized when negotiated at an average interest rate of 3.81%.

Current financial liabilities

Current financial liabilities arising on financial expense accrued but not settled in relation to financial items are substantially unchanged with respect to 31 December 2005. The following table details deferred liabilities on the basis of the financial liabilities to which they relate:

In millions of euros	31.12.2006	31.12.2005	Change
Deferred liabilities on:			
Derivative contracts			
- hedging	0.2	0.6	-0.4
- trading	0.0	0.9	-0.9
Total	**0.2**	**1.5**	**-1.3**
Bonds			
- ten-year	4.5	4.5	0.0
- twenty-year	7.0	7.0	0.0
Total	**11.5**	**11.5**	**0.0**
Loans	**4.3**	**3.8**	**0.5**
TOTAL	**16.0**	**16.8**	**-0.8**

25) TERMINATION BENEFITS AND OTHER EMPLOYEE-RELATED PROVISIONS euros 166.1 million

The Terna Group offers its employees benefits during their employment with the group (e.g., loyalty bonus), upon termination of employment (e.g., termination benefits, additional month's pay and indemnity for lack of notice) and after termination of employment (e.g., electricity discount and the ASEM health plan).

Employee benefits (loyalty bonus) are due to Group employees hired under the national labour contract (including managers) upon the achievement of specific seniority requirements (25 and 35 years of service).

Termination benefits are due to all employees, managers hired or appointed before 28 February 1999 (indemnity for lack of notice), and employees (blue collars, white collars and junior managers) hired before 24 July 2001 under the national labour contract (additional month's pay).

Post-employment benefits consist of the following:

- discount on electrical energy consumed for domestic use. This benefit is offered to all Group employees hired before 30 June 1996 under the national electrical energy sector labour contract. It is referred to as the electricity discount;
- health plan in addition to national healthcare, as provided for by the national industrial labour contract for managers (ASEM health plan).

The composition of and changes in termination benefits and other employee-related provisions at 31 December 2006 are detailed below:

In millions of euros	31.12.2005	Accruals	Interest cost	Utilization and other changes	31.12.2006
Employee benefits					
Loyalty bonus	3.9	0.0	0.2	-0.1	4.0
Total	**3.9**	**0.0**	**0.2**	**-0.1**	**4.0**
Termination benefits					
Termination benefits	74.6	9.0	2.9	-1.1	85.4
Additional month's pay	9.2	0.5	0.4	-3.1	7.0
Indemnity for lack of notice and other similar benefits	2.3	0.0	0.1	1.5	3.9
Total	**86.1**	**9.5**	**3.4**	**-2.7**	**96.3**
Post-employment benefits					
electricity discount	63.0	1.1	2.5	-13.7	52.9
ASEM	15.2	0.3	0.6	-3.2	12.9
Total	**78.2**	**1.4**	**3.1**	**-16.9**	**65.8**
TOTAL	**168.2**	**10.9**	**6.7**	**-19.7**	**166.1**

This caption amounts to euros 166.1 million at 31 December 2006 (euros 168.2 million at 31 December 2005) and shows a net decrease of euros 2.1 million compared to the previous year, mainly due to the combined effect of the net accruals of termination benefits (euros 10.8 million), net utilization, transfers and other changes in the electricity discount and ASEM made by the group (euros -12.4 million).

In millions of euros	Termin. ben.	Indemnity for lack of notice	Additional month's pay	Loyalty bonus	ASEM	Electricity discount	Elec. discount substitute indemnity	Total
31.12.2005	**74.6**	**2.1**	**9.2**	**3.9**	**15.2**	**63**	**0.2**	**168.2**
Cost	9	-0.1	0.5	0	0.3	1.1	0	10.9
Interest	2.9	0.1	0.4	0.2	0.6	2.5	0	6.7
(Gains)/Losses	5.3	1.5	-2	1.4	-3.1	-11.1	0	-8
Disbursements and transfers	-10.5	-0.1	-1.1	-1.5	-0.1	-2.6	0	-15.9
Change in consolidation scope	4.0	0.2	0	0	0	0	0	4.2
31.12.2006	**85.3**	**3.7**	**7**	**4**	**12.9**	**52.9**	**0.2**	**166.1**

The main assumptions made in the actuarial estimate of employee benefit obligations are the following:

	2006	**2005**
discount rate	4.25%	4.0%
rate of increase in personnel expenses	2.0% - 4.0%	2.0% - 4.0%
rate of increase in healthcare costs	3.0%	3.0%

26) PROVISIONS FOR CONTINGENCIES AND CHARGES - euros 59.1 MILLION

The caption at 31 December 2006 and changes therein may be analyzed as follows:

In millions of euros	Provision for disputes and litigation	Provision for contingencies and other charges	Provision for leaving incentives	Total
BALANCE AT 31 DEC. 2005	**14.3**	**13.5**	**9.6**	**37.4**
Accruals	0.4	20.5	4.1	25
Utilization	-1	-3.2	-1.8	-6.0
Change in consolidation scope	-	2.7	-	2.7
BALANCE AT 31 DEC. 2006	**13.7**	**33.5**	**11.9**	**59.1**

Provision for litigation - euros 13.7 million

This provision is substantially in line with 2005. It is accrued mainly to cover year-end liabilities which could arise on lawsuits and out-of-court litigation relating to Group activities. The amount accrued takes into account the opinions of both the internal and independent lawyers. Litigation for which a positive outcome is expected and those entailing a remote, potential charge are not provided for, and nor are those for which no charge can be calculated; The latter are described under “off-balance sheet items”.

Provision for contingencies and charges - other - euros 33.5 million

With respect to 2005, the provision shows a net increase of euros 20.0 million due to the net effect of accruals (euros 20.5 million), utilization (euros 3.2 million) of the year and the contribution of the companies acquired (euros 2.7 million), including, in particular:

- euros 1.6 million for the long-term incentive plan for managers not benefiting from the stock option plan;
- euros 5.6 million for “Urban and environmental redevelopment projects” to offset the environmental impact of the construction of long distance lines;
- euros 9.8 million, reflecting the estimated cost to be incurred by the parent for additional INPS contributions;

Provision for leaving incentives - euros 11.9 million

This provision reflects the estimated non-recurring charges related to the agreed early termination of the working relationship of employees who are eligible for pension.

27) TAX LIABILITIES, INCLUDING DEFERRED - euros 454.5 million

Changes in this caption are detailed as follows:

		IMPACT RECOGNIZED IN PROFITS OR LOSSES			
In millions of euros	31.12.2005	Accruals	Utilization	Other changes	31.12.2006
Land related to buildings	3.8		-0.1		3.7
Employee benefits	0.1		-0.1	-1.7	-1.7
FVH derivatives and FV bond	1.3				1.3
Amortization and depreciation	456.9	5.7	-17.9		444.7
Difference in the fair value of former TSO properties	2				2
Change in consolidation scope	-			1.0	1.0
IRAP rate adjustment	-	3.5			3.5
Financial expenses	3.6		-3.6		-
TOTAL	**467.7**	**9.2**	**-21.7**	**-0.7**	**454.5**

Deferred tax liabilities decreased by euros 13.2 million on 31 December 2005, mainly due to the combined effect of the following events:

- utilization (euros 17.9 million) to absorb amortization/depreciation in excess of the deductible portion.
- utilization (euros 3.6 million) of the taxes accrued on financial expenses following the repayment of the EDB loan by Novatrans;

- accruals made by the parent (euros 5.7 million) mainly related to amortization/depreciation in addition to the rates of the year;
- adjustment (euros 3.5 million) of the IRAP rate (from 4.43% in 2005 to 4.72%) applied to provisions for deferred taxation, to better reflect the rates that will be applicable when the related temporary differences reverse.

28) OTHER NON-CURRENT LIABILITIES - euros 170.8 million

This caption, which is substantially in line with the balance at 31 December 2005 (euros 176.2 million), includes deferrals of grants related to plants (euros 156.4 million) and deferred portions of the parent's grid transmission consideration to cover future costs of the National Transmission Grid safety plan (euros 14.4 million). The decrease on 2005 (euros 5.4 million) is mainly due to the release of portions of grants in connection with the depreciation of the year applicable to plants.

29) CURRENT LIABILITIES

Current liabilities at 31 December 2006 are detailed as follows:

In millions of euros	31.12.2006	31.12.2005	Change
Short-term loans (*)	50.0	55.0	-5.0
Current portion of long-term loans (*)	71.1	58.3	12.8
Trade payables	1,280.6	951.4	329.2
Tax liabilities	75.3	14.4	60.9
Current financial liabilities (*)	16.0	16.8	-0.8
Other current liabilities	112.8	104.9	7.9
TOTAL	**1,605.8**	**1,200.8**	**405.0**

(*) Reference should be made to the comments in note 24) LOANS.

Trade payables - euros 1,280.6 million

Trade payables at 31 December 2006 are detailed as follows:

In millions of euros	31.12.2006	31.12.2005	Change
Suppliers			
Suppliers:			
- non-energy related payables	228.4	200.9	27.5
- energy-related payables	1,046.9	747.2	299.7
Associates - Cesi	4.4	2.7	1.7
Payables for contract work in progress			
Payables for contract work in progress	0.9	0.6	0.3
TOTAL	**1,280.6**	**951.4**	**329.2**

SUPPLIERS

Non-energy related payables

Amounts due to suppliers relate to invoices received and to be received for tenders, services and the purchase of materials and equipment.

The increase on 2005 (euros 27.5 million) is due to greater purchases and services in the last few months of the year as part of ordinary investing activities and operations, and the payables of the subsidiaries RTM1 and RTM2 (euros 5 million) which were not included in the consolidation scope of the Terna Group in 2005. The caption also includes amounts due for services provided to Enel Group companies (euros 28.7 million), which mainly comprise the following amounts:

euros 4.1 million due to Enel Distribuzione for invoices to be received for the electricity discount (discount on energy consumed for domestic use, which is given to all Group employees hired before 30 June 1996 under the national electricity sector labour contract);

euros 24.0 million due to Enel Servizi for personnel administration, IT services, canteen services and security.

Energy-related payables

This caption includes the effects of amounts due for energy in transit on the balance sheet, mainly in connection with the purchase of energy and the transmission consideration due to the owners of other portions of the National Transmission Grid. The increase (euros 299.7 million) on 2005 is mainly due to the operations of the TSO business activity for the last two months of 2005 only, and deferred payables relating to capacity payments (euros 84 million), UESS - basic units (euros 29.8 million), interconnection (euros 18.6 million), CCT returns (euros 59.1 million) whose allocation and/or coverage is yet to be defined by AEEG.

Associates

This caption, which amounts to euros 4.4 million, refers to amounts due to Cesi for services provided to the parent in relation to the construction and management of laboratories and plants for tests, inspections, studies and experimental research relating to the general electro-technical field and its technical and scientific progress. The euros 1.7 million increase on 31 December 2005 is due to the greater services rendered in the last few months of the year.

Commitments with suppliers for the 2007-2012 period amount to euros 1,140.5 million and relate to the as yet unpurchased portions of contractual purchase commitments pending at year end, which do not fall under normal operations.

PAYABLES FOR CONTRACT WORK IN PROGRESS

This caption amounts to euros 0.9 million at 31 December 2006, in line with 31 December 2005 and is composed as follows:

In millions of euros	Payments on account	Contract value	Balance at 31.12.2006	Payments on account	Contract value	Balance at 31.12.2005
Other	(2.8)	1.9	(0.9)	(5.3)	4.7	(0.6)
TOTAL	**(2.8)**	**1.9**	**(0.9)**	**(5.3)**	**4.7**	**(0.6)**

Tax liabilities - euros 75.3 million

The caption includes the group payable for taxes of the year. In particular, it relates to:

- the parent (euros 72.3 million, of which euros 62.5 million relate to IRES and euros 9.8 million to IRAP);
- the RTL Group (euros 3.0 million), in particular RTM1 (euros 2.0 million) and RTM2 (euros 1.0 million); conversely, RTL offset the income tax payable of the year against the tax credits arising from the 2005 IRES and IRAP advances.

Other current liabilities - euros 112.8 million

Other current liabilities are detailed below:

In millions of euros	31.12.2006	Due within one year	Due after one year	31.12.2005	Change
Payments on account	19.7	0.7	19.0	25.2	-5.5
Other tax liabilities	48.4	48.4	-	14.4	34.0
Amounts payable to social security institutions	12.6	12.6	-	11.7	0.9
Amounts payable to employees	26.0	26.0	-	21.9	4.1
Other	6.1	3.8	2.3	31.7	-25.6
TOTAL	**112.8**	**91.5**	**21.3**	**104.9**	**7.9**

PAYMENTS ON ACCOUNT

This caption, which amounts to euros 19.7 million, includes grants related to plants collected by the parent for non-current assets still under construction at 31 December 2006.

The net decrease of euros 5.5 million on 2005 (euros 25.2 million) is mainly due to the effect of the new contributions received from third parties for connections to the National Transmission Grid (euros 15.0 million) and the decrease (euros 20.5 million) in the contributions which directly reduce the carrying amount of the related assets, which became operational during the year.

OTHER TAX LIABILITIES

Other tax liabilities, which amount to euros 48.4 million, include euros 43.8 million in relation to the parent, mainly for the settlement of VAT in December (euros 35.5 million), substitute tax withholdings (euros 5.5 million) and registry tax on the agreement for the acquisition of the TSO business activity (euros 2.8 million).

The residual euros 4.6 million relates to the following:

the RTL Group, for the VAT payable (euros 1.1 million) and the withholdings on employees' remuneration (euros 0.2 million);

the Brazilian subsidiaries, for local taxes and withholdings (euros 3.3 million).

The significant increase (euros 34.0 million) is mainly due to the parent which, in 2005, had a lower balance of sums payable to taxation authorities. Indeed, in the last VAT settlement, it was in a credit position.

AMOUNTS PAYABLE TO SOCIAL SECURITY INSTITUTIONS

Amounts payable to social security institutions amount to euros 12.6 million (euros 11.7 million at 31 December 2005) and mainly relate to the parent's amounts payable to INPS for December 2006 and settled in January 2007;

The caption also includes the contributions of the year relating to employees' incentives, to be paid in the following year, and the portion of the contributions arising from the renewal of employees' labour contract which was signed in July 2006.

AMOUNTS PAYABLE TO EMPLOYEES

Amounts payable to employees amount to euros 26.0 million (euros 21.9 million at 31 December 2005) and mainly relate to termination benefits due from the parent to employees whose employment was terminated before 31 December 2006 (euros 8.2 million), amounts due for employees' leaving incentives to be paid in 2007 (euros 9.9 million) and vacation and holidays accrued but not taken, to be paid in January (euros 6.4 million for the parent and euros 0.8 million for subsidiaries).

OTHER

Other payables of euros 6.1 million (euros 31.7 million at 31 December 2005) mainly relate to the parent and may be analyzed as follows:

- euros 2.3 million for guarantee deposits made in connection with the contractual obligations undertaken by electricity market operators with respect to dispatching contracts;
- euros 1.3 million for the amount due to ACEA SpA, being mainly the portion of the incentive to unify the National Transmission Grid following the sale of the grid to the parent (AEEG Resolution no. 73/06);
- euros 2.1 million for deferred liabilities of a sundry nature;

the euros 25.6 million decrease on 31 December 2005 is mainly due to the reclassification of the parent's energy items (euros 23.5 million), which arose in 2005 in conjunction with the acquisition of the TSO business activity, to "Trade payables".

E) COMMITMENTS AND CONTINGENCIES ARISING FROM OFF-BALANCE SHEET ITEMS

Environmental litigation

Environmental litigation relates to the installation and operating of electrical systems and, in particular, the effects of electric and magnetic fields.

The parent was summoned in various civil and administrative cases in which requests were made for the transfer or change in operations of allegedly damaging electrical lines, even if installed in full compliance with current legislation to this regard. Only a very small number of cases include claims for compensation for damage to health due to electromagnetic fields.

The Prime Minister's Decree of 8 July 2003, which completed outline Law no. 36 of 22 February 2001, established the amounts of the three parameters (exposure limits, warning values and quality standards), provided for by the law, with which electrical systems must comply. This decree had a favourable impact on the pending litigation, as until then, the scope of the outline law had been limited to general principles only. In terms of the decisions taken to this regard, in only a few rare cases were judgments passed against the parent. Moreover, these were appealed and the appeals are still pending. However, no claims of compensation for damage to health have been upheld.

Electric and magnetic field legislation

The outline Law, passed on 22 February 2001, gives the government responsibility for establishing the relevant parameters (exposure limits, warning values and quality standards) with which plants must comply under specific measures.

To this end, the outline law regarding reclamation provides for a recovery mechanism for reclamation costs, calculated by the Electricity and Gas Regulator pursuant to Law no. 481/95, as these are expenses incurred in the public's interest.

On 29 August 2003, the Prime Minister's Decree of 8 July 2003 for the "Establishment of exposure limits, warning values and quality standards for the protection of the population from electric and magnetic fields at the grid frequency (50 Hz) used by long distance power lines", was published in the Official Journal of the Italian Republic. It established the amounts of the three parameters provided for by the outline law. In terms of regional regulations, certain regions have proposed laws concerning this issue, with more

restrictive limits than those provided for by the Prime Minister's Decree of 1992, and the more recent Decree of 8 July 2003.
However, under Judgement no. 307 of the Constitutional Court, passed down on 7 October 2003, certain regional laws regarding electromagnetic fields are anti-constitutional (including the Campania Region's Law no. 13 of 24 November 2001), on the basis of the principle that the limits established by the Government legislation cannot be waived, not even by regional legislation, as the protection of health must be ensured consistently throughout Italy.

GSE (formerly GRTN) business activity litigation

With respect to the litigation over events that occurred up to the date of transfer in relation to the GSE business activity responsible for energy transmission and dispatching activities ("business activity"), under the provisions of Article 1 of the Prime Minister's Decree of 11 May 2004, and the transfer agreement signed by Terna and GSE on 28 February 2005, the litigation was not transferred. Accordingly, GSE retains all liability, charges or liabilities to be incurred as a result or in connection with the litigation. Moreover, the parent has referred to these provisions in litigation in which it is involved and has requested the former GRTN (now GSE SpA) to hold it harmless from any charges.
As it holds the concession for transmission and dispatching activities since 1 November 2005, Terna was summoned in certain cases appealing AEEG's and/or MAP's measures relating to the above issue. Only in those cases in which the plaintiffs claim not only defects in the measures, but also Terna's alleged violation of the rules established by such Authorities, is the parent company called to appear in court.

Other litigation

In addition, cases relating to urban planning and environmental issues are pending, following the construction and operating of certain transmission lines. Any unfavourable outcome to these cases could have adverse effects for the group, which cannot be foreseen to date. Accordingly, no accruals have been made in this respect.
The outcome of a limited number of cases cannot be forecast as undoubtedly positive for the parent, and the possible consequences could consist of compensation for damage, as well as incurring, *inter alia*, charges to change lines and suspend their use temporarily. In any case, any unfavourable outcome would not jeopardise line operations.

The above litigation has been examined, also considering the opinion of independent legal experts, and any negative outcome is considered remote.

INPS Memorandum no. 63 of 6 May 2005 provided that, with retroactive effect from 1999, government industrial companies and public bodies carrying out industrial, privatised activities, owed contributions to CIG, CIGS and DS, as well as amounts payable for redundancy, entailing charges of approximately euros 24.8 million.

Given the complexity of this issue, Terna, along with other companies operating in the electrical energy sector, initially took legal recourse before an administrative law judge, claiming the measure be suspended and declared null and void. The judge claimed it was not that court’s jurisdiction, since the issue concerned solely subjective rights. To date, Terna has taken its claims before the ordinary judicial authorities to claim that it has no obligation to pay the contributions. The hearing was set for 24 April 2007. However, INPS considered it necessary to request an opinion from the Council of State, and suspended payment of these contributions until it obtained such opinion. On 8 February 2006, the Council of State found that the contributions should not be applied retroactively, and that the Memorandum should be duly integrated and corrected.

F) BUSINESS COMBINATIONS

Acquisition of Terna Participações

On 13 March 2006, the parent Terna SpA acquired the entire share capital of Brazil-based Donnery Holdings SA (real 100) for approximately real 25 thousand (roughly euros 10 thousand). The company was originally set up in São Paulo on 23 January 2006. The new shareholders then decided to change the company’s name to Terna Participações SA. The purpose of Terna Participações SA is to hold investments in other Brazilian and foreign companies operating in the electrical energy transmission sector.

Acquisition and merger of Munirah

On 31 March 2006, TSN finalized the acquisition of 100% of Munirah Transmissora de Energia SA ("Munirah") from Control Y Montajes Industriales CYMI SA and Fluxo Engenharia Ltda.

The acquisition, which was governed by a purchase and sale agreement signed on 15 December 2005, was finalized once ANEEL and the financing bank BNDES had given their approval.

Munirah holds concessions on 106 km of transmission lines and two bays in two substations (owned by TSN and Chesf) in Bahia, and makes up the extension of the 500-kV lines owned by TSN that close the North-Northeast circuit.

This transaction will enable Terna to consolidate its presence in Brazil by giving it control over a strategic line in terms of geographical position and proximity to TSN's assets.

At the same time of the acquisition, Munirah was merged into TSN, to streamline the investment structure and optimize administrative expenses.

The table below provides figures recognized at the acquisition date (31 March 2006), reflecting the assets and liabilities of the company, measured at fair value at that date, which corresponds to the IFRS balances recognized immediately after the business combination. The euros 3 million difference between the price paid to acquire Munirah, real 48 million (approximately euros 18 million), and the fair value of assets acquired and liabilities assumed and incurred, amounting to approximately euros 15 million, has been allocated to goodwill arising on the merger.

Brazilian real/million	
Property, plant and equipment	97.4
Intangible assets	0.1
Inventories	3.5
Trade and other receivables	2.0
Cash and cash equivalents	0.9
Financial liabilities	61.0
Tax liabilities	0.8
Trade and other payables	1.0
Net identifiable assets and liabilities	**41.1**
Goodwill	7.4
Consideration	**48.5**
Cash and cash equivalents	-0.9
NET CASH OUTFLOWS	**47.6**

Acquisition of Rete Trasmissione Milano 1

On 24 November 2006, RTL SpA acquired 100% of RTM1 - Rete Trasmissione Milano1 from Edison SpA. The consideration paid amounted to approximately euros 304 million, net of the incentives provided for by the Electricity and Gas Regulator (Resolution no. 73/06).

In accordance with the provisions of Law no. 290/2003 and the subsequent Prime Minister's Decree of 11 May 2004 concerning the unification process of the domestic transmission grid under Terna SpA, the latter provided RTL with the funding necessary to acquire this investment, through a capital injection equal to the investment's cost. In addition, it financed RTL through the intercompany current account for an amount equal to the costs directly related to the acquisition.

RTM1 owns 2,763 km of high-voltage electrical energy transmission lines and 29 electrical substations scattered throughout Northern Italy. It also manages two control centers.

The table below provides the amount recognized at the acquisition date, reflecting the company's assets and liabilities, measured at fair value at that date, and the IFRS balances recognized immediately after the business combination. The euros 11.9 million difference between the price paid to acquire RTM1, approximately euros 287 million, and the fair value of assets acquired and liabilities assumed and incurred, amounting to approximately euros 275 million, has been allocated to goodwill arising on the merger. This amount was allocated on the basis of the provisional values of a specific appraisal under completion by independent experts.

In millions of euros	IFRS carrying amounts before the business combination	Fair value
RTM1		
Property, plant and equipment	191.6	291.8
Inventories	1.2	1.2
Trade and other receivables	16.7	16.7
Cash and cash equivalents	0.1	0.1
Provisions for contingencies and charges	1.5	1.5
Termination benefits	3.3	3.3
Trade and other payables	29.7	29.7
Net identifiable assets and liabilities	**175.1**	**275.3**
Goodwill		11.9
Acquisition price		287.2
Consideration (including acquisition costs)		293.9
Incentive as per Resolution no. 73/06		-6.7
Acquisition price		287.2
Intercompany payable recognized		17.3
NET CASH OUTFLOWS		**304.5**

Acquisition of Rete Trasmissione Milano 2

On 24 November 2006, RTL SpA acquired 99.99% of RTM2 - Rete Trasmissione Milano2 from AEM SpA. The consideration paid amounted to approximately euros 121 million, net of the incentives provided for by the Electricity and Gas Regulator (Resolution no. 73/06).

In accordance with the provisions of Law no. 290/2003 and the subsequent Prime Minister's Decree of 11 May 2004 concerning the unification process of the domestic transmission grid under Terna SpA, the latter provided RTL with the funding necessary to acquire this investment, through a capital injection equal to the investment's cost. In addition, it financed RTL through the intercompany current account for an amount equal to the costs directly related to the acquisition.

RTM2 owns 1,095 km of high-voltage electrical energy transmission lines and 12 electrical substations scattered throughout Northern Italy. It also manages two control centers.

The table below provides the amount recognized at the acquisition date, reflecting the company's assets and liabilities, measured at fair value at that date. The euros 25.9 million difference between the price paid to acquire RTM2, approximately euros 121 million, and the fair value of assets acquired and liabilities assumed, amounting to approximately euros 95 million, has been allocated to goodwill arising on the merger. This amount was allocated on the basis of the provisional values of a specific appraisal under completion by independent experts.

In millions of euros	IFRS CARRYING AMOUNTS BEFORE THE BUSINESS COMBINATION	FAIR VALUE
RTM2		
Property, plant and equipment	78	88.2
Trade and other receivables	9.7	9.7
Cash and cash equivalents	3.6	3.6
Provisions for contingencies and charges	2.2	2.2
Termination benefits	0.8	0.8
Trade and other payables	3.7	3.7
Net identifiable assets and liabilities	**84.6**	**94.8**
Goodwill		25.9
Acquisition price		120.7
Consideration (including acquisition costs)		123.1
Incentive as per Resolution no. 73/06		-2.4
NET CASH OUTFLOWS		**120.7**

G) RELATED PARTY TRANSACTIONS

Related parties are identified in accordance with the provisions of IAS 24.

A party is related to the company if:

(a) it directly or indirectly, through one or more intermediaries:

- (I) controls the company, is controlled by the company, or is jointly controlled thereby (including parents, subsidiaries and associates);
- (II) it holds an investment in the company that gives it significant influence over that company;
- (III) it jointly controls the company;

(b) the party is an associate of the company;

(c) the party is a joint venture in which the company is an investor;

(d) the party is a member of senior management with strategic duties of the company or its parent;

(e) the party is a close relative of one of the parties described in letters (a) or (d);

(f) the party is controlled, jointly controlled or under the significant influence of one of the parties described in letters (d) or (e), or those parties directly or indirectly hold a significant portion of voting shares;

(g) the party is a pension fund for the employees of the company, or any of its related parties.

A related party transaction occurs when there is a transfer of resources, services or obligations between related parties, regardless of whether a consideration is agreed.

Related party transactions carried out by the Terna Group during the year essentially included those with the associate Cesi SpA and the group's employee pension funds FONDENEL and FOPEN.

In particular, agreements with Cesi SpA in which Terna is the customer mainly relate to services and technical consultancy, studies and research, design and trials carried out on behalf of Terna. Other agreements mainly relate to the lease of laboratories and other similar structures for specific use.

FONDENEL and FOPEN are pension funds in which the group's employees participate for complementary pensions. The related transactions with an impact on the group's balance sheet and income statement involve contributions incurred by the Terna Group, which are calculated and paid on a monthly basis.

	INCOME STATEMENT FIGURES			BALANCE SHEET FIGURES		
In millions of euros	Revenues	Costs	Investments	Receivables	Payables	Guarantees
Cesi SpA	0.1	0.9	7.6	-	4.5	2.0
Fondenel	-	0.4	-	-	-	-
Fopen	-	1.3	-	-	0.7	-
TOTAL	**0.1**	**2.6**	**7.6**	**-**	**5.2**	**2.0**

The guarantees relate to sureties received on contracts in which Terna is the customer.

H) SIGNIFICANT NON-RECURRING TRANSACTIONS AND EVENTS AND ATYPICAL OR UNUSUAL TRANSACTIONS

With the exception of that discussed above, there were no atypical or unusual transactions during 2006.

I) NOTES TO THE CONSOLIDATED CASH FLOW STATEMENT

Cash flows generated by operating activities during the year amount to approximately euros 769.0 million, including roughly 940.3 million from operating activities before changes in net working capital and outflows of roughly euros171.3 million to fund the change in working capital.

Investing activities also used net financial resources of approximately euros 676.1 million. In particular, the acquisition of AEM Trasmissione SpA (RTM2) and Edison Rete SpA (RTM1) through the subsidiary RTL and the acquisition of Munirah through the subsidiary TSN generated an increase in property, plant and equipment of euros 416.7 million, with the recognition of goodwill totalling euros 40.4 million. On the other hand, the IPO of the Brazilian subsidiary Terna Participaçoes on the São Paulo stock exchange generated net proceeds of euros 115.3 million for the group, as a result of the combined effect of the following factors:

- Terna SpA’s collection of euros 82.7 million, corresponding to the list price of Terna Part shares sold on the OTC market for euros 93.9 million, net of local taxes and fees incurred for the transaction (euros 11.2 million);
- the increase in the nominal value of shares held by Terna SpA (euros 32.7 million) following Terna Participações SA’s total share capital increase (share premium) subscribed by other investors on the primary market.

Cash outflows for self-financing were mainly due to the distribution of dividends in 2005 (euros 160 million) and the interim dividend for 2006 (euros 106 million), while medium/long-term financial indebtedness, net of the related fair value hedges, increased approximately euros 178.4 million. Moreover, 34% of equity was attributed to minority interests following the subscription of that percentage of Terna Participações share capital by other investors.

Cash flows generated by these transactions amounted to approximately euros 123.8 million.

L) SUBSEQUENT EVENTS

2007-2011 business plan

On 31 January 2007, Terna presented financial analysts with its 2007-2011 business plan, approved by the company's Board of Directors.

The Terna Group's 2007-2011 business plan focuses on three main guidelines:

- Development of the domestic transmission grid (RTN): the investment plan provides for total expenditure of euros 2.7 billion from 2007 to 2011, with a 35% increase on the previous plan. Development investments account for 80% of total investments, up from euros 1.4 billion to euros 2.2 billion.
- Cost cutting with an increase in profits margins: in particular, by rationalizing costs for regulated activities in Italy. The plan provides for a reduction of approximately euros 60 million in total Terna Group costs in the years covered on a like-for-like basis.
- Guaranteed high safety of the electrical system and reliability of the domestic transmission grid with average service interruption times of less than 1 minute/year and grid availability of over 99%.

Credit rating confirmation

On 31 January 2007, Standard & Poor's Ratings Services confirmed its ratings for Terna SpA, following the Italian utility company's presentation of its 2007-2011 business plan: long-term rating of AA- and short-term rating of 'A-1+ with a stable outlook.

New dispatching and conduction organization

The new organizational structure for the Dispatching and Conduction Department was implemented on 1 March 2007, to complement the work performed on processes following the acquisition of the GRTN business activity. This new structure enables process-based management, while ensuring that operating and strategic objectives are aligned, preventing the scattering of similar activities within the same process to more than one unit. In addition, a portion of the resources formerly under the Systems and Technology Department (which is now the Technology and Management Systems Department), has come under the Technologies and Process Systems Function reporting to the Dispatching and Conduction Department.
Similarly, work groups have begun identifying further measures to take to optimize in detail the processes related to real time management.

Fibre optics

On 4 April 2007, an agreement was signed with the Wind Telecomunicazioni Group to acquire the exclusive right to use optical fibre pairs owned by the Wind Group for 20 years. The pairs run for a total length of approximately 11,000 km throughout all of Italy.
The agreement amounts to euros 43.5 million.

The data transmission infrastructure is a crucial element of the security and efficiency of control, conduction and protection processes for the high voltage grid, as it makes it possible to improve grid supervision and carry out work on Terna plants, while allowing the development of advanced solutions to protect the electricity system.
This transaction will enable Terna to further boost the safety of the system and is included in the investments provided for by the 2007-2011 business plan.

Merger of RTM1 and RTM2 into RTL

On 18 April 2007, the shareholders of Rete di Trasmissione Locale Società per Azioni (RTL), “Rete Trasmissione Milano 1 Società per Azioni” (RTM1) and “Rete Trasmissione Milano 2 Società per Azioni” (RTM2) met and approved the plan for the merger of RTM1 and RTM2 into RTL, on the basis of the companies’ financial statements as of and for the year ended 31 December 2006, with the cancellation of all shares of RTM1 and RTM2, in accordance with the methods set out in the plan and, accordingly, without RTL increasing its share capital or provided for a share exchange ratio or cash consideration.
The merger will take effect from the date of registration of the merger deed with the company registrar, or a subsequent date indicated in the merger deed.
Pursuant to point 6), Article 2501-*ter* of the Italian Civil Code, referred to by Article 2504 *bis* of the Italian Civil Code and paragraph 9, Article 172 of Presidential Decree no. 917 of 22 December 1986, the transactions carried out by the companies to be merged will be recognized in the financial statements of the merging company and the merger will take effect for accounting and tax purposes from midnight on the first day of the year in which the merger takes effect.
In particular, the purpose of the transaction is to improve the Terna Group companies’ operations, by expanding synergies through a Group reorganization in order to streamline the investment chain and pursue increased management efficiency, while reducing administrative costs. To this end, all companies in the same sector will be merged together.

Acquisition of AEM Trasporto Energia Srl Torino

On 20 April 2007, through RTL, the Terna Group signed an agreement with Iride Energia to acquire 100% of AEM Trasporto Energia Srl (“AEM TE”) and the 220-kV electrical substation in Moncalieri (Turin), which is part of the domestic transmission grid (“RTN”).

The consideration totalled euros 49.4 million, including euros 38.8 million to acquire the 100% investment in AEM TE, euros 2.8 million for the company’s net financial position at 31 December 2006 and euros 10.6 million to acquire the Moncalieri (Turin) substation. The acquisition agreement provides for an adjustment to the consideration in relation to the change in AEM TE’s equity between 31 December 2006 and the date the transaction is concluded.

AEM TE owns approximately 220 km of triads and four electrical substations in Piedmont, which are part of the domestic transmission grid (Martinetto, Rosone, Sud Ovest and Villa).

At 31 December 2006, AEM TE reported revenues of euros 7.6 million, EBITDA of euros 4.3 million and profits for the year of euros 1.7 million. Net invested capital amounted to approximately euros 25.7 million, including property, plant and equipment totalling roughly euros 27.1 million. Equity amounted to around euros 28.6 million.
The transaction is subject to authorization from the Anti-Trust Authority before it can be concluded.

Control of Terna SpA by Cassa Depositi e Prestiti

On 19 April 2007, Cassa Depositi e Prestiti SpA, which owns 29.99% of Terna SpA, notified the company that it had verified that it controlled Terna SpA. This assessment was based on the following elements:
- the composition and breakdown of the shareholding structure;
- events at particularly significant shareholders' meetings;
- the composition of the Board of Directors.

REPORTS

REPORT OF THE BOARD OF STATUTORY AUDITORS ON TERNA SPA'S CONSOLIDATED FINANCIAL STATEMENT AS OF DECEMBER 31, 2006

To the Shareholders' Meeting of TERNA SpA,

TERNA's consolidated financial statement as of December 31, 2006 was drawn up by the Parent Company TERNA SpA ("Company", "TERNA", "Parent Company"), according to the international accounting principles (IAS/IFRS) and comprises the Balance Sheet, the Income Statement, the Summary Statement, the Notes to the Financial Statement and the Statement of Cash Flows; it is also supplemented by the Director's Report. In particular, with reference to the Notes to the Financial Statement, the following is pointed out:

- the area of consolidation extends to the equity investments in which the Parent Company applies, directly or indirectly, financial and operational policies in order to obtain benefits deriving from its activities. This area, with respect to the previous year, shows a variation deriving from the acquisition of equity investment in RTM1 S.p.A. and RTM2 S.p.A. as well as a reduction of the shares held in the Brazilian companies TSN S.A. and Novatrans Energia S.A. following the listing of the holding Terna Participações in the domestic stock market;
- the criteria adopted for consolidation is the integral one and consolidation has determined a positive difference classified as Goodwill.

In particular, the impairment test gave rise to a recoverable value of the above-mentioned Goodwill which exceeded its book value.

Furthermore, the Notes to the Financial Statement, provide a clear account of the policies used in drawing up the financial statement, the accounting principles selected and applied, the nature and the economic and financial results of the transactions with related parties.

TERNA Group's consolidated financial statement indicates the balance-sheet format selected among those specified in the IAS 1.

Specifically, the Balance Sheet was drawn up according to the classification of assets and liabilities as current and non-current, the Income Statement was classified on the basis of the nature of costs, while the Statement of Cash Flows was indicated using the indirect method.

Moreover, 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 IAS 1 international standard.

As a consequence of indications received and of the assessments carried out, the consolidated financial statement, as far as its formation and structure are concerned, appears to be in compliance with the international accounting standards which were correctly applied.

We would also like to point out the following:

- the correspondence of the Consolidated Financial Statement to facts and information that we are aware of, following the fulfilment of our duties;
- the Director's Report of the Terna Group is complete, pursuant to Article 2428 of the Civil Code.

To conclude, in view of the above and also considering the results of the activity carried out by the Independent Auditors KPMG S.p.A., no significant facts have emerged worthy to be mentioned in this Report.

Rome, May 7, 2007

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 consolidated financial statements of the TERNA Group as at and for the year ended 31 December 2006, comprising the income statement, balance sheet, statement of changes in equity, statement of recognised income and expense, cash flow statement and notes thereto. These financial statements are the responsibility of the parent's directors. 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 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 directors. We believe that our audit provides a reasonable basis for our opinion.

Reference should be made to the report dated 11 April 2006 for our opinion on the prior year consolidated financial statements, which included the prior year figures presented for comparative purposes.

3 In our opinion, the consolidated financial statements of the TERNA Group as at and for the year ended 31 December 2006 comply with the International Financial Reporting Standards endorsed by the European Union and the Italian regulations implementing article 9 of Legislative decree no. 38 of 28 February 2005. Therefore, they are clearly stated and give a true and fair view of the financial position of the TERNA Group as at 31 December 2006, the results of its operations, changes in its equity and its cash flows for the year then ended.

Rome, 7 May 2007

KPMG S.p.A.

(Signed on the original)

Bruno Mastrangelo
Director of Audit

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 grids
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 recognized 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 S.p.A.

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OUR FUTURE

INCREASING THE SERVICE'S EFFICIENCY AND THE COMPANY'S COMPETITIVENESS.
ALWAYS ENHANCING THE KNOWLEDGE AND EXPERIENCE OF COLLABORATORS.
PLACING ENVIRONMENTAL RESPECT AS A TOP PRIORITY.
DEVELOPING AN INTERNATIONAL COMPANY.

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